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A CRITICAL EXAMINATION ON THE LEVEL OF PENETRATION AND PERFORMANCE OF THE PRIVATE SECTOR INSURANCE ENTITIES

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ABSTRACT

The economic reform process which was initiated in India in the year 1991 aimed at removing the control on the manufacturing and service industries so as to allow them a scope to grow. As a result of this process the insurance sector was opened up to the private players with an expectation to attain international standards. Entry of private players in the insurance sector was expected to bring gradual upgradation in the performance of this sector in the country. In the last decade the insurance industry experienced functioning in a liberalised environment and has witnessed dynamic changes in the sector such as large number of foreign players in joint ventures with Indian corporate, various forms of intermediary channels, product innovation. Now that more than a decade has passed since the advent of the private players and the entry has resulted in new risk parameters so as to suit the needs of the customers as well as to face international exposure. The present paper is an attempt to look back and study how the private sector non-life insurers who emerged out as a result of the recent privatization of the general insurance sector are playing out in the market.

INTRODUCTION

The reforms and developments in the Indian insurance sector reveals a 360-degree turn witnessed over a period of almost 200 years from private sector to a nationalised sector and back to private sector. Insurance industry witnessed dramatic changes in the year 2000 when the monopoly of public sector insurers came to an end and doors of the insurance market were opened for the entry of private sector insurers. As a result of the economic reforms undertaken by the government in early nineties reforms were undertaken in many sectors as banking, insurance etc. The fact that the success of every modern economy depends on the performance of its insurance industry cannot be denied and so it was felt to open up this industry and loosen the tight controls. The necessity to privatise were to narrow the wide gap in terms of market potential and its exploitation by the nationalized industry secondly, absence of competition has left the consumer at a loser’s position as the choice available to them was limited, absence of competitive pricing, inadequate and restricted services offered by the insurers and inadequacy to tap the available market. So it was felt in 1990s these objectives can be accomplished by introducing competition. As such reforms were initiated in this sector by inducting private players into the market so as to meet the growing needs of insurance.

The opening of the insurance sector for private participation naturally raised issues relating to solvency margins of the insurance companies, fair treatment to the insured etc. These issues are addressed by the Regulations framed by the Insurance Regulatory and Development Authority (IRDA). The former issue is addressed by stipulating a high level of capital requirement for entry into this sector by the entities and maintenance of mandatory solvency requirements, while the latter is covered by the regulations put in place for protection of policyholder interests by the IRDA from time to time. The high initial capital requirements and the 26% cap on Foreign Direct Investment stood as an obstacle to some extent in the collaboration of the Indian enterprises and the major foreign insurance companies to form the Indian Insurance companies. Thus, as on date, 23 non-life insurance companies in the private sector are operating in the country in collaboration with established foreign insurance companies from across the globe.

STATEMENT OF THE PROBLEM

So, the primary idea behind opening up of the insurance sector for private participation was to expand the coverage and spread awareness about insurance, the interests of the consumers would be better served if there is competition among the insurers. It was also recognized that the country has a vast potential waiting to be tapped and this can be done only when we have a large number of companies spreading their wings across the country and offering a variety of products catering to the demands of different sections of the population. It was also felt that competition would generate a healthy attitude towards redressal of consumer grievances and improve the quality of service. We have fourteen years of experience of public and private sector operating together and it is, perhaps, time to see whether the expectations are fulfilled. So, the present study is an attempt to analyse the performance of the private sector enterprises in fulfilling the objectives of privatisation of the industry.

1. OBJECTIVES OF THE STUDY

The present study has been undertaken with the following objectives in mind.

Objectives:

1. To evaluate the extent of penetration of and outreach so far achieved by private sector entities in India during the study period from 2001-02 to 2012-13.
2. To examine the overall performance of private sector entities in India during the study period 2001-02 to 2012-13.
3. To highlight the constraints those are encountered in achieving the target.
4. To make a comparative analysis of the four public sector insurers with other private sector insurers with respect to solvency ratio.

RESEARCH METHODOLOGY

The research design is descriptive in nature.

Scope of the study

The scope of the present study is confined to the following:

a. Academic Scope

   The Academic scope of the study is confined only to the private sector insurance companies undertaking risk coverage in respect of non-life insurance products.

b. Geographical Scope

   The study gives a wide coverage of performance of private sector insurance companies undertaking non-life risk for the whole of the country.

c. Analytical Scope

   The analytical scope is confined only to secondary information based on IRDA reports, IRDA Journals etc.

Tools of measuring performance and penetration

The following tools of measuring performance and penetration have been selected for the purpose of study.

a. Number of New Policies issued

b. Premium Underwritten in India

c. Investment Income

d. Underwriting performance (Profit/Losses)

Source of Data collection

The nature of data collected and used for the research are mainly secondary in nature. The relevant and required data are collected from the secondary sources such as Annual Reports of IRDA for various years, reports and national and international journals.

Sources of Primary information:

However primary data were also collected in order to establish veracity with the secondary information. For this purpose personal queries were conducted upon executives, officials of the insurance companies at regional and branch level, besides select numbers of policyholders were also interviewed in order to elicit their responses towards private sector insurers.
Convenient sampling on selective basis has been followed for the study which is based on purposive sampling.

Periodicity of the study

The periodicity of the present study is 2002-03 to 2012-13 i.e. eleven years. Justification for selecting the periodicity being the insurance sector witnessed the entry of private entities in 2001 and opened up for foreign investors. Private sector insurers started registering in 2000 but were unable to commence full scale business operations till March, 2001. Therefore, the study covers the period from 2002-2003 i.e. after one complete year of functioning of private entities in insurance sector till date.

Statistical tools employed

The statistical tools used for the purpose of analysis are the percentage and ratios.

The information/data collected have been classified, tabulated and analysed as per the requirements to fulfill the aforesaid objectives.

CONCEPTUAL FRAMEWORK

a) FDI in insurance – foreign companies can operate in the insurance sector only by forming a joint venture with an Indian company and the maximum holding of foreign investor is restricted to 26%.

b) Premium underwritten - Premium underwritten by an insurer is the amount of premium collected by the insurer for undertaking the insurance risk.

c) Net Incurred claim – Net Incurred Claim is the amount of claims underwritten by the insurer. These are those claims that have been paid by the insurance companies to their clients. High incurred claims ratio indicates that the insurance companies have been able to service their claims to the satisfaction of their customers.

d) Underwriting - Underwriting is the process of selecting risks for the purpose of insurance. The risk is classified according to the degree of insurability so that the appropriate premium rates may be charged for undertaking the risk. The results of underwriting risk may be the profit or loss which arises out because of the operations of an insurance company. The risks failing to qualify in the underwriting process may not be insured by the insurance company.

e) Operating expenses – Operating expenses are those expenses which are incurred by an insurance company in operating its activities. These expenses include official expenses, administrative expenses and distribution expenses etc. In order to increase profitability, every insurance company should try to decrease its operating expenses and increase its revenue.

Till date there are twenty-three (23) general insurance companies operating in India, of these six (6) are under the public sector and the rest under the private sector.

A. GROSS PREMIUM UNDERWRITTEN

To calculate the performance of insurers the first dimension we have taken is in terms of gross premium underwritten in India. The premium underwritten by an insurer is a measure to judge the penetration level of the insurer.

In consonance with our objective number one we now discuss hereunder gross premium underwritten by the insurers under our research enquiry.

Table: 1 GROSS PREMIUM UNDERWRITTEN

YEAR	Number of private sector companies registered	Gross Premium underwritten by Private sector units(in crore)	Premium underwritten by the industry as a whole (in crore)	Market share of the private sector companies (In percentage)
2002-03	8	1341.60	14272.67	9.40
2003-04	8	2257.83	15594.52	14.47
2004-05	8	3507.62	17480.59	20.07
2005-06	9	5361.53	20359.72	26.33
2006-07	9	8646.57	24905.47	34.71
2007-08	11	10991.89	27823.74	39.50
2008-09	13	12321.09	30351.84	40.59
2009-10	13	13977.00	34620.45	40.37
2010-11	15	17424.63	42576.45	40.92
2011-12	15	22315.03	52875.77	42.20
2012-13	17	27950.69	62972.82	44.38

Source: IRDA annual reports.

Table 1 exhibit that the gross premium underwritten by the private sector insurers, it reveals a regular increase in the market share of the private players every year. In the very first year of operation of the private players their market share was 3.74% which rose up to 9.40% and then 14% of the total premium underwritten by the industry in the next two years. Then the market share has been stagnant at 40% for three years from 2009- 2011. This upward movement in the market share of premium underwritten by the private insurers depicts that the level of penetration by private players has improved each year. And that they have been successful over the years in snatching the share of cake from the mouth of public insurers. The four public players have lost their market to the new players in the field. The growth rate of premium underwritten by the industry over the years proves the improvement in the penetration level of the insurers as well as successful tapping of the uninsured market.

The improvement in the premium of the non-life industry can be attributed to various factors such as:

a. the increase in the sale of mega risk policies,

b. the popularity and new market for the health care products,

c. high demand for automobiles in the country which in turn increased the demand for insurance of the same,

d. the revision of the motor tariff rates in July,2002 which were not revised for a long period

e. increase in medi-claim premium

f. last but not the least the extensive growth of the economy.

B. NUMBER OF NEW POLICIES ISSUED

The number of policies issued by the insurers is an important parameter for measuring the penetration level. It is a measure to assess the extent of penetration level achieved. This has been indicated in the following table.

TABLE: 2 NUMBER OF NEW POLICIES ISSUED

Year	No. of policies issued by the	Total number of policies issued	Market share of private insurers

	private insurers (in lakhs)	by the industry as a whole	(in percentage)
2002-03	1676	43561	3.85
2003-04	3298	41726	7.90
2004-05	5144	49778	10.33
2005-06	8946	52892	16.91
2006-07	12692	46664	27.19
2007-08	18703	57250	32.66
2008-09	21922	67060	32.69
2009-10	24084	67488	35.68
2010-11	28765	79341	36.25
2011-12	32930	85744	38.40
2012-13	38056	107024	35.55

Source: IRDA annual reports.

The data furnished above reveals that the number of policies issued by the private sector entities grew at a healthy rate over the years. The number of policies issued by the industry as a whole has grown at a considerable rate every year after the entry of private players in the market. The private players have been successful in increasing their market share every year. The year 2012-13 witnessed growth in overall policies issued but there has been a slight decrease in the number of policies issued by the private players. Unprecedented growth in the number of policies issued is a remarkable feature of the post liberalised period. The private sector insurers can be given the credit for the enlargement of the non-life insurance coverage.

C. UNDERWRITING PERFORMANCE (Underwriting profit/loss)

The third parameter available for measuring the performance is underwriting performance of the insurer. Underwriting performance can result either in profit or in loss of the insurer which is projected in the following table.

TABLE: 3 UNDERWRITING PERFORMANCE

YEAR	Underwriting experience of private sector companies	Underwriting experience by the industry as a whole
2001-02	(127.56)	(2188.99)
2002-03	(9832)	(1768.48)
2003-04	(6373)	(2218.48)
2004-05	250	(2329.38)
2005-06	(5061)	(3998.76)
2006-07	(106.42)	(2557.54)
2007-08	(598.90)	(3899.49)
2008-09	(1099.21)	(5326.11)
2009-10	(1359.51)	(5900.69)
2010-11	(2419.45)	(9968.95)
2011-12	(2999.45)	(8816.84)
2012-13	(1842.56)	(6984.28)

Source: IRDA annual reports.

The above table depicts that the underwriting losses of the private entities decreases by Rs. 1,843 crore in the year 2012-13 as compared to the previous year. It is the strength and capability of the insurance companies to compensate for the impact of their underwriting losses through their investment income. The improvement in the results of underwriting losses was due to decline in net claims payable, decrease in expenses of management as well as decrease in reserves for unexpired risks by the insurers. The positive underwriting performance in 2004-05 by the private entities was due to decrease in management expenses as well as decline in additional reserves of these entities and lastly because of the reinsurance commission received by the private insurers. The abrupt increase in the total underwriting losses of the non-life insurance players during the year 2010-11was mainly due to the increase in Motor Third Party Liability segment.

D. SOLVENCY MARGIN

Solvency margin is the excess of the assets of the insurers over their liabilities so as to maintain a safety margin. All insurance companies operating in India are mandatorily required by the IRDA to maintain a minimum solvency ratio of 1.5 at all times. And this minimum solvency margin maintenance has to be reported quarterly to IRDA by all insurers. Solvency margin is also used an as indicator of performance as discussed hereunder.

It is an important parameter for measuring the strength of an insurance company, but it alone cannot be the single criteria for judging so other factors like claims efficiency, liquidity and investment policy also play an important role in measuring the efficiency of an insurer. The IRDA regulations 2000 require all general insurers to maintain an excess of assets over liabilities to an extent of not less than Rs.50 crores or a sum equivalent to 30% of net incurred claims. All the insurers are required to meet the solvency margin requirements at all times.

In the year 2003-04 the comparison revealed that two public sector insurers namely New India Assurance Company Limited and United India Assurance Company Limited out of four public sector insurers reported a solvency ratio of above 1.5% while the other two National Insurance Company Limited and Oriental Assurance Company Limited could not reach the required mandatory solvency level in the previous year. Of the eight private sector insurers operating except Tata AIG General Insurance Company Ltd, all the other insurers met this solvency requirement stipulated by IRDA. The solvency margin reported by Tata AIG was 1.36. Five insurers reported an improvement in their solvency ratio as compared to the previous year.

During 2004-05 two insurers New India Assurance Company Limited and United India Assurance Company Limited under the public sector reported performance above the solvency ratio while the solvency ratio of Oriental Insurance Company Limited and National Insurance Company Limited declined to 1.30. Under the private sector all insurers except Tata AIG General Insurance Company Limited which was at 1.31 met the solvency margin.

In the year 2005-06, all the four public sector insurers witnessed an improvement in the solvency ratio and met the solvency requirement of IRDA. Of the eight non-life insurers under private sector six met the solvency ratio except Bajaj Allianz General Insurance Company and ICICI Lombard General Insurance Company Limited.

The year 2006-07 was historic in the sense that all the non-life insurers under the public as well as private sector met the stipulated solvency ratio of 1.5%.

During 2007-08 IRDA introduced the quarterly reporting of solvency status for all the insurers. Accordingly insurers are required to file their solvency status on June 30th, September 30th, December 31st and March 31st. All the four public sector insurers met the requirements. All the private sector insurers also met the stipulated margins.

In the year 2008-09, all the four public sector insurers complied with the stipulated ratio. Under the private sector, all insurers except Cholamandalam MS General Insurance met the solvency ratio. Five insurers under the private sector reported higher solvency ratio.

During 2009-10, two insurers Royal Sundaram General Insurance Company and HDFC Ergo General Insurance Company under the private sector did not meet the required stipulation. All the public sector insurers complied with the requirements of IRDA.

Year 2010-11 witnessed the fulfilment of the stipulated solvency ratio by all the public as well as private sector insurers.

In the year 2011-12, all the private and public sector insurers complied with the stipulated solvency margin prescribed by the IRDA.

The year 2012-13, all the insurers under the banner of public sector succeeded in complying with the statutory solvency margin requirement, of the seventeen private sector insurers except one all other insurers complied with the requirement of solvency margin by the IRDA.

E. OPERATING EXPENSES

We now consider another parameter used as a measure tool for performance evaluation of insurance company named as operating expenses.

Operating Expenses are the expenses incurred.

Table:4 OPERATING EXPENSES

YEAR	Operating Expenses of Private sector companies(in crore)	Operating Expenses of the industry as a whole	Market share of the private sector companies (In percentage)
2001-02	175090	270087	6.48
2002-03	317719	308432	10.30
2003-04	495166	414284	11.95
2004-05	691982	433229	15.97
2005-06	106051	507743	20.88
2006-07	170015	530689	32.03
2007-08	248230	613527	40.45
2008-09	301988	736709	40.99
2009-10	312961	839220	37.29
2010-11	393188	1062048	37.02
2011-12	461400	1117800	41.27
2012-13	551600	1330700	41.45

Source: IRDA annual reports.

The above table depicts that the operating expenses of the private entities has been always on a rise. The reasons for this are the expenses incurred by the insurers in establishing new branches, maintenance of the offices, creating distribution channels to reach the masses, maintaining mandatory solvency margin etc. The overall industry has always faced an increase in the expenses which was mainly because of the high expenses incurred by the private entities. The year 2003-04 exhibited a sharp increase in the expenses of the public sector insurers on account of Voluntary Retirement Scheme introduced to bring down the staff strength. There are mandatory restrictions imposed on the insurers in incurring expenses by the management. The reasons being the business of insurance is undertaken for mitigating risk of others and the insurer makes itself liable to a third party so under this background the premium collected in a given year cannot be considered an income and spent off. The premium need to be conserved so as to meet unforeseen event.

F. NUMBER OF OFFICES

The total number of offices of private sector insurers India as on 31st March,2013 was 1827 as compared to that of public sector insurers which is a 6272. This shows an unhealthy growth of the private entities. Although the number of offices operated by the private sector insurers are on a rise yet the penetration level is low. Out of the total of 640 districts in India the public sector insurers function through their offices set up at 573 districts (i.e. at almost 90% coverage), while the private sector entities operate through their offices at 270 districts only covering nearly 44% only. In India still a decade after the privatisation of the insurance sector there are nearly 67 (nearly 10%) districts in India which do not have any offices of the non-life insurers. out of the total 640 districts in India as on 31st March 2013. Out of the total 35 states and union territories in India the non-life insurers have been successful in opening offices at all districts for only nineteen of such states and union territories. The non-life sector insurers have a long way to go as there are still 362 districts in the country where they do not have any offices. This low level of penetration of the non-life insurers both public and private is a major reason behind the low insurance penetration by the non-life insurers as compared to the life insurers. So, to improve the coverage the insurers need to open offices in the untapped districts of the country.

However we encountered a contradictory situation in this regard. To enhance the level of penetration, opening of new offices is essential but not sufficient condition; because opening of new offices will lead to increase in expenses. The insurers may now look for some alternatives such as instead of opening a physical office it may be a kind of virtual office/ satellite office/ insurance correspondent intermediaries or bancassurance. Hence, it is necessary to establish a trade-off between opening of new office vis a vis premium underwritten vis a vis premium income mobilised vis a vis number of policies issued and the extent of coverage offered. Consideration of all these issues is not only essential but a sufficient condition for managerial decision.

SUGGESTIONS

1. The private sector insurers require to infuse additional capital from time to time so as to raise the underwriting capacity which will help to underwrite higher business.

2. Leveraging on better technology will help in improving the penetration level of the private insurers.
3. Simplify the administration of business by computerisation of operations of the insurers at the branch level.
4. Rigorous inspection on the part of the regulators to improve the performance of the insurers is the need of the hour.
5. In India the majority of the population stills resides in villages and rural areas and so it is necessary to develop products catering to their needs.
6. Initiative on the part of the private insurers to open offices in those districts which do not have any non-life insurers office.
7. Geographical division should be kept in mind while providing information and in preparation of annual reports.
8. NABARD gives information in rural sector through this system – IRDA should also improve it and provide information on geographical location wise.

CONCLUSION

No doubt the reforms initiated decades ago has many achievements to its credit yet these achievements require to be further built upon to improve the efficiency of this sector. The sector still has a long way to go in terms of cost efficiency as well as penetration level across the country. The continual entry of private players in joint venture with foreign players has benefitted customers with improvement in services rendered, innovative products which are customer friendly, strengthening their bargaining capacity. But the insurers are on a weaker side as there prevails price war among the insurers with the detariffing of the general insurance industry. So insurers need to improve and consolidate their underwriting of risk. This can be overcome by training the underwriters well as well as equipping the sales person to respond to the varied needs of the customer. No doubt the short term performance of the insurance industry seems quite challenging yet the high potential untapped market provides for ample scope in future. Privatisation of insurance sector was the beginning of a process which has a long way to go and is not a solution in itself.

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