ANALYSIS OF FDI IN INSURANCE SECTOR IN INDIA

Yogita Sharma*

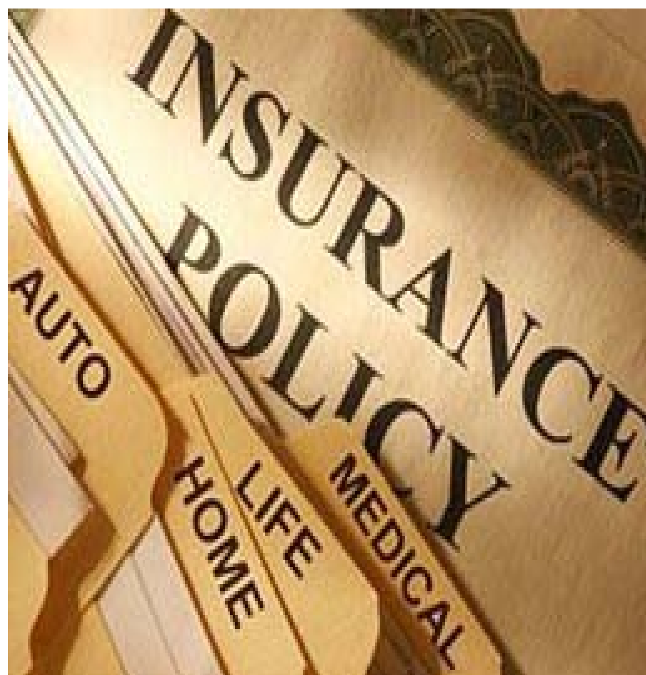
ABSTRACT

There is hardly a facet of the Indian psyche that the concept of 'foreign' has not permeated. This term, connoting modernization, international brands and acquisitions by MNCs in popular imagination, has acquired renewed significance after the reforms initiated by the Indian Government in 1991. Generally speaking FDI refers to capital inflows from abroad that invest in the production capacity of the economy and are "usually preferred over other forms of external finance because they are non-debt creating, non-volatile and their returns depend on the performance of the projects financed by the investors. FDI also facilitates international trade and transfer of knowledge, skills and technology. "Foreign direct investment is of growing importance to global economic growth. This Paper mainly focus on the Foreign Direct Investment in the Insurance sector and its significance in insurance sector in India . The Insurance sector in India has a great potential even during the downtrend and FDI flow is expected to rise in the mere future. This paper attempt to current status of fdi in insurance sector in India. Currently, only 26% of FDIs is permitted in insurance sector. The total insurance business would touch US$ 60 billion size. If insurance sector is opened up to an extent of 49% for FDIs, it is expected that FDI's contribution to insurance business would touch nearly US$ 2 billion.

*Lecturer in Commerce, GNG College, Yamuna Nagar

INTRODUCTION

There is hardly a facet of the Indian psyche that the concept of 'foreign' has not permeated. This term, connoting modernization, international brands and acquisitions by MNCs in popular imagination, has acquired renewed significance after the reforms initiated by the Indian Government in 1991. Generally speaking FDI refers to capital inflows from abroad that invest in the production capacity of the economy and are "usually preferred over other forms of external finance because they are non-debt creating, non-volatile and their returns depend on the performance of the projects financed by the investors. FDI inflow helps the developing countries to develop a transparent, broad, and effective policy environment for investment issues as well as, builds human and institutional capacities to execute the same. The insurance sector is of considerable importance to every developing economy; it inculcates the savings habit, which in turn generates long-term investible funds for infrastructure building. The nature of insurance business ensures constant inflow of funds - the payout is staggered and contingency related - thereby making it readily available for investment on infrastructure building. Its contribution to GDP is quite significant. The Union government had opened up the insurance sector for private participation in 1999, also allowing the private companies to have foreign equity up to 26 per cent. Following the opening up of the insurance sector, many private sector companies have entered the insurance business. The insurance sector has been a fast developing sector with substantial revenue growth in the non-life insurance market, but in spite of its huge population.



HISTORY OF INSURANCE

A contract of insurance may be defined as a contract whereby, one person, called the 'insurer', undertakes, in return for the agreed consideration, called the 'premium' to pay to another person, called 'assured', a sum of money or its equivalent on the happening of a specified event.The aim of all insurance is to make provisions against dangers which beset human life and dealings. Those who seek it endeavor to avert disasters from themselves by shifting possible losses on the shoulders of others who are willing for pecuniary consideration, to take risk thereof, and in the case of life assurance, they endeavor to assure to those dependent on them a certain provision in case of their death, or to provide a fund out of which their creditors can be satisfied. In India, insurance has a deep-rooted history. It finds mention in the writings of Manu (Manusmrithi), Yagnavalkya (Dharmasastra) and Kautilya (Arthasastra). The writings talk in terms of pooling of resources that could be re-distributed in times of calamities such as fire, floods, epidemics and famine. This was probably a pre-cursor to modern day insurance. Ancient Indian history has preserved the earliest traces of insurance in the form of marine trade loans and carriers' contracts. Insurance in India has evolved over time heavily drawing from other countries, England in particular.

THE BRITISH PERIOD

1818 saw the advent of life insurance business in India with the establishment of the Oriental Life Insurance Company in Calcutta. This Company however failed in 1834. 1870 saw the enactment of the British Insurance Act. This era, however, was dominated by foreign insurance offices which did good business in India. The Indian Life Assurance Companies Act, 1912 was the first statutory measure to regulate life business. In 1928, the Indian Insurance Companies Act was enacted to enable the Government to collect statistical information about both life and non-life business transacted in India by Indian and foreign insurers including provident insurance societies. In 1938, with a view to protecting the interest of the Insurance public, the earlier legislation was consolidated and amended by the Insurance Act, 1938 with comprehensive provisions for effective control over the activities of insurers.

OBJECTIVES OF STUDY:

- Toknow what are the strength/opportunity and weakness and threats.
- To know the significance of Foreign Direct Investment for Indian Insurance Industry.
- To know what are the problems faced by in insurance sector in India.
- To know why opposite parties against raising fdi in insurance sector.

- To knowwhat areissues regardingfdi in insurance sector in India.

SWOT ANALYSIS

STRENGHTS/OPPORTUNITY

- A range of new products had been launched to cater to different segments of the market, while traditional agents were supplemented by other channels including the Internet and bank branches.
- These developments were instrumental in propelling business growth, in real terms, of 19% in life premiums and 11.1% in non-life premiums between 1999 and 2003.
- India has a large population with an increase in its per capita income.
- India's middle income is rapidly increasing emerging as a profitable market.
- India's improving economic fundamentals will support faster growth in per capita income in the coming years, which will translate into stronger demand for insurance products.
- Strong growth can be sustained for 30–40 years before the market reaches saturation.
- There is plenty of room for growth in personal accident, health and other liability classes.
- Rising household income and risk awareness will be the key catalysts to spurring more demand for these lines of business in the future.
- Health insurance could potentially have an important role in driving insurance market development forward.

WEAKNESS/THREATS

- India is among the lowest-spending nations in Asia in respect of purchasing insurance (China, which spent USD 36.3 per capita on insurance products & Indian spent USD 16.4) .
- Even after the liberalization of the insurance sector, the public sector Insurance companies have continued to dominate the insurance market.
- In the long run, other forms of non-price competition like aggressive advertisement wars are likely to lead to increasing costs, eventually harming the interests of the consumers.
- A key challenge for India's non-life insurance sector will be to reform the existing tariff structure. From a pricing perspective, the Indian non-life segment is still heavily regulated
- Reinsurance is only provided by GIC .

- While the insurance business is highly concentrated in India, the share of foreign companies is low.
- Strong growth prospects pose pressure on the industry, and the economy at large, to better manage the exposure to natural perils.
- Questionable Reputation of the Foreign Partners.

THE NATIONALIZED ERA

The Insurance Amendment Act of 1950 abolished Principal Agencies. However, there were a large number of insurance companies and the level of competition was high. There were also allegations of unfair trade practices. The Government of India, therefore, decided to nationalize insurance business. An Ordinance was issued on 19th January, 1956 nationalizing the Life Insurance sector and Life Insurance Corporation came into existence in the same year. The LIC absorbed 154 Indian, 16 non-Indian insurers as also 75 provident societies—245 Indian and foreign insurers in all. The LIC had monopoly till the late 90s when the Insurance sector was reopened to the private sector.This millennium has seen insurance come a full circle in a journey extending to nearly 200 years. The process of re-opening of the sector had begun in the early 1990s and the last decade and more has seen it been opened up substantially. In 1993, the Government set up a committee under the chairmanship of RN Malhotra, former Governor of RBI, to propose recommendations for reforms in the insurance sector. The committee submitted its report in 1994 wherein, among other things, it recommended that the private sector be permitted to enter the insurance industry. They stated that foreign companies be allowed to enter by floating Indian companies, preferably a joint venture with Indian partners.Following the recommendations of the MalhotraCommittee report, in 1999, the Insurance Regulatory and Development Authority was constituted as an autonomous body to regulate and develop the insurance industry. The IRDA opened up the market in August 2000 with the invitation for application for registrations. Foreign companies were allowed ownership of up to 26%. In December, 2000, the subsidiaries of the General Insurance Corporation of India were restructured as independent companies and at the same time GIC was converted into a national reinsurer. Parliament passed a bill de-linking the four subsidiaries from GIC in July, 2002. Today there are a number of private sector insurance companies. The table below shows the breakup of insurance companies:-

Type of Business	No of Public Sector Companies	No of Private Sector Companies	Total Companies
Life Insurance	01	20	21
General Insurance	06	14	20
Re insurance	01	0	1
Total	08	34	42

Source: Insurance Regulatory & Development Authority Official Website www.irda.org

The insurance sector in India used to be dominated by the state-owned Life Insurance Corporation and the General Insurance Corporation and its four subsidiaries. But in 1999, the Insurance Regulatory and Development Authority (IRDA) Bill opened it up to private and foreign players, whose share in the insurance market has been rising.As a part of overall financial sector reforms, the Government set up the Committee for Reforms in the Insurance Sector in 1992. In its report released in early 1994, it recommended the opening up of the sector to private sector participation.

CURRENT STATUS OF FDI IN INSURANCE SECTOR

Since end of 2000, While Life insurance has been privatized. Indian Government have opened the entry door for foreign players and private companies in Life insurance sector. In the present scenario has revealed 22 Private Life Insurance Companies working in Indian markets, Private life insurance companies have been keeping behind Indian largest public company's (LIC) in an innovative products, smart marketing, and aggressive distribution attracts customer toward the private life insurance companies, sign up Indian customers faster than anyone expected. Indian, who had always seen life insurance as atax saving device, are now suddenly turning tothe private sector and snapping up the newinnovative products offer to customers and investmentplans. The Life Insurance companiesin India have grew by an impressive 36% withpremium income in the year 2003-2004 Rs 24.29billion from new business Rs253.43 billion during the fiscal year 2004-2005 in this duration havebeen braving stiff completion from Private Life Insurance Companies. In which LIC has clocked21.87% growth in business at Rs 197.86 billion by selling 2.4 billion in new polices in the year 2004-2005, but this was still enough the fall. Its market share as Private Player grew 129% Rs 55.57 billion in the year 2004-2005 with annual growth rate 15-20 %, the largest number of Life Insurance Polices in force, the potential of the Indian Insurance industry is huge.The total value of insurance market estimated Rs 450 billion in 2004-2005.Theinsurance business grow in India 17% in Fiscal year 2008-2009 $ 30 billion. The country economy clocks GDP 7.6%. In Fiscal year 2007-2008 Life Insurance has been grown up their business 23.3%Rs

930 billion, The Private Life Insurance Companies have made a record first quarter year in 2009,has recorded 13.22% growth in first year premium and 20.36% number of polices increase after the considering to extend the limit of FDI in insurance industry. In the year 2002-03 public company's (LIC) was collected 546228.49 cr. in the comparison with five selected private sector companies their were total collection 733.52 cr. we can discus in the year 2004-05 while total significant collection of public company was 75127.29 and in a comparatives withselected private companies their were total collection of premium around 4402.29 cr. In the year 2007-08 while total collection of public company's was 149789.99 cr. and selected private companies their were total collection of premium 27979.99 cr. In during the last session 2009-10 public company has been collected total premium around 1, 85,985, its comparison of selected private companies, their were total collection of premium 16,495.86 cr. The huge premium collection have increased every financial year that was gearing insurance business in India on fast pace.Presents the resultant figure of the insurance companies and its market share that indicate the penetration of life insurance companies in Indian markets, such penetration indicate the fruitful growth and its positive result of utilization foreign investment in life insurance sector. The new players have improved the service quality of the life insurance. As a result haveseen LIC continuing declining in its career from theyear 2000 onward, market share have been distributing among the private players. In the financial year 2009-10, LIC still hold 65% market share among doing business of life insurance companies in India, for upcomingnature of these private players are gaining strength togive more competition to LIC in earlier future. Marketshare of LIC has decreased from 95 %(2002-03) to 81%(2004-05), in the financial year 2007-08 still hold 74.39%and following private players hold the rest of themarket share.The central government has proposed to enhance foreign direct investment (FDI) in insurance to 49% in its second wave of reforms announced recently. At present foreign investment in private insurance companies is restricted to 26% of their capital, which is now proposed to be increased to 49% by passing an amendment to the Insurance Act in the ensuing session of Parliament. Announcing this decision, finance minister P Chidambaram said "the benefits of this amendment to the insurance act will go to the private sector insurance companies, which require huge amounts of capital and that capital will be facilitated with the increase in foreign investment to 49%." He also clarified that this will not apply to public sector insurers like Life Insurance Corporation of India (LIC) and the five general insurancecompanies. At present there are 44 private insurance companies authorized by the Insurance Regulatory and Development Authority (IRDA) operating in the country. These comprise of 23 life insurance, 17 general

insurance and four health insurance companies, since the insurance sector was opened for private sector in the year 2000. These are all joint ventures between the Indian promoters who hold up to 76% and foreign insurance companies who hold up to 26% as mandated by the law.The insurance business requires additional capital as it grows and this has to come from the promoters. If the Indian promoters are unable to contribute their share of the capital, they will not be able to grow. Foreign companies with deep pockets will be able to fill this gap, if they are allowed to invest up to 49% of the capital. It is estimated that the private insurers need about Rs60,000crore of additional capital during the next five years. Therefore, the raising of FDI cap to 49% will come handy for the foreign partner to increase their stake in the company, without the local partner having to put matching capital in to the company. The foreign partner will bemore than happy to increase its stake, as it will help it get a bigger share of the pie, and will also give it a larger role in running the company according to its ways, by virtue of a higher shareholding in the company. This will, therefore, be a boon to the foreign insurers to come to India in a big way.

PROBLEMS FACING THE INDIAN INSURANCE SECTOR:

The government's intention was to create a monopoly and protect it from foreign and private competition. So, what were the implications of such a conservative approach? Insurance sector faced problems such as capital scarcity, poor product quality and technological obsolescence. In the year 2000, life insurance penetration in india stood at an abysmal 2.4%.

- ✓ There is a huge lack of proper awareness regarding the need of insurance.
- ✓ Insurance premiums are looked at as a means of tax evasion and savings. The true importance of insurance often gets overlooked. In addition to this, india is a country with a huge lower middle class section.In their daily struggle to try and get both the ends meet, insurance premiums come as a luxury.
- ✓ The inflexible and expensive plans offered in the market make it more difficult for the common people to invest.
- ✓ The situation in rural india is even worse. A small fraction of the people have bank accounts, and the concept of insurance is very much alien. People have little disposable income, and the only form of life insurance is joint family

MYTHS ABOUT HIKE IN FDI IN INSURANCE FROM 26% TO 49%

MYTH 1: FDI CAP HIKE NECESSARY TO IMPROVE INSURANCE PENETRATION

NO! DOMESTIC CAPITAL MARKETS ARE ENOUGH.

UPA claims that to improve insurance penetration in country additional capital of Rs.60,000crores required over 2010-2015 based on IRDA projections. Since constraints of Indian partners to currently contribute 74% of capital are a hurdle, foreign partners will contribute if cap relaxed. BUT IRDA Chairman's deposition to Parliamentary Standing Committee itself states these projections are "not very accurate" and "just an arithmetic". Public Sector insurance companies are confident of being able to raise money from domestic capital markets as and when required. No need for hiking cap.

MYTH 2: FDI CAP HIKE NECESSARY TO INCREASE INFRA INVESTMENTS

NO! LIC & PUBLIC SECTOR NON-LIFE COMPANIES CONTRIBUTE OVER 70% OF INFRASTRUCTURE INVESTMENTS

UPA claims investments are required in crucial infrastructure sector and increasing FDI will enable private insurers to hike spend on infra – BUT LIC's share of investment in infra was 70% and that of public sector general insurers' was 71% compared to the private sector during 2009-10 so it is obvious that private insurers with foreign partners are more interested in profits than in investing in buildingIndia! Presence of foreign equity does NOT increase infra investments.

MYTH 3: FDI CAP HIKE NEEDED TO IMPROVE PRODUCT OFFERING

NO! CURRENT 26% LIMIT ENOUGH TO BRING IN NEW TECHNOLOGY AND PRODUCTS

Product portfolios of the public sector insurers are comparable to those of private sector. Most new products introduced by foreign insurers are investment-oriented in nature with HIGH RISKattached and are totally inappropriate in providing social security to the Indian people, especially for the poor and aamaadmi. These reasons were used by government to bring in 26% foreign equity and assurances were given that the cap would not be increased- it is absurd that the very same reasons are now being given to justify increase in FDI limit!

ISSUES IN FDI IN INSURANCE SECTOR:

Efficiency of the companies with FDI: The opening up of this sector for private participation in 1999, allowed the private companies to have foreign equity up to 26 per cent. Following this up 12 private sector companies have entered the life insurance business. Apart from the HDFC, which has foreign equity of 18.6%, all the other private companies have foreign equity of 26 per cent. In general insurance 8 private companies have entered, 6 of which have foreign equity of 26 per cent. Among the private players in general insurance, Reliance and Cholamandalam does not have any foreign equity. The aggregate loss of the

private life insurers amounted to Rs. 38633 lakhs in contrast to the Rs.9620 crores surplus (after tax) earned by the LIC. In general insurance, 4 out of the 8 private insurers suffered losses in 2002-03, with the Reliance, a company with no foreign equity, emerging as the most profitable player. In fact the 6 private players with foreign equity made an aggregate loss of Rs. 294lakhs. on the other hand the public sector insurers in general insurance made aggregate after tax profits of Rs. 62570 lakhs.

2**. Credibility of foreign companies**: The argument that foreign companies shall bring in more expertise and professionalism into the existing system is debatable after the recent incidents of the global financial crisis where firms like AIG, Lehman Brothers and Goldman Sachs collapsed. Earlier too, The Prudential Financial Services (ICICI's partner in India) faced an enquiry by the securities and insurance regulators in the U.S. based upon allegations of having falsified documents and forged signatures and asking their clients to sign blank forms. This was after it made a payment of $2.6 billion to settle a class-action lawsuit attacking wrong insurance sales practices in 1997 and a $ 65 million dollar fine from state insurance regulators in 1996. AMP closed its life operations for new business in June 2003. Royal Sun Alliance also shut down their profitable businesses in 2002. A recent report by Mercer Oliver Wyman, a consultancy, found that European life insurance companies are short of capital by a whopping 60 billion Euros. According to the Mercer Oliver Wyman Report the German, Swiss, French and British insurers suffer from severe capital inadequacy, which is a result of undertaking risky investments in equity and debt instruments in the past. Hence FDI in Insurance in India would expose our financial markets to the dubious and speculative activities of the foreign insurance companies at a time when the virtues of regulating such activities are being discussed in the advanced countries.

3**. Greater channelization of savings to insurance**: One of the most important duties played by the insurance sector is to mobilize national savings and channelize them into investments in different sectors of the economy. However, no significant change seems to have occurred as far as mobilizing savings by the insurance sector is concerned even after the liberalization of the insurance sector in 1999. Therefore the private or foreign participation has not been able to achieve the goal.

4**. Flow of funds to infrastructure:** The primary aim of life insurance is about mobilizing the savings for the development of the economy in long term investment in social and infrastructure sectors. The same vision was argued for the opening up of insurance market would enable huge flow of funds into infrastructure. But more than fifty percent of the policies they sell are ULIPS where the investments go into the equity markets. As per a

report, 95% of policies sold by Birla Sun Life and over 80 percent of policies sold by ICICI Prudential were unit-linked policies during 2003-04. Under these schemes, nearly 50 percent of the funds are invested in equities thus limiting the fund availability for infrastructural investments. On the other hand, the LIC has invested Rs.40,000 crore as at 31.3.2003 in power generation, road transport, water supply, housing and other social sector activities. IRDA figures further imply that the share of the public sector life and non-life insurance companies in investment in infrastructure is greater than their market share. Despite the FDI cap being set at 26%, the investment from the insurance sector to the infrastructure sector was predominantly from the public sector companies. Hence the point of raising the FDI cap in the insurance sector for mobilizing resources does not hold good

COMMENTS OF POLITICAL PARTIES REGARDING RAISING FDI IN INSURANCE SECTOR IN NIDIA

- The North Zone Insurance Employees Association (NZIEA) opposed the government's proposal to raise the foreign direct investment (FDI) in the insurance sector from 26 to 48 per cent protesting that the FDI in the sector will mostly benefit the speculative market and "do no good to the country".
- Addressing a press conference NZIEA general secretary Anil Kumar Bhatnagar said that the Centre had recently approved the insurance laws (amendment) bill, 2008, and it was being proposed to be placed for discussion in the RajyaSabha .Bhatnagar said that the Parliamentary standing committee headed by former finance minister YashwantSinhahad unanimously submitted its report on December2013 to the parliament, and the committee had opposed the increase in FDI in the insurance sector.
- The CPI(M), which has been opposing the opening up of the insurance and pension sectors, said the Cabinet's decisions will make India's finance sector more vulnerable to speculative finance capital.

ADVANTAGES OF FDI IN INSURANCE SECTOR

1**. Capital for expansion**: FDI has the potential to meet India’s long term capital requirements to fund the building of infrastructures which is critical for the development of the country. Infrastructure has been the major factor which has restricted the progress of the Indian economy. Insurance sector has the capability of raising long term capital from the masses as it is the only avenue where people put in money for as long as 30 years even more. An increase in FDI in insurance would indirectly be a boon for the Indian economy, the

investments not withstanding but by making more people invest in long term funds to fuel the growth of the Indian economy.

2**. Wider Scope for Growth**: FDI in insurance would increase the penetration of insurance in India, where the penetration of insurance is abysmally low with insurance premium at about 3% of GDP against about 8% global average. This would be better through marketing effort by MNCs, better product innovation, consumer education etc.

3. **Moving towards Global Practices**: India's insurance market lags behind other economies in the baseline measure of insurance penetration. At only 3.1%, India is well behind the 12.5% for the UK, 10.5% for Japan, 10.3% for Korea and 9.2% for the US. Currently, FDI represents only Rs.827 core of the Rs.3179 crore capitalizations of private life insurance companies.

4. **Provide customers with competitive products, more options and better service levels**: Opening the FDI in the insurance sector would be good for the consumers, in a lot of ways. Increasing FDI limit would impact a lot of industries in a positive way and that we could even do without the FDI in many other sectors for some for example in real estate.

CONCLUSION:

we conclude that the suggested policy stance of enabling a greater role for foreign capital in the insurance sector, maynot necessarily have the desired impact in view the experience of its limited role thus far in terms of facilitating investment in infrastructure, deepening insurance accessibility for the poor and also in developing products suited as a means of providing social security to the Indian masses at large. On the other hand, increased role of foreign capital may lead to the possibility of exposing the economy to the vulnerabilities of the global market by way of likely inheritance of unsound balance sheets and financial health of the foreign partners through joint ventures and subsidiary routes, flight of capital outside the country and also endangering the interest of the policy holders. The present global economic scenario, any further hike in FDI at this juncture may not be in the interest of the Indian insurance industry, whereby the common man too would not stand to gain through insurance, particularly as a means of social security

REFERENCES

1. Gujarat National Law University, Gandhinagar, India. Planning Commission of India.2002. Report of the Steering Group on Foreign Direct Investment: Foreign Investment India. Government Report. p11. New Delhi: Planning Commission, Government of India. Accessed from

http://planningcommission.nic.in.aboutus/committee/strgrp/stgp_fdi.pdf. on 5th September, 2008 at 10:34 pm.

2. Foreign Investment Promotion Board (FIPB) has been set up by the government of India in order to increase the flow of foreign direct investments into the country. FIPB is the only agency in the country that deals with foreign direct investments and investments into India. The main objective of Foreign Investment Promotion Board (FIPB) is to encourage foreign 204 MqJBL (2009) Vol
3. Is higher FDI limit in insurance a threat for public sector insurers?zeenews.india.com/.../is-higher-fdi-limit-in-insurance-a-threat-for-p
4. Free Fdi in Insurance Essay - Tejasspawarwww.antiessays.com/free-essays/313034.html
5. FDI in insurance, a long way to go?
6. business-standard.com › Home › Economy & Policy
7. Big bang reforms: Cabinet approves 49% FDI in insurance, 26% in ...
8. timesofindia.indiatimes.com › Business