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Review of General Insurance

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REVIEW OF GENERAL INSURANCE*

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INTRODUCTORY REMARKS

Integrated Development of the insurance industry should be the main focus in the present scenario. One of the reasons, behind the turmoil in the financial world recently, was lack of coordination between various regulators in developed markets in Europe and in the United States. Hopefully, this wonderful thought of 'integration and co-creation' is going to strengthen the industry.

The moment people talk of 'insurance', they think of Life Insurance, and infer this as an investment product, expecting some money back after a period of time, if no loss happens. Due to this lack of awareness and clear-cut understanding of the General Insurance Industry, there is low level of penetration of general insurance in India. The focus of this talk is on General Insurance industry and putting it in the correct context.

In the context of Life Insurance, the tendency of the investor is to calculate how much he will get back after ten or fifteen years. Life Insurance industry's growth has been phenomenal mainly because of the investment angle to that. Conceptually, if you ask someone to pay for the 'risk' of fire or theft, it becomes a 'risk' for him and an opportunity' for the insurer. For insurance industry 'risk' becomes an 'opportunity' till such time it is a threat and not that it becomes a reality. From the insured's angle, the perception of the risk is there. But the reluctance to price the risk and part with the money for carrying the risk by others is not generally felt. This is one of the important reasons why General Insurance industry is not growing very well in India. Penetration level of General Insurance industry in India is only .6% of the GDP as compared to Life Insurance industry which has grown to more than 6%.The major reason behind this is

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reluctance to pay for the risk and also general unawareness of the public about the General Insurance industry.

Between 1972 and 2001, the industry was nationalized and run by four PSU companies fully-owned by the government of India through GIC, as a holding company.

In 1972, there were around 107 insurance companies; whose total industrial premium figure was around Rs.180 cr. It grew to Rs. 2350 cr. in1992. Between 1992 to 2002, it grew to Rs.12,260 crore. Thus, whereas it took 20 years from 1972 to 1992 to achieve a growth of Rs.2000 crore, the volume grew by Rs. 10,000 crore in a span of 10 years between 1992 and 2002, when the industry was open to the private sector many more players came.

Between 2002-2009 (8 years), the industry has grown to Rs.31000 crore, i.e. around Rs. 20,000 crore. As against a growth of Rs.10000 crore in a period of 20 years, it grew 20,000 crore in 8 years. Therefore the opening up of the sector in the General Insurance industry has been a success and the growth has been phenomenal.

CURRENT STATUS OF GENERAL INSURANCE

Currently, there are about 18 General Insurance companies dealing with all the products-motor, fire, health etc. Apart from this, there are two stand-alone health insurance companies. One company is selling agricultural products and another company is selling export-credit insurance products. All put together report around 22 players. Many more are waiting in the pipeline. And 3-4 more players may come perhaps in the next financial year. Therefore this industry is poised for a great growth. To start a General Insurance company, it takes about a Rs. 100 crore as minimum capital. Investors with Rs. 100 crore can participate in the industry which grows with an annual premium of Rs. 3000 crore. So that is the opportunity of making more money in the industry. As premiums are paid in advance, there is little chance of bad debt loss. That is why more and more people are coming in the industry. Therefore growth is an attraction in the industry. But let us look at the people who are really operating; what is really happening.

There are two segments of profitable activity in the General Insurance companies.The core activity is underwriting, that is of issuing policies and settling claims, for which you have incurred the expenses of commission, and the management and office expenses. All the companies have been making underwriting losses except for one private company which has been making marginal profits for some years. World over also, the underwriting profits are not happening in a big way. They are marginal. The combined ratio is hovering around 92-93 %. Therefore, making huge underwriting profit is very difficult the world over. In India, we would like to break-even first, and then make some profits after sometime.

In India, still, companies are reporting net profits. How is it happening? It is by investment income, by selling the shares and making capital gains out of it, and showing net profit in the balance–sheet. Even that is drying up, because the underwriting losses are eating away the investment income and investment profits of the companies, and so the loss-scene is very alarming. It is intriguing to understand how the industry has functioned over a period as far as the profit-scene is concerned. The industry made a profit of Rs.23 crore, Rs.18 crore, Rs. 47 crore and Rs. 100 crore in different years between 1972 and 1983. From 1988-1989 onwards, the industry has been making underwriting losses, Rs.146 crore in 1988-89 , Rs. 120 crore in 1992-93, Rs. 384 crore in 1997-1998. The loss story continued up to 2002-03, with a loss of about Rs.5,700 crore after that. The total loss situation, which was incurred by the PSUs, turned positive with the entry of private players in 2001. From 2002 onwards, some organizations have been making some profits. But the last year, 2008-2009, when the industry as a whole made a premium of Rs. 31,000 crore, the total underwriting loss was of Rs. 1500 crore for all the 21 players put together. This was shocking and discouraging for the players. Because of this huge loss last year, which has eaten away the investment income, most of the private companies have reported a net loss situation. This has been noticed by all the companies, by their Boards as well as IRDA. So the corrections have to take place in the current year onwards. All the companies are understanding and addressing the problem of these huge underwriting losses.

Therefore, high underwriting losses are a big problem with the General Insurance industry today. Why is it happening? Is it controllable?

There are three segments to the business- fire insurance, marine and miscellaneous insurance.

Fire insurance is the insurance which covers big properties, refineries, big plants and things like that. We are talking of the individual risk of Rs.10,000 crore, Rs.15,000 crore, Rs.50,000 crore. Reliance refineries' sum insured is Rs. 50,000 crore (approx.). When you undertake such huge risk, you cannot retain it to the balance-sheet. It is more driven by the reinsurers. I cannot take bigger risk unless I have a capacity within me or I have purchased reinsurance from other reinsurance company. So it is a very tricky affair. If there is a bigger risk which an Insurance company wants to undertake, then they can take such risks when they are very sure that their capital can provide for such big risks or there is a reinsurer support for that. And naturally these risks have to be priced properly. Therefore fire is an important element of the risk-taking by the General insurance companies.

Pricing of this product is very essential. Till 2006 end, these products were priced by tariff advisory committee which ensured reasonable profit for the Companies. 2007 onwards, it was de-tariffed. After de-tariffing, the important segment of fire, has seen tremendous discounts being given by the companies. The companies, in the name of competition, have reduced the price levels, to unprofitable levels, giving huge discounts up to 80 to 90 % of the tariff rates. Some insurers still give discounts at the same level to grab the market. But the losses keep on occurring. In the case of Fire, it is disappointing to note that the industry premium level of Rs.6000 crore heavily came down to Rs.3000 crore in 2007-08. It was Rs.5000–Rs.6000 crore, prior to 2007-2008. It has come down to Rs.3000 crore level in the last year. That means the premiums have come down around 50% which is not at all desirable or warranted with the risk being same. This is one of the important factors contributing to underwriting losses. The remedy is pricing properly - Pricing of fire insurance products properly! The insurance companies understand that they should price insurance products properly. They also have the will to do it, but the competition and the craving for top-line growth is preventing them from doing it. Unless their drive for top-line growth comes down and insurers price their important products properly and adequately, the loss-situation is not going to change. This has been well-elaborated and well-analyzed. Some of the insurance companies have internally taken decision not to take very low-priced products in the current financial year. That is why the growth of some other companies is affected in the current year. Hopefully this year, or by the end of next financial year, this pricing aspect is well-addressed and high risk carrying situation in companies is rectified. It is a great illness for

General Insurance companies. Hope, it is addressed fast.

Motor insurance is one variant. There are two segments (i) Own Damage (ii) Third-party segment. Third-party segment consists of 'liabilities' we meet out of insurance companies' funds to compensate the victims of road-accidents. There, there is a big gap. Liability is unlimited as per the Act, but premium is fixed by the tariff. So, this gap has been sucking up the blood of insurance companies for a long time. Public sector companies were losing Rs.3000 to Rs.4000 crores annually on this particular Third-party liability segment alone. We were craving for a revision in TP premium rates for a long time. It was revised after a gap of 11 years in 2007. After 2007, it is static and not an indexed revision. Hence, within 2 years of revision, it is found to be inadequate. We are talking to the IRDA and stake-holders as to how to revise the premium rates. This is one thing where we have very little elbow-room, but we have the responsibility of managing the claims properly and efficiently. We are addressing that. Actually, for dealing with commercial vehicle's claims, it has been assigned to a pool so that common wisdom of all the companies is available for the management.

Motor Own Damage claims also create lot of issues and losses, but that is addressed by individual companies in an efficient way. However, as a common activity in controlling OD losses, there are leakages through the fraudulent claims. There are leakages through the no-claim bonuses being claimed by the same person even though he has made a claim in another company. There must be exchange of data between insurance company, so that such leakages are plugged.

An important factor that can come to the aid of motor insurance profitability is the Motor Vehicles Amendment Act, which is waiting Parliamentary approval. We will have better leverage in settling claims outside the court, once the amendments are in place.

Another sector, which was lingering previously and has grown tremendously, is the **health sector**. Health insurance is occupying 22% of the total premium today with a phenomenal growth rate of 40-45 %. It continues in the current year also. Here also, there is a run-away loss situation. The loss ratios of all the companies, including private companies, are not very good. Most of the companies are incurring more than 100% loss. PSU companies' rates are hovering around 120% to 130 % loss. There are many issues in health insurance claims management. There is very little or no regulation on health service providers who have jacked up the cost of health in India. It is a social problem in fact, because the insurance companies' losses are ultimately shifted to a common man who is purchasing health insurance through increased premium. So therefore, we all have represented to the government that there must be a regulation on the health service providers.

Non-availability of health service providers in the rural areas is another issue by which we are not able to penetrate the rural market to have health insurance. Parallely, the government is trying to get into this by providing the health insurance free of cost to the rural people through RSBY etc. They are addressing to a small segment of BPI only. There are enough studies that say that rural indebtedness is because of ill-health and huge health costs. Insurance companies are prepared to give this cover to the rural masses. But non-availability of health service providers in the rural area is a big issue.

'Lack of awareness' is a very important problem for the General Insurance industry. One can make an appeal to IRDA and General Insurance Council. Both are taking steps in this direction. One of the committees has even told the government that General Insurance should be part of the school curriculum, so that awareness about it can grow.

Another important lacuna, or where we have failed so far, is creating a sturdy data base of General Insurance industry's premium and claims in the last 30 years. IRDA has taken upon itself the task of collecting the data. They have accumulated this data in health and motor insurance for the last two years. I hope, it continues.

In case of some Companies, health data is unavailable. We are lacking very much, may be because of lack of computerization in PSUs. Complete connectivity between the companies is needed. Core insurance solution needs to be implemented. We have also come out with a portal to transact the business through internet. This is evolving now. So this is looked upon as a big drawback in the General insurance industry by the reinsurers who want to come and operate in India.

In future, the insurance laws are to be amended. They are almost in the final stage. This is going to take away lot of operational problems happening to the General Insurance industry. It is not only about the General Insurance Act but it also covers Motor Vehicles Act.

WHAT THE FUTURE LOOKS LIKE

Today we have only one set of regulations. Can we graduate to risk-based capital when the other countries are thinking of Euro II solvency models? We are only thinking and debating whether to go into risk-based capital regime to have better control of the companies. This is a tough challenge for the regulator. The companies have to grapple with it in a seasoned way. We should equip ourselves with it. This risk-based capital assures a sturdy risk-management department within the company to analyze the risk faced by insurance companies like the low-priced risk and various other exposures the company might be having. The company has to undergo stress-scenario and find out as to how the lack of insurance capacity is going to affect the balance sheet in the next 2-3 years. This is a new skill which the industries have to develop to address the issues.

Government is also trying to shift some of the social obligations like CGHS to the insurance industry. There will be more and more insurance opportunities but managing them will also be a challenge.

'Qualified people' and 'people with insurance knowledge' are in demand in the industry. There is a dearth of insurance-based people in the field. Developing expertise in the area for meeting the challenges of the sector, promises a great future to you. On the whole, interesting times are there for the insurance industry.