Impact of Foreign Direct Investment on Life Insurance Sector in India

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Abstract

Foreign direct investment in the insurance sector has been increased from 26 per cent to 49 per cent. The increase in the limit has an impact on the number of policies issued, incurred claims ratio and assets under management of life insurance companies. In the study, the impact of foreign direct investment on the performance of the life insurance companies was analyzed using the secondary data collected for a period of 13 years from April 2001 to March 2014. The data for the study was collected during the period when FDI limit was at 26 per cent. The effect of foreign direct investment was examined by using Pearson's Correlation and Simple Regression Analysis. The assets under management (investment decisions) of the private sector life insurance companies were influenced by the foreign promoters. But even after the entry of private sector insurance companies, the insurance density and insurance penetration of India were at low levels when compared to developing countries. LIC is the largest public sector life insurance company and is facing a tough competition after opening up the life insurance market to foreign players.

Keywords: *Foreign equity capital, Life insurance, insurance density, insurance penetration*

Introduction

Insurance in India has a deep-rooted history. India is the fifth largest insurance market among the globally emerging insurance economies. People put aside a sum of money every year to invest in insurance for protecting themselves from catastrophes. Life insurance policy would be always effective only when the policyholder is able to pay the premiums over the entire duration of the policy and the designated beneficiary would receive the benefits upon the death of the insured. Insurance inculcates saving habits to hedge against the future risks, which in turn generates long-term investible funds for the government, which can be channalised for the development of the country. Insurance forms a crucial part in a properly constructed financial plan and is mainly used as a tax saving instrument. Insurance policies can be used as an investment vehicle, but the returns will be limited.

India is the second most preferred destination for foreign direct investment (FDI) after China. Continuous flow of foreign investments across various industries in India clearly shows the faith the foreign investors have in the country's economy. The insurance sector has already undergone the sweet and sour experience of foreign investment in the early parts of 1990s. The government formed the Malhotra Committee in the year 1993 to propose recommendations for reforms in the insurance sector. One of the suggestions of the committee was to allow foreign insurance companies to purchase equity holdings of the Indian insurance companies and can do business in India as a joint venture with Indian partners. Forming of IRDA in 1999 was considered a major boost in the insurance sector. IRDA is acting as a watchdog and frames the rules and regulations for the activities of both government and private insurers in India. India allowed private companies in insurance sector in 2000, setting a limit on FDI to 26 per cent. But it had a little effect on the insurance sector only for a decade. IRDA batted for a hike in the foreign direct investment limit to 49 per cent in the insurance sector from the previous 26 per cent. Thus the FDI limit was raised from 26 per cent to 49 per cent in the Union Budget of 2014-15. However, the largest public sector company in insurance industry is Life Insurance Corporation (LIC), which is still owned by the government.

Review of Literature

Sadhak (2005) had analyzed the impact of globalization of life insurance in India, which forms an integral part of a nation's economy. The author suggested that the driving forces of globalization of insurance sector are push and pull factors. The push factors are the motives behind the movement of foreign insurance companies and the pull factors are the motives behind allowing the foreign insurance companies into the developing countries. He further stated that foreign equity in the local insurance companies can mobilize more savings, strengthen the financial stability of the host country and improve production and trade and that foreign equity is required in insurance sector in India to improve the insurance density and insurance premium.

Shilpa Thakur (2010) had argued about the competition in life insurance sector in India and the misuse of dominant position held by LIC. The author pointed out that for a longer period, LIC has been a dominant player in the life insurance sector in India and due to its established leadership skills, it was difficult for the new players to compete in the market. India needs more private participation in the life insurance sector in order to cover the entire population. The Insurance Amendment Bill presented in the Parliament is proposed to raise the FDI slab from 26 per cent to 49 per cent. LIC, which has a sovereign guarantee from the central government, is an unfair trade practice. With the opening up of market for foreign players the competition will be boosted and increasing the size of market.

Sanjay Manocha (2010) had propounded the opportunities to be tapped by the Indian insurance companies amidst of the global competition. In order to encourage competition, development and growth of insurance sector, the government opened the gates for the foreign companies to invest in the insurance sector. With the entry of foreign companies, the local players will get an opportunity to form alliances with them and can gain knowledge about the technical know-how and increase the financial strength. The new companies can provide innovative products, targeting the niche markets with a right mix of risk and returns. Private insurers through proper customer relationship management must understand customer requirements, satisfy the customers and create more distribution channels to reach out the customers. In the sophisticated world, people are increasingly becoming aware of their health, so there is a good potential for the insurance sector to grow in the future.

Asian Insurance Post (2013) in November issue had focused on the key challenges lying ahead of the life insurance industry in India. The life insurance industry must try to reach out the customers through social media and must provide updated information in the company's website as the internet penetration is high in India. The larger insurer will have to act upon multiple areas and the small insurers will have to tap the niche markets. The industry must give more focus to the end customers and must make the intermediaries to act upon the necessity of the clients. Thus it is at the onus of the life insurance industry to take requisite decisions to reach a stable position through coordinated efforts between insurers and regulatory body.

Subrahmanyam (2014) had enlisted the key performance indicators for an insurer in Indian scenario. The key goals of insurance companies are premium, number of policy holders, expenses, turnover, etc. While setting the goals, the management should consider the infrastructure, competition level and economic condition. The insurance agents must also help them to achieve the target in a specified time.

Objectives

1. To analyze the effects of foreign direct investment in the life insurance sector in India
2. To analyze the impact of foreign direct investment on the performance of life insurance companies in India
3. To analyze the impact of foreign direct investment on the investment decisions of the life insurance companies in India

Methodology

Type of study: It is a comprehensive and in-depth study about the performance of the life insurance companies in India, which are decade-old and have proved their worth in terms of performance and effective returns.

Sources of data: The required secondary data for the research have been collected from published information in the websites of IRDA, RBI, MEA, DIPP, FIPB, SEBI, IBEF and the websites of concerned insurance companies, newspapers, magazines, books, periodicals, research journals and reports.

Period of the study: The information about the performance of insurance companies in India was collected for a period of 13 years from April 2001 to March 2014.

Analysis And Interpretation

The following statistical tools of SPSS were employed to analyze the data and they are Analysis of Variance (ANOVA), Karl Pearson's Correlation and Simple Linear Regression.

(1) Analysis of Variance (ANOVA)

One way ANOVA was used to test variance among the year-wise inflow of foreign capital in the private sector life insurance companies in India. (Significance level, $\alpha = 0.05$)

H_0: There is no significant difference between foreign equity share capital inflows in the private sector life insurance companies.

H_a: There is significant difference between foreign equity share capital inflows in the private sector life insurance companies.

The result of ANOVA is presented in Table 1 below:

Table 1 Analysis of Variance of Foreign Equity Share Capital of Life Insurance Companies Over the Span of 10 Years

Year	Source of Variation	Sum of Squares	df	Mean Square	F- Value	p-value	Results
2004	Between Groups	39262.704	11	3569.337	4693.4	0.000	H_a accepted
	Within Groups	7.605	10	0.760			
	Total	39270.309	21				
2005	Between Groups	72751.429	11	6613.766	110.8	0.000	H_a accepted
	Within Groups	596.851	10	59.685			
	Total	73348.281	21				
2006	Between Groups	114857.793	11	10441.618	14.79	0.000	H_a accepted
	Within Groups	7055.750	10	705.575			
	Total	121913.543	21				
2007	Between Groups	177984.715	11	16180.429	15.88	0.000	H_a accepted
	Within Groups	10183.780	10	1018.378			
	Total	188168.495	21				
2008	Between Groups	317588.666	11	28871.697	6.89	0.002	H_a accepted
	Within Groups	41867.048	10	4186.705			
	Total	359455.714	21				
2009	Between Groups	591040.058	11	53730.914	9.08	0.001	H_a accepted
	Within Groups	59126.485	10	5912.649			
	Total	650166.544	21				
2010	Between Groups	662359.074	11	60214.461	6.98	0.002	H_a accepted
	Within Groups	86261.242	10	8626.124			
	Total	748620.316	21				
2011	Between Groups	620457.732	11	56405.248	3.88	0.021	H_a accepted
	Within Groups	145289.442	10	14528.944			
	Total	765747.173	21				
2012	Between Groups	508217.940	11	46201.631	3.91	0.020	H_a accepted
	Within Groups	118100.127	10	11810.013			
	Total	626318.067	21				
2013	Between Groups	588427.030	11	53493.366	2.88	0.053	H_0 accepted
	Within Groups	185575.351	10	18557.535			
	Total	774002.382	21				
2014	Between Groups	565412.970	11	51401.179	2.46	0.084	H_0 accepted
	Within Groups	208969.587	10	20896.959			
	Total	774382.558	21				

Inference: The result indicated that foreign capital of private sector life insurance companies varied significantly from the year 2004 to 2012, but in 2013 foreign capital did not vary significantly. This implies that foreign capital increased gradually with increase in number of joint ventures in the life insurance sector.

(2) Correlation Analysis

Correlation analysis was used to test the relationship between insurance density and number of policies issued by private sector life insurance companies in India. The result of correlation analysis is presented in the Table 2 below:

Table 2 Correlation between insurance density and number of policies issued by life insurance companies over the span of 11 years

Insurance density vs. Number of policies issued by life insurance companies											
Year	**2003**	**2004**	**2005**	**2006**	**2007**	**2008**	**2009**	**2010**	**2011**	**2012**	**2013**
Pearson Correlation	0.941	0.948	0.952	0.971	0.987	0.985	0.997	0.997	0.998	0.979	0.985

Inference: The result indicated that correlation values were high in the years 2009, 2010 and 2011 which imply that number of policies issued by private sector life insurance companies were high which lead to high insurance density.

(3) Regression Analysis on Claims Incurred

Regression analysis was used to test foreign equity share capital influence on the claims incurred by private sector life insurance companies in India. (Significance level, $\alpha = 0.05$)

H_0: $\beta = 0$ (Foreign equity share capital is not a useful predictor of claims incurred by private sector life insurance companies.)

H_a: $\beta \neq 0$ (Foreign equity share capital is a useful predictor of claims incurred by private sector life insurance companies.)

The result of regression analysis is presented in the Table 3 below:

Table 3 Regression of Foreign Equity Share Capital on Claims Incurred by Life Insurance Companies in India

Sl. No.	Life Insurance Companies	R square value	p-value	Results
1	Ageon Religare	0.664	0.048	H_a accepted
2	Aviva	0.709	0.001	H_a accepted
3	Bajaj Allianz	0.698	0.001	H_a accepted
4	Bharti Axa	0.911	0.000	H_a accepted
5	Birla Sunlife	0.690	0.001	H_a accepted
6	Canara HSBC	0.972	0.000	H_a accepted
7	DLF Pramerica	0.517	0.017	H_a accepted
8	Edelweiss Tokio	0.277	0.647	H_0 accepted
9	Exide Life	0.047	0.497	H_0 accepted
10	Future Generali	0.832	0.004	H_a accepted
11	HDFC Standard	0.601	0.003	H_a accepted
12	ICICI Prudential	0.445	0.080	H_0 accepted
13	IDBI Federal	0.662	0.026	H_a accepted
14	Indiafirst	0.639	0.015	H_a accepted
15	Kotak Mahindra	0.672	0.001	H_a accepted
16	Max Life	0.783	0.000	H_a accepted
17	PNB Metlife	0.845	0.000	H_a accepted
18	Reliance	0.807	0.000	H_a accepted
19	SBI Life	0.510	0.009	H_a accepted
20	Shriram Life	0.274	0.148	H_0 accepted
21	Star Union Dai-ichi	0.197	0.378	H_0 accepted
22	TATA Aia	0.852	0.000	H_a accepted

Inference: The result indicated that foreign capital is a useful predictor of claims incurred by seventeen private sector life insurance companies except for five of them, viz., Edelweiss Tokio (0.277), Exide Life (0.047), ICICI Prudential (0.445), Shriram Life (0.274) and Star Union Dai-ichi (0.197).

(4) Regression Analysis on Assets under Management

Regression analysis was used to test foreign equity share capital influence on the assets under management of private sector life insurance companies in India. (Significance level, $\alpha = 0.05$)

H_0: $\beta = 0$ (Foreign equity share capital is not a useful predictor of asset under management of private sector life insurance companies.)

H_a: $\beta \neq 0$ (Foreign equity share capital is a useful predictor of claims incurred asset under management of private sector life insurance companies.)

The result of regression analysis is presented in the Table 4 below:

Table 4 Regression of Foreign Equity Share Capital on Assets under Management by Life Insurance Companies in India

Sl. No.	Life Insurance Companies	R square value	p-value	Results
1	Ageon Religare	0.952	0.001	H_a accepted
2	Aviva	0.970	0.000	H_a accepted
3	Bajaj Allianz	0.733	0.000	H_a accepted
4	Bharti Axa	0.963	0.000	H_a accepted
5	Birla Sunlife	0.822	0.000	H_a accepted
6	Canara HSBC	0.908	0.003	H_a accepted
7	DLF Pramerica	0.623	0.042	H_a accepted
8	Edelweiss Tokio	0.380	0.874	H_0 accepted
9	Exide Life	0.045	0.510	H_0 accepted
10	Future Generali	0.948	0.000	H_a accepted
11	HDFC Standard	0.703	0.001	H_a accepted
12	ICICI Prudential	0.545	0.006	H_a accepted
13	IDBI Federal	0.897	0.001	H_a accepted
14	Indiafirst	0.582	0.034	H_a accepted
15	Kotak Mahindra	0.682	0.001	H_a accepted
16	Max Life	0.751	0.000	H_a accepted
17	PNB Metlife	0.879	0.000	H_a accepted
18	Reliance	0.542	0.006	H_a accepted
19	SBI Life	0.593	0.003	H_a accepted
20	Shriram Life	0.060	0.525	H_0 accepted
21	Star Union Dai-ichi	0.404	0.175	H_a accepted
22	TATA Aia	0.865	0.000	H_a accepted

Inference: The result indicated that foreign capital is a useful predictor of assets under management by nineteen private sector life insurance companies except for three of them, viz., Edelweiss Tokio (0.38), Exide Life (0.45) and Shriram Life (0.06).

Findings

The important findings of the present study are:

1. Life insurance sector has a premium base of USD 105.47 billion in India.
2. LIC issues more number of policies every year than the total number of policies issued by all 23 private life insurers in India.
3. Private life insurance companies have the highest percentage increase in the number of policies issued every year when compared to LIC (compared individually).
4. Sahara India Life Insurance has the entire equity share capital owned solely by the Indian promoters without any foreign direct investors' intervention.

5. LIC is paying more commission than the private sector life insurance companies (compared individually) and hence, there are more agents LIC.
6. LIC is receiving more complaints than private sector life insurance companies.
7. Both LIC and private sector life insurers' grievance resolving capacity had tremendously increased over the years due to the efforts of ombudsman and IRDA in providing a good redressal support to the clients.
8. LIC holds shares of worth Rs. 2.33 lakh crores in all the Nifty companies put together.
9. With an aim to boost trade, Bangladesh offered to establish Special Economic Zones (SEZs) for Indian companies besides allowing LIC to start operation in the country.
10. None of the private sector insurance companies provides loans to the public. However, LIC is the largest provider of personal loans to the public than all other high street banks taken together.

Suggestions

The suggestions given out of the present study are:

1. Increase in foreign direct investment slab in the insurance sector will allow more capital inflow for the private sector insurers, which would help them to meet out their operational cost and develop new models for reaching out the untapped niche markets in the country.
2. The insurance companies must reduce its dependence on traditional model of consultative selling of the insurance policies. They must try to adopt online and mobile-based insurance approach.
3. In order to improve insurance penetration, the Government has to provide financial education, understanding about insurance products and improve the propensity to purchase insurance products based on its premium and returns.
4. The Government of India must take initiatives to popularize the 'Insurance Portability' concept all over the country. It provides an equal field to all the insurance companies and the customers can compare and choose the products offered by different insurers.
5. Insurance companies can make use of e-distribution platforms to provide online insurance policies, reach customers easily and receive premiums thus reducing the effort and cost involved in developing a physical distribution network.
6. The business data of the insurance companies must be collected and processed in an orderly manner and made available at regular intervals.
7. The insurance industry must light up the micro-insurance penetration in India by changes in the regulatory framework and technology led innovations.

Conclusion

In the road to become a developed nation, India must financially empower its citizens. One such way of empowering its people is to provide risk protection or insurance cover for their life. Providing insurance cover to 1.2 billion people is not a 'one-man show'. This can be achieved through combined and collaborative efforts of the government, private companies and regulators. Insurance penetration and density are still at an alarmingly low level compared to the developing countries. The main reasons are lack of awareness about insurance among the consumers, the distribution network, regulatory framework and policies of the government. Increasing the foreign equity slab should encourage further capital employment and ease out the operational cost. Foreign direct investment in the insurance sector is a long-term process and it is very important that the government, investors and public have patience to attain the investment objectives.

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