Changing Horizon of Insurance Sector

The insurance landscape in India is undergoing a major change. With the re-opening of the sector, several new players have entered the scene, offering plethora of professional opportunities. It's high time for the professionals to take note of it and update themselves with the latest goings on in this arena. This article is an attempt in that direction.

—Sam Ghosh

Ensconced in a monopoly run from the nationalization days beginning in 1956, the insurance industry has indeed awakened: to a deregulated environment in which several private players have partnered with multinational insurance giants.

However, despite its teeming one billion population, India still has a low insurance penetration of 1.95 per cent, 51st in the world. Despite the fact that India boasts a saving rate of around 25 per cent, less than 5 percent is spent on insurance. But there is indeed a great potential for the sector in India as well as those looking for brighter professional opportunities.

Looking Ahead

Today, a combination of the upsurge in consumer awareness and other developments has put the insurance sector under pressure. The lifting of the bar on composite insurance, where companies are allowed to do only life or non-life business today, can also be expected. And thus, instead of categorizing insurance by class, the focus may shift more to the period for which the cover was offered and the risk underwritten. Already, there is a demand for permitting the industry to underwrite pure risk and leaving investment decisions to policyholders.

The four main challenges facing the industry are product innovation, distribution, customer service, and investments. Unit-linked personal insurance products might find greater acceptability with rising customer awareness about customized, personalized and flexible products.

The increasingly tough competition has actually changed the rules of the game. The market is flooded with an array of products. In such a scenario, the differentiators among different players are the products, pricing, and service. Meanwhile, the profile of the Indian consumer is also evolving. Consumers are increasingly more aware and are actively managing their financial affairs. Today, while boundaries between various financial products are blurring, people are increasingly looking not just at products, but also at integrated financial solutions that can offer stability of

The author is the CEO, Bajaj Allianz Life Insurance Company Ltd. & Country Manager Allianz AG. He can be reached at shipra.alam@bajajallianz.co.in

returns along with total protection.

To cater to these myriad needs of customers, insurance products need to be further customized. Insurance today has emerged as an attractive and stable investment alternative that offers total protection — Life, Health and Wealth. In terms of returns, insurance products today offer competitive returns ranging between 7% and 9%. Besides returns, what really increases the appeal of insurance is the benefit of life protection from insurance products along with health cover benefits.

Consumers today also seek products that offer flexible options. The customers now prefer products with benefits unbundled and customisable to suit their diverse needs.

Further, the trends of the developed economies where people not only live longer but also retire earlier are now catching up in India too. Earlier, the fear of an early death primarily necessitated Insurance today the fear is also of outliving one's assets in the wake of living too long. With the breakdown of traditional forms of social security like joint family system, consumers are now focusing on the needs of a comfortable retired life. The long-term decline in interest rates has further pushed this trend.

This all adds up to major change in demand for insurance products. While sale of traditional life insurance products like individual, whole life and term will remain popular, the new products like single premium, investment linked, retirement products, variable life and annuity products will also rise in the times to come. Firms will need to constantly innovate in terms of product development to meet ever-changing consumer needs. However, product

innovations are quickly and easily cloned and pricing will also not vary significantly, with most product premiums hovering around a narrow band.

In this backdrop, a key difference will be the customer experience that each life insurance player can offer, in terms of quality of advice on product choice, policy servicing as well as settlement of claims. Long-term growth in business will depend greatly on distribution network where the emphasis must not only be just on selling insurance but also on acting as financial advisors. This calls for a strong focus on training of the distribution force to act as financial consultants and build a long lasting relationship with customer.

The intermediaries

The intermediaries in insurance business and the distribution channels used by carriers will perhaps be the strongest drivers of growth in the sector. Multi-channel distribution and marketing of insurance products will be the smart strategy for the Indian market. While tied agents will continue to play an important role in distribution, alternative channels like corporate agents, brokers, and bancassurance will play a greater role in distribution. Firms will need to forge relationships with the partners for strategic advantage. They need to have strong partner relationship management. For example, local partners may have strong distribution channel in their line of business. That can be used to sell insurance also in a cost-effective manner.

The time has come for the industry to gradually move from traditional individual agents towards new distribution channels. There are 850,000 insurance agents in India and the qualitative selection of agents by companies is imperative to gain the cutting edge.

Work-site marketing

Relatively inexpensive and easy to launch, the work-site marketing is one potential distribution channel. In this scenario, sale of financial products and other services to employees is done through workplace-participation and is entirely on a voluntary basis where the employee pays for the products generally through a payroll deduction. Companies must constantly explore avenues to increase the number of distribution channels through a variety of distribution patterns, particularly given the rapidly changing customer profile. Traditional intermediaries have played a very important role as a distribution outlet for insurance services and products. The Internet and telemarketing will play an increasingly critical role in customer relationship.

Banc assurance is an effective and upcoming distribution channel

for Insurance products and companies. In countries like Italy, France and Spain, insurance companies have taken advantage of customers' typical loyalty to single banks and pattern of long-term banking relationships by successfully selling their products through these banks. Here banks can leverage their existing resources and earn supplementary fees while widening their range of available services.

At present, 12% of the world's insurance products are sold through the Internet, a figure likely to grow exponentially with a likely increase in customer usage of the Internet. Rural and semi urban sectors are the ones that could be serviced by the banc assurance model. However, there are some reservations against the efficacy of insurance distribution through public sector banks as these banks do not have deep relationships with their customers.

Other approaches, like call-centre, direct marketing, and the Internet will grow dramatically in importance over the next several years and will enable firms to acquire, retain and build loyalty among customers while lowering transaction costs.

A customer accessing any channel should be recognized as a client and not required to provide information again. What's more, a client should be able to move easily from one mode of service to another (for example, from on-line to face-to-face to on-line) without disruption in service.

The Challenges

The four main challenges facing the industry are product innovation, distribution, customer service, and investments. Unit-linked personal insurance products might find greater acceptability with rising customer awareness about customized, personalized and flexible products. Flexible products and new technology will play a crucial role in reducing the cost and, therefore, the price of insurance products. Finding the niche markets, having the right product mix through add-on benefits and riders, effective branding of products and services and product differentiation from competitors' offering will be the key challenges for the new companies.

IT in Insurance

In today's highly competitive financial services environment, effective organizations employ technology in a strategic role to achieve competitive edge. Technology plays an increasing role in aiding design and administering of products, as well in efforts to build life-long customer relationships.

At the same time, technology investment will only help as long as firms find the right people: people with the right attitude, values, and ethics, commitment to excellence, and focus on customer service. The critical success factor is a top-down emphasis on exceeding customer expectations with quality people, excellent products, and legendary service.

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Rural-Urban Mix

It must be borne in mind that India is a predominantly rural country and will continue to be so in near future. New players tend to favour the "creamy" layer of the urban population. But, in doing so, they are missing a large chunk of the insurable population. A strong case in point is the current business composition of predominant market leader – the Life Insurance Corporation of India. The lion's share of its new business comes from the rural and semi-rural markets. In a country of 1 billion people, mass marketing is always a profitable and cost-effective option for gaining market share. The rural sector is a perfect case for mass marketing.

Competition in rural areas tends to be "kinder and gentler" than that in urban areas, which can easily be termed cutthroat.

Rural insurance should be looked upon as an opportunity and not an obligation. A smaller bundle of innovative products in sync with rural needs and perception and an efficient delivery system are the two aspects that have to be developed in order to penetrate the rural markets.

Impending Reforms

Pension reforms: The two issues that urgently need to be addressed are the escalating burden of the unfunded government pension and the coverage for building retirement income for the non-salaried workforce. The Insurance Regulatory Development Authority - the regulatory authority in Insurance, has already submitted a road map for

pension reforms to the government. The new pension authority would fix the minimum capital requirement for new entrants including mutual funds and banks. Players would need to convince potential of their long-term commitment and responsibility and make known all components of options they intend to offer in pension products.

Some feel that in order to maximize pension fund efficacy, management should be given over to insurance carriers, banks, and mutual funds. They also recommend against auctioning the management of Pension Funds, proposing instead that entities with impeccable reputations, experience, and financial strengths should be entrusted with this important task.

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Health insurance: This is one area where India does not have much progress to date.

Conclusion

Competition will surely cause the market to grow beyond current rates, create a bigger "pie" and offer additional consumer choices through the introduction of new products, services, and price options. Yet, at the same time, public and private sector companies have to work together to ensure healthy growth and development of the sector. Challenges such as developing a common industry code of conduct, contributing to a common catastrophe reserve fund, and chalking out agreements between insurers to settle claims to the benefit of the consumer will require concerted effort from both sectors. ■

ANNOUNCEMENT

FOR THE INFORMATION OF THE MEMBERS

Treatment of inter-divisional transfers

Attention of the members is invited to the definition of the term 'revenue' in Accounting Standard (AS) 9, Revenue Recognition, issued by the Institute of Chartered Accountants of India, which is reproduced below:

> *"Revenue* is the gross inflow of cash, receivables or other consideration **arising in the course of the ordinary activities of an enterprise** from the sale of goods, from the rendering of services, and from the use by others of enterprise resources yielding interest, royalties and dividends. Revenue is measured by the charges made to customers or clients for goods supplied and services rendered to them and by the charges and rewards arising from the use of resources by them. In an agency relationship, the revenue is the amount of commission and not the gross inflow of cash, receivables or other consideration." (emphasis supplied)

The use of the word 'enterprise' in the definition of the term 'revenue' clearly implies that the transfers within the enterprise cannot be considered as fulfilling the definition of the term 'revenue'. Thus, the recognition of inter-divisional transfers as sales is an inappropriate accounting treatment and is inconsistent with Accounting Standard (AS) 9, Revenue Recognition. This aspect is further strengthened by considering the recognition criteria laid down in AS 9. Paragraphs 10 and 11 of AS 9, reproduced below, provide as to when revenue from the sale of goods should be recognised:

> ***"10. Revenue from sales or service transactions should be recognised when the requirements as to performance set out in paragraphs 11 and 12 are satisfied, provided that at the time of performance it is not unreasonable to expect ultimate collection. If at the time of raising of any claim it is unreasonable to expect ultimate collection, revenue recognition should be postponed.***
>
> ***11. In a transaction involving the sale of goods, performance should be regarded as being achieved when the following conditions have been fulfilled:***
>
> ***(i) the seller of goods has transferred to the buyer the property in the goods for a price or all significant risks and rewards of ownership have been transferred to the buyer and the seller retains no effective control of the goods transferred to a degree usually associated with ownership; and***
>
> ***(ii) no significant uncertainty exists regarding the amount of the consideration that will be derived from the sale of the goods."***

Since in case of inter-divisional transfers, risks and rewards remain within the enterprise and also there is no consideration from the point of view of the enterprise as a whole, the recognition criteria for revenue recognition are also not fulfilled in respect of inter-divisional transfers.