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A study of foreign direct investment in Indian insurance industry

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Abstract
Insurance Laws (Amendment) Bill, 2021 approved by Lok Sabha on 22 March 2021 and Rajya Sabha on 18 March 2021. The bill proposes to revise India's insurance legislation. The measure also aims to eliminate antiquated restrictions from earlier legislation and adapt current insurance business methods in a changing, dynamic environment that incorporates private involvement. Foreign investment is estimated to contribute 20,000-25,000 crores. The measure raises the FDI ceiling in the insurance industry to 74% from 49%. Foreign direct investment, foreign venture capital, and foreign portfolio investment would all include foreign insurance investment. Insurance firms may raise money using non-equity instruments. The insurance industry helps transfer national savings into other economic sectors. FDI in insurance can satisfy India's long-term cash needs to develop infrastructure. The current study examines the Indian insurance business, its prospects owing to FDI, and its significant difficulties.

Keywords: Insurance sector, FDI, insurance laws, IRDAI, life insurance

1. Introduction

In our nation, the insurance industry has gone through three stages: non-regulation during the British era and the immediate post-independence period, regulation during the post-independence period, and deregulation during the present phase. Numerous insurers have entered the insurance market during the present period of deregulation, leading to a considerable increase in business along with fierce rivalry amongst insurers. Even after liberalization, state-sector insurance firms hold over 90% of the market share. The insurance industry helps transfer national savings into other economic sectors. India's insurance penetration will rise as a result of FDI in the insurance sector, which may also help India satisfy its long-term financial needs for infrastructure development. Since the insurance industry is the only one where individuals invest money for up to 30 years or more, it has the potential to raise long-term capital from the general public. Indirectly, the Indian economy would benefit from increased FDI in the insurance sector. With significant premium growth in the non-life insurance market, the insurance industry has also been growing quickly. The amount of FDI coming into the nation has increased over time. However, India has a huge potential for absorbing more FDI in the years to come. It is vital to the development of emerging countries. IRDA favours increasing foreign ownership in insurance joint ventures.

2. Insurance industry in India – overview

A contract for insurance is an agreement between two parties, the insurer and the assured, in which the insurer promises to pay the assured a sum of money or its equivalent upon the occurrence of a certain event, in exchange for payment of a premium. The purpose of all insurance is to protect against risks that threaten human life and business. In order to avoid disasters for themselves, those who seek it try to place the risk of losses on the shoulders of others who are willing to do so in exchange for financial gain. In the case of life insurance, they try to guarantee their dependents a certain level of support in the event of their passing or to set up a fund from which their debts can be paid off.

The history of insurance in India is very old; even it is mentioned in Manusmrithi and Kautilya Arthasastra. The first Life insurance company in India was established in the year 1818, "Oriental Life Insurance Company", in Kolkata. But this company could not run much and it failed in 1834.

In the year 1870, the first Indian life insurance company was started in the country, whose name was Bombay Mutual Life Assurance Society. In the year 1938, Insurance Act 1938 was passed to protect the insurance interests of the public and to control the insurance business in the country.

The voice for nationalization of the insurance business in the country was being made since 1944, as a result, on January 19, 1956; the life insurance business was nationalized in India. The work of nationalization was done in two phases, in the first phase the management of the companies was taken by the government through an ordinance and in the second phase the ownership of the companies would also be taken by the government through a comprehensive bill. The Life Insurance Act of India was passed by the Parliament of the country on 19 June 1956 and the Life Insurance Corporation of India was established on 1 September 1956. Thus, one hundred fifty four Indian insurance companies, sixteen non-Indian insurance companies and seventy five provident fund societies (a total of 270 Indian and foreign insurance companies) operating in India were merged with LIC.

"In 1972 with the passing of the General Insurance Business (Nationalisation) Act, general insurance business was nationalized with effect from 1st January, 1973. One hundred seven insurers were amalgamated and grouped into four companies, namely National Insurance Company Ltd., the New India Assurance Company Ltd., the Oriental Insurance Company Ltd and the United India Insurance Company Ltd. The General Insurance Corporation of India was incorporated as a company in 1971 and it commence business on January 1st 1973" [1].

On the recommendations of the Malhotra Committee, to regulate and develop the insurance industry Insurance Regulatory and Development Authority of India (IRDAI) was formed in April 2000 under the Insurance Regulatory and Development Authority of India Act, 1999. The establishment of IRDAI was a historic move in the insurance sector of India. The purpose of establishing IRDAI was to make such a statutory body that regulates the insurance sector and promotes competition in the insurance industry of the country so that the people of the country can get good insurance products at low cost.

3. FDI in insurance industry

Even after 40 years of nationalization of insurance business in the country, only 25% of the insurable population is covered under insurance. LIC had a monopoly on the country's life insurance business till the end of the 90s, after that the insurance sector was opened to private insurance companies in the year 2000 by the Government of India with the objective of increasing insurance penetration and insurance density in the country (new economic policy i.e. liberalization, privatization and globalization). For the first time in India, the insurance sector was opened to private companies by the Atal Bihari Vajpayee government in August 2000. Private sector firms were allowed by the government to set up insurance companies and allowed FDI of 26%.

The country's insurance industry has been demanding to increase the Foreign Direct Investment (FDI) limit for a long time. In the year 2015, this limit was increased from 26 per cent to 49 per cent by the Narendra Modi government in its first term (2014-2019). It was the beginning of a new chapter in the Indian insurance business

The country's first paper Union Budget for the year 2021-22 was presented by Finance Minister Nirmala Sitharaman on Monday, in which she proposed to increase the foreign direct investment limit from 49 per cent to 74 per cent in Indian insurance companies. In order to attract more FDI in the country's insurance industry, on March 2021, bypassing the Insurance Amendment Bill in the Rajya Sabha and Lok Sabha the limit of FDI in insurance companies was increased from 49 per cent to 74 per cent. IRDAI was in favor of the amended bill (increases the foreign equity capital)

4. Benefits of increase of FDI

4.1 Increased Insurance Penetration: At present the population of India is about 140 crores. Considering such a huge population, it can be said that there is a great need for insurance in the country. Insurance penetration in our country is 3% while in developed country like Japan it is around 10%. With the increase of FDI in the insurance industry, the competition will also increase, thus the customers will get good insurance products at low prices. In such a situation, there will definitely be more investment in the insurance industry by the customers and there will also be an increase in insurance penetration in the country.

4.2 Level Playing Field: A large part of the country's insurance industry is dominated by public insurance companies. After increase in FDI, adequate funds will be available with private insurance companies and they will be able to give tough competition to public insurance company.

4.3 Increased Capital Inflow: Many private insurance companies operating in the country are running at a loss and are troubled by the lack of capital, in such a situation, the increase in FDI will allow sufficient capital to flow into these companies.

4.4 Job Creation: Due to the inflow of capital in private insurance companies, their business will increase, as a result, employment opportunities will also increase in the country.

4.5 Consumer Friendly: The final benefit of FDI will be received by the customers, as new companies coming into the market will increase the competition, as a result of which customers will get better facilities, cheaper insurance products will be available and claim settlement will be completed in less time.

4.6 Effect on Economy: Due to the increase in FDI limit, more foreign capital will flow into the country than before. The demand for Indian currency will increase in the international currency market, as a result of which the exchange rate of rupee to dollar will decrease. The reduction in the exchange rate will have a direct impact on the common man as it will reduce the cost of imported goods. As a final effect of this, the foreign exchange reserves of the country will increase.

5. Disadvantages in the of increase of FDI

Due to the increase in the ceiling limit, small companies may fear that they will not be able to compete with multi-national companies, so they can leave the market. In addition, the government may find it difficult to exercise control over the functioning of such companies due to the management and controlling stake.

6. Review of literature

Ahlawat and Bansal (2016) [3] found in their study that the Indian insurance industry is far behind from insurance industry of developed countries. Increasing in FDI limit (Insurance Amendment Bill 2015) will increase the number of private players in the field of insurance and the public will get better products and services at a cheaper price. But it should be ensured that the investment is for a long time period and all profit does not transfer outside India.

Gattaiah (2017) [5] studied the relationship between the premium income of public and private life and Non-life insurance companies working in India by application of a t-test. He found in his study that there is no significant relation between the premium income of public and private life insurance companies because the calculated t-value (1.957) is less than the critical value (2.145). As per the second hypothesis of the paper again, there is no significant relation in the growth rate of total insurance premium income of public and private non-life insurance companies because the calculated t-value (0.807) is less than the critical value (2.447).

Yadav and Mohania (2016) [11] concluded in their study that increases in FDI limits definitely increase insurance penetration and insurance density in India. Entry of new private players will increase the competition, as a result, the public will get better products and services at affordable prices. Apart from this due to increase demand in the insurance market, they require more employees which will increase employment in the country. Further, they said the Reserve Bank of India and the Insurance Regulatory and Development Authority of India need to keep eye on the outflow of Indian currency.

Hasan (2015) [13] study shows that regulatory changes (Insurance Amendment Bill 2015) in the insurance industry will give a positive impact on the growth of the Indian insurance industry and the economy. With the participation of foreign players, the insurance sector will get the new best know-how and implement the best practices. Further, he said it is a possibility that without providing participation in management and control they would be less interested to invest in the Indian insurance market.

Jadhav (2018) [18] studied in his paper about guidelines for FDI in the insurance market of India, the advantages and disadvantages of increasing FDI and issues related to FDI in India. As per the author, the Insurance Amendment Bill 2015 will help the insurance sector to face the competition at the international level and it helps the companies to raise funds for their future plan. Lastly, the customer will get the benefit of the competitive market in the form of new products and better services.

7. Objectives

The main objective of the study is to analyze the role that FDI in the progress of the insurance business in India and the current trend of the FDI in the Indian insurance sector.

8. Research methodology

The information and data for the current study have been obtained from the Insurance Act, 1938, the Insurance Regulatory and Development Authority of India Act, 1999, The Insurance (Amendment) Bill, 2015, The Insurance (Amendment) Bill, 2021, Annual Report of the IRDAI. The information thus collected has been supplemented by other details available on the websites, Journals and other research articles/ Studies published in various Journals/ books. The sample size is less than 30, therefore t-test is applied to analyse the significant difference in the mean value of the two samples.

9. Hypothesis

H_0: There is no significant difference in the mean value of Share of Foreign Promoters (FDI) of Life and Non-Life insurance companies.

10. Data analysis and interpretation

When an individual or a company invested money in the business of another foreign country, such investment is known as Foreign Direct Investment (FDI). After opening up the insurance sector for private players investments made by the foreign promoters in the share of insurance companies are shown in table no. 1.

Table 1: FDI in Equity Share Capital (Rs. Crore)

Year	Life Insurance Sector			Non-life Insurance sector		
	Total Equity Share Capital	Share of Foreign Promoters	FDI Ratio (%)	Total Equity Share Capital	Share of Foreign Promoters	FDI Ratio (%)
2000-01	864.00	184.65	24.36	1511.5	92.3	6.12
2001-02	1669.00	235.55	25.86	1731.50	149.5	8.64
2002-03	2234.13	563.44	25.22	1938.00	175.76	9.07
2003-04	3243.71	782.34	24.12	2363.96	246.21	10.42
2004-05	4352.81	1053.94	24.21	2513.96	246.21	9.79
2005-06	5892.05	1355.34	23.01	3214.01	333.52	10.38
2006-07	8124.41	1809.74	22.28	3485.87	364.53	10.46
2007-08	12296.42	2821.63	22.95	4090.85	493.26	12.06
2008-09	18254.77	4354.51	23.86	4829.90	676.62	14.01
2009-10	21020.00	5053.58	24.04	5684.67	896.32	15.77
2010-11	23661.85	5723.81	24.19	6705.89	1,090.08	16.26
2011-12	24931.92	6324.26	25.37	7826.10	1,324.45	16.92
2012-13	25518.72	6045.9	23.69	9519.65	1,586.63	16.67
2013-14	25938.51	6113.36	23.57	10240.21	1,678.86	16.56
2014-15	26239.55	6187.24	23.98	11504.31	1,987.21	16.89
2015-16	26691.46	7498.63	28.09	12603.39	2462.99	19.54
2016-17	26956.94	9353.32	35.44	13127.82	3503.54	26.69
2017-18	27264.38	9565.95	35.09	14,970.69	3,805.30	25.42

2018-19	27615.94	9764.20	35.36	17664.00	4045.63	23.66
2019-20	28087.96	10507.07	37.41	21,360.73	4275.79	20.02
2020-21	28,346.37	10,045.17	35.44	33,719.44	4,425.24	13.12
2021-22	35,546.75	11,371.59	31.99	38,732.29	3,614.14	9.33

Source: Annual Report of IRDAI

FDI Ratio = Ratio of Share of Foreign Promoters to Total Equity Share Capital
The average FDI ratio in the life insurance business during 2001-01 to 2014-15 was 24.05%. After the Insurance Amendment Bill 2015, average FDI ratio in the life insurance business increased to 19.68%. One important point is that after 2018-19, FDI ratio in the life insurance business is decreasing. It's come down from 37.41% to 31.99% in the last three years (2018-19 to 2021-22).
The average FDI ratio in Non-life insurance business during 2001-01 to 2014-15 was 12.67%. After the increased in FDI limit (Insurance Amendment Bill 2015), average FDI ratio in Non-life insurance business increased to 19.68%. One notable point is that after 2016-17, FDI ratio in the Non-life insurance business is continuously decreasing. It's come down from 26.69% to 9.33% in the last six years (2016-17 to 2021-22). Therefore, it can be said that the FDI ratio of the insurance industry has decreasing trend in the last three years. The reason behind the decreasing FDI ratio was Covid-19 pandemic that had stopped many projects and investments.

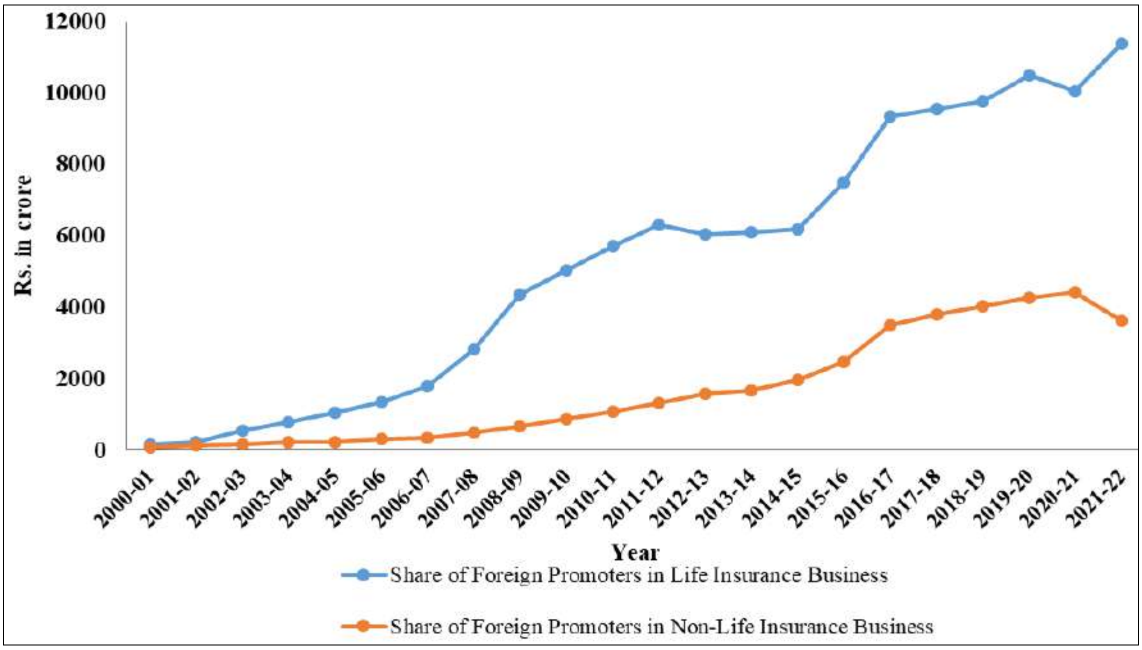

Chart 1: Share of Foreign Promoters in Insurance Industry

11. Testing of hypothesis

To test the hypothesis, "there is no significant difference in the mean value of Share of Foreign Promoters (FDI) of Life and Non-Life insurance companies", t-test was applied. The following are the results of t-test

Table 2: Descriptive Statistics

	N	Mean	Std. Deviation	Std. Error Mean
FDI Ratio of Life Insurance Sector	22	27.2514	5.13626	1.09505
FDI Ratio of Non-Life Insurance Sector	22	14.9000	5.64984	1.20455

Table 3: Independent Samples Test

	Levene's Test for Equality of Variances		t-test for Equality of Means						
	F	Sig.	t	DF	Sig. (2-tailed)	Mean Difference	Std. Error Difference	95% Confidence Interval of the Difference	
								Lower	Upper
Equal variances assumed	.067	.797	7.587	42	.000	12.35136	1.62791	9.06611	15.63661
Equal variances not assumed			7.587	41.624	.000	12.35136	1.62791	9.06523	15.63749

The Mean Score of FDI Ratio of Life Insurance Sector is 27.2514 whereas it is 14.90 for Non-Life Insurance Sector. It signifies that FDI in Life Insurance Sector is significantly higher than the Non-Life Insurance Sector. Further the mean value of share of Foreign Promoters (FDI) of Life and Non-Life Insurance Companies has been measured at significance level of 0.05, which is found to be significant. The p-value is 0.00 which is less than the critical level of 0.05. It signifies the rejection of null hypothesis and accepting the alternative hypothesis. Hence it can be observed that there is significant difference in the mean value of Share of Foreign Promoters (FDI) of Life and Non-Life Insurance Companies.

12. Conclusion

The Insurance industry of the country had been demanding for a long time to increase the FDI limit in the insurance sector. The Government of India has increased the FDI limit from 49 per cent to 74 per cent by passing the Insurance Amendment Bill, 2021. As a result of the Insurance Amendment Bill 2021, foreign players will get participation in the management and control of the insurance business in India therefore they will be more interested to invest in India. With the entry of new private players in the insurance market the competition will increase, as a result, people will get new insurance products, insurance claims will be settled on time, people will get better services, insurance products will be available at an affordable price and employment opportunity will be generated in the country. Due to the above advantages, people will be interested to buy more insurance products that will directly help in increasing the Insurance penetration and insurance density in the country. In conclusion, it can be said that increasing the FDI limit is a welcome step, it will not only help in the growth and development of the insurance industry but also the development of the economy of the country.

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