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PROBLEMS WITH MICROINSURANCE IN INDIA IN 2015

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ABSTRACT
India is enjoying rapid growth and benefits from a young population. Its middle class is growing rapidly but 70 percent of the population is still rural, often very poor, and handicapped by poor health and health services, and low literacy rates. What happens when a poor family's breadwinner dies, when a child in a disadvantaged household is hospitalized, or the home of a vulnerable family is destroyed by fire or natural disaster? Every serious illness, every accident and every natural disaster threatens the very existence of poor people and usually leads to deeper poverty. These highlight the need for micro insurance. Micro insurance is the term used to refer the insurance to the low income people as it is different from insurance in general where micro insurance is a low value product with less premium and benefits. Micro insurance can boost resources for the rural poor, governments and private sector. The entire economy gains as the insurance industry matures further as well. There is a need for micro insurance in India's poverty reduction strategy. Micro insurance is a tool for investment, savings and as a measure of social security. In India, liberalization of the economy and the insurance sector has created new opportunities for insurance to reach the vast majority of the poor, including those working in the informal sector. Market penetration is largely driven by supply, not demand. Micro insurance in India has valuable lessons for rest of the world, particularly in the regulation of the industry. Unlike micro lending -- the better-known side of micro finance -- micro insurance has been a hard sell among the world's poor. The reasons include lack of understanding of how insurance products work, the poor population's general reticence to part with what little financial resources they have, badly designed products and a shortage of localized risk management knowledge among providers. It increases the livelihood of the poor where they can eat well, have good health since they wouldn't have to save as much for emergencies.

KEYWORDS
micro insurance, liberalisation, premium, investment, penetration.

INTRODUCTION
Microinsurance is insurance with low premiums and low caps / coverage. In this definition, "micro" refers to the small financial transaction that each insurance policy generates. "General microinsurance product means health insurance contract, any contract covering the belongings, such as, hut, livestock or tools or instruments or any personal accident contract, either on individual or group basis, as per terms stated in Schedule-I appended to these regulations"; and "life microinsurance product" means any term insurance contract with or without return of premium, any endowment insurance contract or health insurance contract, with or without an accident benefit rider, either on individual or group basis, as per terms stated in Schedule-II appended to these regulations as those within defined (low) minimum and maximum caps. The IRDA's characterization of microinsurance by the product features is further complemented by their definition for microinsurance agents, those appointed by and acting for an insurer, for distribution of microinsurance products (and only those products). Microinsurance is a financial arrangement to protect low-income people against specific perils in exchange for regular premium payments proportionate to the likelihood and cost of the risk involved. The author of this definition adds that micro-insurance does not refer to: (i) the size of the risk-carrier (some are small and even informal, others very large companies); (ii) the scope of the risk (the risks themselves are by no means "micro" to the households that experience them); (iii) the delivery channel: it can be delivered through a variety of different channels, including small community-based schemes, credit unions or other types of microfinance institutions, but also by enormous multinational insurance companies, etc. Microinsurance is synonymous to community-based financing arrangements, including community health funds, mutual health organizations, rural health insurance, revolving drugs funds, and community involvement in user-fee management. Most community financing schemes have evolved in the context of severe economic constraints, political instability, and lack of good governance. The common feature within all, is the active involvement of the community in revenue collection, pooling, resource allocation and, frequently, service provision.Microinsurance is the use of insurance as an economic instrument at the "micro" (i.e. smaller than national) level of society. This definition integrates the above approaches into one comprehensive conceptual framework. It was first published in 1999, pre-dating the other three approaches, and has been noted to be the first recorded use of the term "microinsurance". Under this definition, decisions in microinsurance are made within each unit, (rather than far away, at the level ofgovernments, companies, NGOs that offer support in operations, etc.). Insurance functions on the concept of risk pooling, and likewise, regardless of its small unit size and its activities at the level of single communities, so does microinsurance. Microinsurance links multiple small units into larger structures, creating networks that enhance both insurance functions (through broader risk pools) and support structures for improved governance (i.e. training, data banks, research facilities, access to reinsurance etc.). This mechanism is conceived as an autonomous enterprise, independent of permanent external financial lifelines, and its main objective is to pool both risks and resources of whole groups for the purpose of providing financial protection to all members against the financial consequences of mutually determined risks.
The last definition therefore, includes the critical features of the previous three:
1. transactions are low-cost (and reflect members' willingness to pay);
2. clients are essentially low-net-worth (but not necessarily uniformly poor);
3. The essential role of the network of microinsurance units is to enhance risk management of the members of the entire pool of microinsurance units over and above what each can do when operating as a stand-alone entity.

LITERATURE REVIEW
The literature available on this subject is quite vast. Prathma Rajan (2011) gave a detailed understanding of the RSBY (Rastriya Swastya Bhima Yojana) scheme by conducting several rounds of interviews with both FINO and ICICI Lombard. Intense primary and secondary research was involved during the process to ensure unbiased analysis. Oscar Joseph Akotey, Kofi A. Osei, Albert Gemegah, (2011) investigated using the probit model indicates that premium flexibility, income level and nodal agency are significant determinants of micro-insurance demand. Insurance knowledge, expectation (trust) and marital status were also found to have positive and significant impact on the demand for micro insurance. The analysis showed that formal education is not a significant determinant; rather one's level of insurance knowledge has a positive and significant impact on micro-insurance demand Stefan Hochrainer, Reinhard Mechler, Daniel Kull, (2010) found that micro-insurance instruments may help low-income farming households better manage drought risk by smoothing livelihoods and reducing debt, thus avoiding poverty traps. Yet many obstacles to optimal design, viability and affordability of these schemes, are encountered. One of those is climate change and the authors find that changing drought risk under climate change would pose a threat to the viability of micro-insurance, as well as the livelihoods of people requesting such contracts. Micro- Insurance Regulation in the Indian Financial Landscape (2008) a report of M- CRIL says that conscious of the relatively recent experience of insurance regulation and the lack of its own capacity to implement a strong regulatory regime, the regulator – the Insurance Regulatory and Development Authority (IRDA) – has limited the scope within which micro-insurance may be offered. Roth, J & McCord, MJ (2008) in their book has been written for people who would like to know how agricultural insurance could play a role in improving the livelihoods of the rural poor. It will be useful for development agents such as donors, development banks and development workers in NGOs, co-operatives, credit unions and Microfinance Institutions (MFIs). They also analysed the successes, failures and challenges of providing agricultural micro-insurance in practice. Jim Roth and Gaby Ramm (2006) in a report of Federal Ministry for Economic

Cooperation and Development explores how microinsurance began in India, and gives reasons for its dynamism. It investigates into the supply and demand of micro-insurance in India, gives the various channels for distribution, gives an examination of social security in India and its relationship to micro-insurance.

OBJECTIVES OF THE STUDY

1. To explore the history of Micro insurance in India.
2. To study the challenges faced by Micro insurance.

For the purpose of the study various research articles, newspapers, journals, magazines and books have been used.

HISTORY OF MICRO INSURANCE

Historically in India, a few micro-insurance schemes were initiated by Nongovernmental Organizations (NGO) due to the need felt in the communities in which these organizations were involved or by the trust hospitals. These schemes have now gathered momentum partly due to the development of micro-finance activity, and partly due to the regulation that makes it mandatory for all formal insurance companies to extend their activities to rural and well-identified social sector in the country (IRDA 2000). As a result, increasingly, Micro-Finance Institutions (MFIs) and NGOs are negotiating with the for-profit insurers for the purchase of customized group or standardized individual insurance schemes for the low-income people. Although the reach of such schemes is still very limited-- -anywhere between 5 and 10 million individuals---their potential is viewed to be considerable. The overall market is estimated to reach Rs. 250 billion by 2008 (ILO2004). The insurance regulatory and development authority (IRDA) defines rural sector as consisting of (i) a population of less than five thousand, (ii) a density of population of less than four hundred per square kilometer, and (iii) more than twenty-five per cent of the male working population is engaged in agricultural pursuits. The categories of workers falling under agricultural pursuits are: cultivators, agricultural labourers, and workers in livestock, forestry, fishing, hunting and plantations, orchards and allied activities. The social sector as defined by the insurance regulator consists of (i) unorganized sector (ii) informal sector (iii) economically vulnerable or backward classes, and (iv) other categories of persons, both in rural and urban areas. The social obligations are in terms of number of individuals to be covered by both life and non-life insurers in certain identified sections of the society. The rural obligations are in terms of certain minimum percentage of total polices written by life insurance companies and, for general insurance companies, these obligations are in terms of percentage of total gross premium collected. In order to fulfill these requirements all insurance companies have designed products for the poorer sections and low-income individuals. Both public and private insurance companies are adopting similar strategies of developing collaborations with the various civil society associations. The presence of these associations as a mediating agency, or a nodal agency, that represents, and acts on behalf of the target community is essential in extending insurance cover to the poor. The nodal agency helps the formal insurance providers overcome both informational disadvantage and high transaction costs in providing insurance to the low-income people. This way micro-insurance combines positive features of formal insurance as well as those of informal insurance. In the absence of a nodal agency, the low resource base of the poor, coupled with high transaction costs gives rise to the affordability issue. Lack of affordability prevents their latent demand from expressing itself in the market. Hence the nodal agencies that organise the poor, impart training, and work for the welfare of the low-income people play an important role both in generating both the demand for insurance as well as the supply of cost-effective insurance.

PROBLEMS

1. Building and positioning a portfolio of microinsurance products is still not a priority. Both the insurers and their channel partners are struggling to analyse whether microinsurance can be an independent revenue generator or provide value add over their existing services. Microinsurance is seen by insurers as a “obligatory necessity”, rather than a profitable product category. The focus of the companies is towards achieving the IRDAmandated numbers,1 even at the cost of subsidising the products. As a consequence, companies develop simple term products (predominantly credit-life) with little innovation, and then wage price wars to somehow “push” the product to the low income segment. Since insurance companies do not require huge numbers to fulfill their mandatory rural business, they often partner with small and medium sized MFIs for their individual credit-life microinsurance products and with large MFIs for group credit-life policies. The commission earned by the aggregators (mostly small MFIs or cooperatives) from the sale of credit-life products does not constitute a substantial fee income for them. This has limited the interest of the aggregators in microinsurance. For the large MFIs, the interest is limited to insuring the portfolio at the lowest possible cost. Moreover, the MFIs do not see any potential benefit from the current microinsurance products, since these single benefit (life) products are inadequate to address the client demand for comprehensive insurance coverage. Also, the processes do not naturally “fit” with those of the agents. As long as these stakeholders are not sure of the benefits from microinsurance, they will remain apprehensive about diverting resources towards microinsurance operations.
2. Insurance companies (and other players involved in microinsurance product design) lack the mortality and riskrelated actuarial data for the target client segment. Moreover, in order to reduce documentation and simplify calculations, 4 they have adopted enrolment forms and formats that are unable to address all risk related queries. As a result, both actuaries and underwriters allocate higher risk weightage to microinsurance products, making them unaffordable and benefits unattractive to the clients. Moreover, the lack of interest from insurance companies is complemented by the lack of demand for customised solutions by the aggregators. As a result, insurers as well as the aggregators have not invested in adequate market research to ensure market “pull” for microinsurance products. Conventionally, insurance is sold as a long term risk hedging (or savings) tool through a combination of term insurance, annuities, endowments and unit linked investment funds. However, inter-organisational and intergeographical migration is prevalent in the target market segment approached by the microinsurance aggregators (MFIs and co-operatives). Furthermore, the association of clients with the MFIs is also often transient and short term. These factors make long term product horizons a challenge for microinsurance. Moreover, the current regulation incentives both aggregators and insurance companies to sell annual term policies, another reason for limited innovation in long term microinsurance products.
3. Insurance as a specific product category, requires dedicated resources and distribution channels. However, the variable revenue and projected income/client numbers cannot justify the fixed cost of administration and distribution of microinsurance in short term. Standalone microinsurance players, therefore, are practically non-existent. This is reinforced by the regulatory bias towards the partner-agent model, which promotes distribution through MFIs. This has culminated into two unfortunate trends. The MFIs have started bundling their credit products with the microinsurance; Microinsurance has become mandatory (or semi mandatory in instances) for the MFI clients, who are neither solicited about the real terms and benefits of the product, nor asked if they want it In a mature insurance market, differentiation is derived from the quality of service. In Indian microinsurance, however, marginal differences in price and commission remain the key differentiators. In the partner-agent model, firstly, the ultimate beneficiary and the nominee are different; and secondly, there is a huge imbalance in the institutional magnitude and negotiating power between the MFIs and the large insurance companies. The small MFIs lack the bargaining power and expertise to negotiate adequate product and process terms. Since, the large MFIs are interested only on low cost credit-life insurance, they negotiate with the insurers on the premium amount and cost sharing arrangements, rather than service quality. Hence, optimum service quality is neither negotiated nor ensured. The absence of customization and standardization of processes has led to high costs, absence of coordination between aggregators and insurers and poor service quality (e.g. turnaround time for pay-in, issuance, claim servicing, renewal etc.). Clarity about the rights and responsibilities, risks and cost sharing among the channel partners is also opaque due to lack of standardization in agreements.
4. The demand for insurance has remained latent across the globe. Insurance companies address the issue in three ways: 1. Invest heavily in product marketing (sometimes cloaked as financial education) for clients, as well as staff. 2. Bundle the insurance benefits with other attractive aspects, like savings, annuity and investment, to address the prominent demand for savings and investment. 3. Design effective staff incentive programs, in order to ensure adequate penetration and service quality. As the Indian microinsurance industry is young, it is still to realize and implement such focused product marketing, product design, and human resource management programmes. The small ticket size and insubstantial revenue (often resulting in short term losses) makes the players apprehensive of investing in such efforts.

SOME SUGGESTIONS

1. Leveraging existing network for micro-insurance
2. Linking micro credit with micro insurance
3. Human Resource is required to be trained to cover the huge untapped market.
4. There is a need for developing adequate feedback mechanisms.
5. IRDA should take initiatives in widening outreach of microinsurance products to the rural poor as providing microinsurance is a necessary and essential adjunct in the inclusive process.
6. Increasing the partnerships between MFIs, Government, and other societies to reach the under covered market.
7. Government Sponsored schemes
8. Community based programmes that pools funds (Refer best practice table)
9. Customer focused approach at the time of new product design.
10. Educating the market in their local languages through media, information kiosks, social meetings etc.
11. Designing the product that is operated in the particular microinsurance environment.
12. Minimizing the documentations and developing efficient, transparent claims processing systems.
13. Risk prevention strategies.
14. Product should be affordable to the poor.
15. Flexibility in premium

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