

Overview of the Indian Life Insurance Industry

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Summary

The life insurance industry in India, accounts for approximately 75% of the overall insurance industry premium, recorded a total premium of Rs. 458,809 crore in FY18 from Rs. 156,076 crore in FY07 at a CAGR of 10.3% during FY07-18 on account of rising popularity of insurance schemes as savings instruments, increasing awareness and emerging middle class preferences.

The public sector (LIC) has been the main driver of life insurance industry premium accounting for ~70% of total premium collected in FY18, and the private sector share has been ~30%.

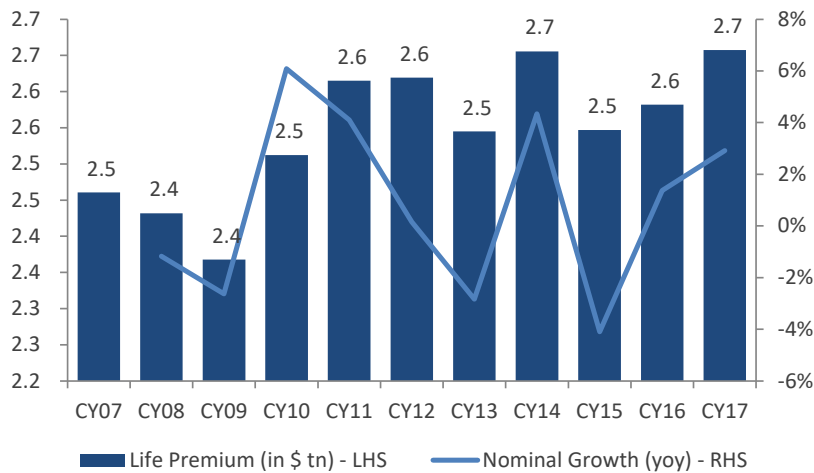
In individual insurance policies, the Agency channel continues to be the largest distribution channel, even as bancassurance has come to be a driving force. Alternate methods of distribution such as online, internet marketing firms which currently have a small share of the distribution pie continue to gain traction.

CARE projects the life insurance market to continue to grow at approximately 14-15% due to factors such as 1) higher demand for retirement products such as pension/annuity coming from rapidly aging population coupled with low availability of government sponsored social security mechanisms and rising awareness of retirement planning, 2) growing awareness/education level in middle-income class group, 3) sustained growth in urbanization rate, 4) intense push to increase insurance coverage especially in rural populace, 5) product innovations/customization, 6) rise of multiple distribution channels, and 7) continued tax benefits.

CARE further expects regulatory changes and government initiatives to aid in the further penetration of insurance products in medium term. However, challenges such as 1) low income of individual agents, and 2) low persistency ratio continue to persist in the segment. These challenges would need to be addressed to improve the depth and spread of the industry.

Global Life Insurance

Chart 1: Global Life Insurance Premium Volume Growth



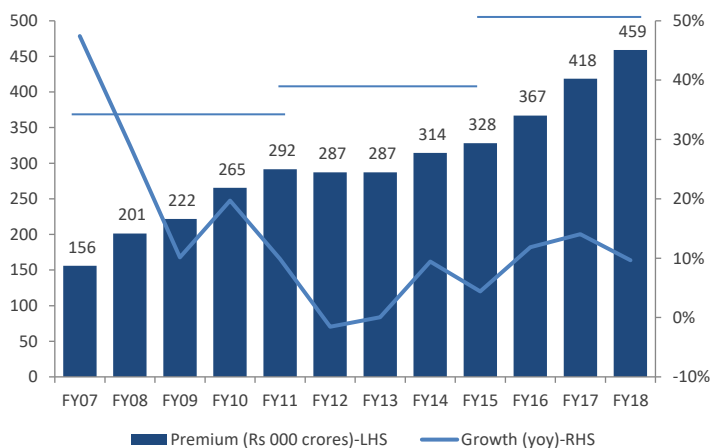
Source: IRDAI Annual Reports

The global life insurance industry grew at a CAGR of 0.8% during the CY07-17 decade and has reached nearly \$2.7 tn in market size (*insurance premium volume*) in CY17 as compared to \$2.5 tn in CY07. Declining life insurance premiums in advanced markets were the primary cause of the slowdown in global growth. In emerging markets, the premium expansion was two to three percentage points lower as compared to the previous year. The slowdown in advanced economies impacted the overall premium growth as these economies account for more than 75% of global premium income.

Domestic Life Insurance: Current market growth is due to the private sector taking centre stage and is more value driven than volume

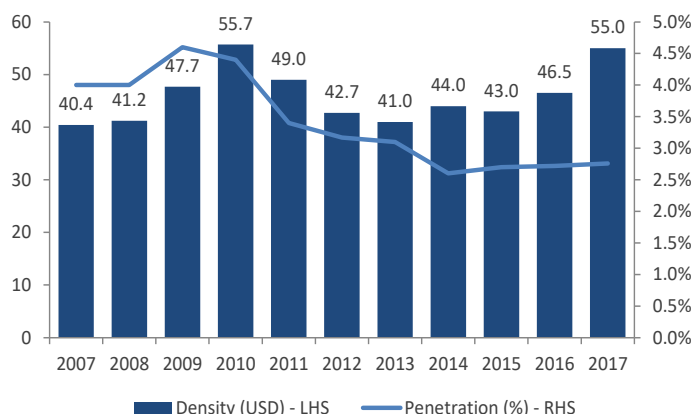
Since the domestic industry was opened to the private sector in 2001, it has witnessed several changes (regulatory and structural) and has undergone transformation leading to increased penetration, higher coverage, rise of multiple channels (agency, bancassurance, broking, direct, corporate agency, etc.), superior reach, and intensifying competitiveness in the market. The industry has also witnessed trends such as increased digital presence, emergence of InsureTech for innovations around customer education & service/ products/ technology/ delivery systems for access.

Chart 2: Life Insurance Total Premium



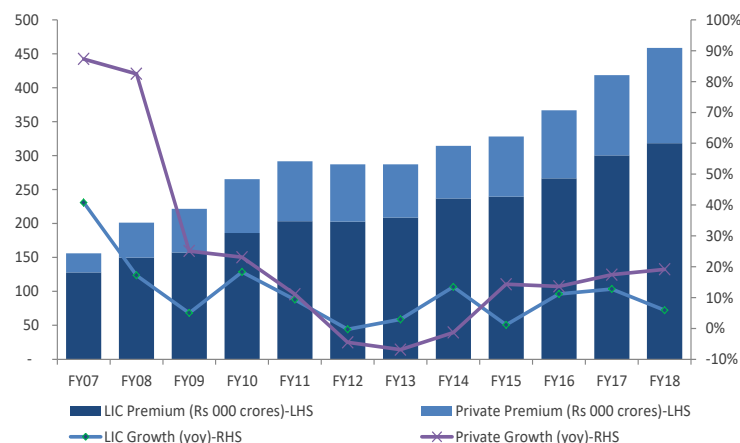
Source: IRDAI

India's total life insurance premium reached Rs. 458,809 crore in FY18 from Rs. 156,076 crore in FY07 at a CAGR of 10.3% during FY07-18, due to 1) rising household savings/ income levels, 2) increasing education/ awareness level, 3) rise of middle class, 4) tax benefits, 5) product innovations/ customization by insurance companies, and 6) entry of multiple distribution channels such as bancassurance. Over 85% is non-linked premium, while balance is linked premium. Non-linked premium is dominated by LIC, while the private sector holds a larger share in Linked premium (due to ULIP products).

Chart 3: Life Insurance: Density and Penetration

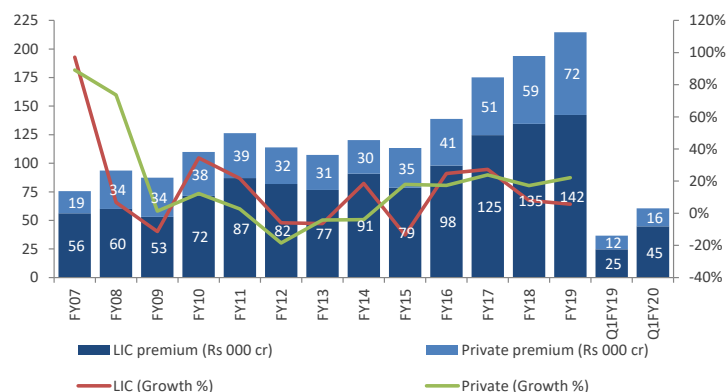
Source: IRDAI, Life Insurance Council

Life insurance penetration (premium as percentage of GDP) in India declined from a peak of 4.6% in CY09 to 2.5% in CY13 and recovered marginally to 2.76% in CY17. Bulk of the decline happened during the years of major regulatory changes, which necessitated significant effort on the part of the insurers to adapt. Several products (predominantly ULIPs) were rendered ineligible and insurers had to re-design them to comply with the new regulations, resulting in a sharp decline in product offerings. However, the insurance industry in India has staged a smart recovery after multiple regulatory actions had significantly impacted the operations.

Chart 4: Total Life Insurance Premium: Public vs. Private

Source: IRDAI

LIC's total premium income reached Rs. 318,223 crore in FY18 from Rs. 127,823 crore in FY07 i.e. a CAGR of 9%. The private sector total premium income grew at a CAGR of 16% during FY07-18 i.e. from Rs. 28,253 crore in FY07 to Rs. 140,586 crore in FY18. The share of public sector in total life insurance premium fell from 82% in FY07 to 69% in FY18. Private sector premium growth was nearly double that of LIC's premium growth due to the 1) focus on metro cities, 2) focus on high value insurance policies (which generated larger premiums), 3) leverage of technology (digital), and 4) expansion of distribution channels (*bancassurance and other agency channels*) compared to LIC's focus on the agency channel

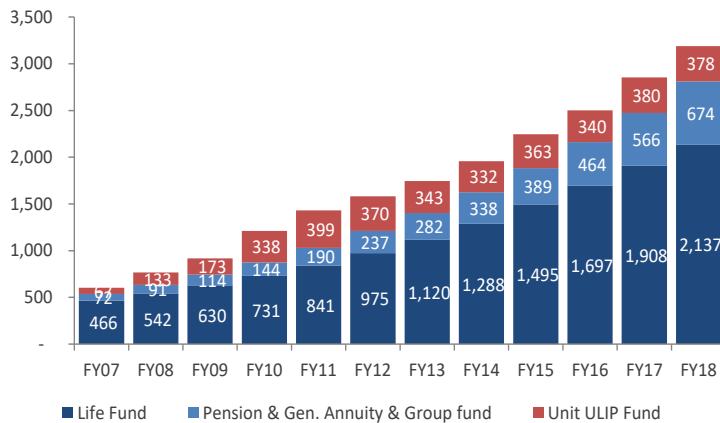
Chart 5: New Business Premium Growth- LIC vs. private insurance companies

Source: IRDAI

LIC's first year premium income reached Rs. 142,192 crore in FY19 from Rs. 15,977 crore in FY03 i.e. a CAGR of 15%. While the private sector premium income grew at a CAGR of 31% during FY03-19 i.e. from Rs. 966 crore in FY03 to Rs. 72,481 crore in FY19. The share of LIC in first year life insurance premium fell from 94% in FY03 to 74% in FY07 and further to 66% in FY19, however, for Q1FY20, LIC has increased its share to ~74%

During FY19, life insurers issued 286.9 lakh new policies, out of which LIC issued 214.3 lakh policies (75% share vs. 83% in FY07) and the private life insurers issued 72.5 lakh policies (25% share vs. 17% share in FY07). The private sector registered a growth of 5.7% in the number of new policies issued against the previous year which was higher than the 0.4% growth reported by LIC. The increase in market share of private companies has been more in the insurance premium (*value*) compared to the quantum of the policies sold annually (*volume*).

Chart 6: Movement in Life Insurance Industry's Assets Under Management



The overall assets under management have grown more than 5 times from Rs 604,180 cr in FY07 to Rs. 3,189,060 cr in FY18 at a CAGR of 16%. Life fund with a current share of 67% (FY07 share: 77%) continues to have the bulk of assets under management. Pension/ Annuity fund has shown a consistent increase to 21% in FY18 (FY07 share: 12%). ULIP fund has been a curious case whose share had sharply increased to 28% in FY10/11 due to the popularity of ULIPs during that period and subsequently dropped due to regulatory changes and reverted to the share that it had in FY07.

Source: IRDAI

The persistency ratio measures how long customers stay with their policies and is import as a high ratio not only contributes to profitability, but also helps in reducing costs through economies of scale. Domestically, this ratio is currently low as per international standards but is generally improving albeit slowly both at the 13th month and 61st month levels. Globally, the persistency ratio is around 90% in the 13th month and over 65% after 5 years.

The life segment has grown consistently over the past decade and has seen various trends such as emergence of bancassurance and alternative distribution channels. However, challenges such as 1) Low income of Individual agents: The average premium income per policy of individual agents grew at a CAGR of 6% over FY08-18 period, even as average premium income per policy of corporate agents grew at a CAGR of 11% over the same period. The average premium income per policy of corporate agents was 2.5 times of individual agents in FY18 highlighting the divide, and 2) High lapse ratio and low persistency ratio: The 61st month persistency ratio of most major companies has remained on the lower side impacting profits and operating costs, continue to persist in the segment. These challenges would have to be addressed to improve the vibrancy and growth of the segment.

Regulatory Movement

IRDAI has simplified product regulations for both the unit-linked products and non-linked products. Some of these modifications include:

Death benefits: For all traditional products, the minimum sum assured on death has been set as a minimum of seven times the annual premium in case of a regular policy and 125% of the premium for single premium policies.

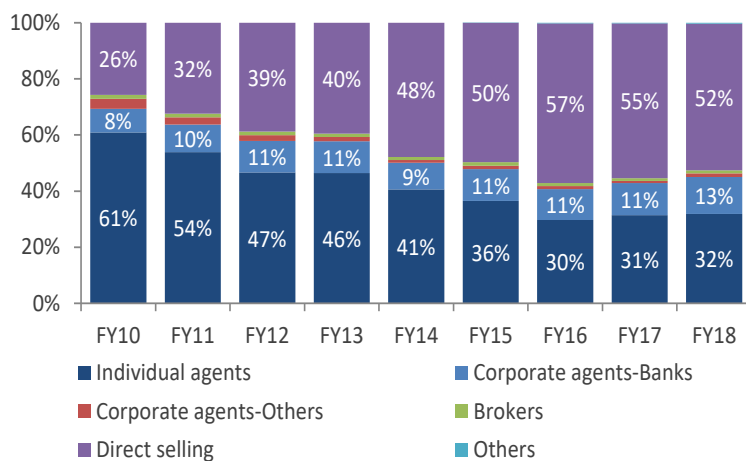
Pension products: The policyholder can utilise the entire proceeds of pension products post surrender/vesting to purchase annuity/deferred annuity at the prevailing annuity rate. Alternatively, the policyholder / the nominee can commute up to 60% in line with similar NPS provisions. However, the nominee can also receive the full amount in case of the policyholder's demise during the deferment period.

Surrender value: A policy would have a surrender value of 30% of the total premium paid less any survival benefits already paid, if surrendered during the 2nd year of the policy and if the premium has been paid for two consecutive years. The surrender value would increase to 35% of the total premium paid, less any survival benefits in the 3rd year. Surrender value would be 50% of the total premium paid if surrendered between the 4th and 7th year. The policyholder could receive 90% of the premium paid in case a policy is surrendered in the last two years.

Distribution Channel Analysis

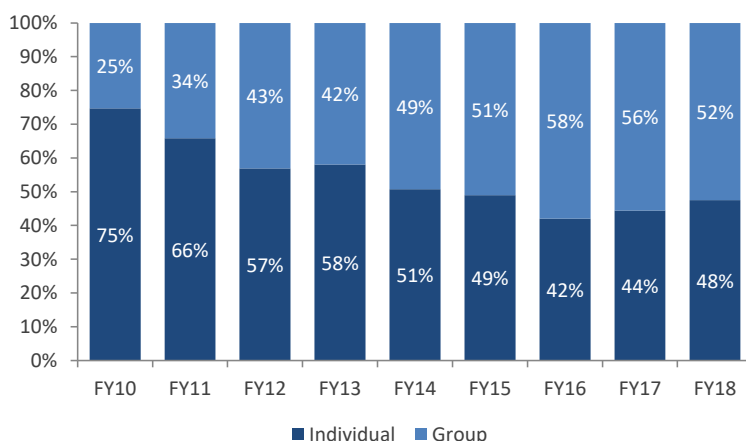
Marketing of life insurance service is critical and complex due to its time span, periodicity, claims and higher brand switching costs that affect the buying behaviour. Consequently, distribution is one of the key determinants of success for insurance companies. Insurance is provided either directly (direct selling, contact centres) or through various distribution channels such as individual agents, corporate agents including bancassurance and brokers. There has been a noticeable shift in the channel mix of the Indian life insurance sector. The following chart highlights the trend in channel mix for the industry:

Chart 7: New Business Premium (Rs cr) by Channel



Source: IRDAI

Chart 8: New Business Premium (Rs cr) by Category

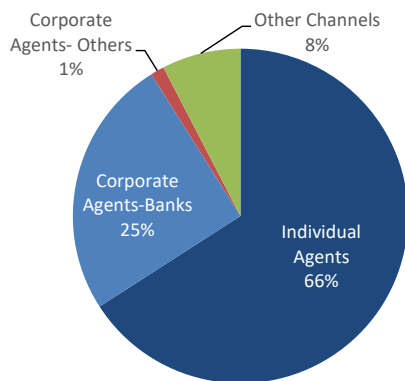


Source: IRDAI

The contribution of the Agency channel to the individual new business premium decreased from 61% in FY10 to 32% in FY18. The share of banks in new business had gone up from 8% in FY10 to 13% in FY18. The cap on ULIP charges, introduced in 2010, led to a rationalisation of owned agency network and introduced a shift towards third-party channels. The well-developed banking sector in India and the nationwide presence of banks resulted in the increase of bancassurance's contribution. Direct selling channel's share has increased from 26% in FY10 to 52% in FY18, primarily on the basis of the group business being sourced directly by the companies.

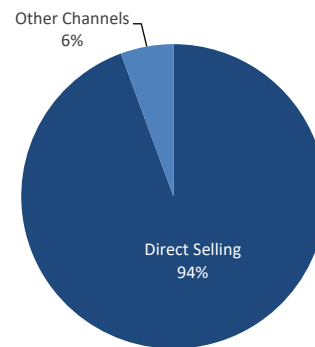
Agency and bancassurance channels continue to remain the dominant third party distribution channels of the life insurance companies and are expected to contribute substantially going forward. However, the alternate distribution channels are just starting to contribute and are expected to increase their share. Domestically, over a 15 year period, the market share of the private insurance companies has reached 31% (FY18) from 2% (FY03) driven by 1) usage of multiple distribution channel, 2) expansion in metros, and 3) faster technology adoption.

Chart 9: Distribution Channels for Individuals (FY18)



Source: IRDAI

Chart 10: Distribution Channels for Group (FY18)



Source: IRDAI

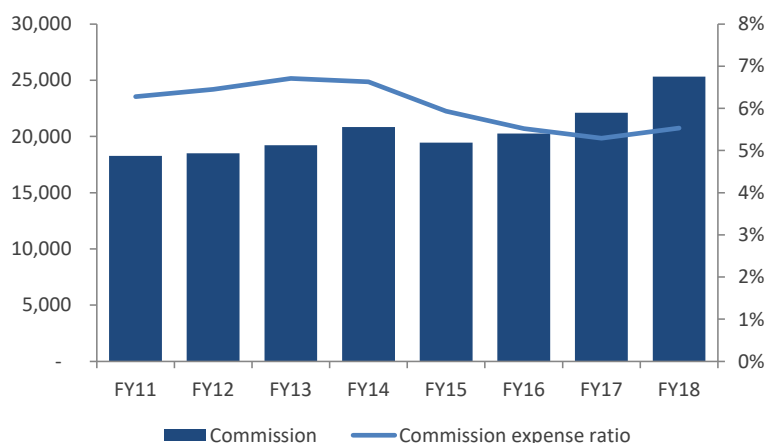
In individual insurance, the Agency channel has continued to be the largest distribution channel, while bancassurance has come to be a driving force for increasing premium especially by the private sector. Alternate methods of distribution such as online, internet marketing firms which currently have a small share of the distribution pie continue to gain traction. On the other hand, the group insurance, direct selling accounts for a lion's share of the new business premium.

Costs and Profitability

Benefits Paid

The life insurance industry paid benefits of Rs. 277,954 cr in FY18 (Rs 142,524 cr in FY11) which constituted 60.6% of the gross premium underwritten (48.9% in FY11). The benefits paid by the private insurers was Rs. 81,236 cr in FY18 constituting 57.8% of the premium underwritten (35.5% in FY11). LIC paid benefits of Rs. 196,718 cr in FY18, constituting 61.8% of the premium underwritten (Rs. 111,273 cr. in FY11, 54.7% of the premium underwritten). A third of the benefits paid in FY18 were accounted by surrenders/ withdrawals. ULIP surrenders accounted nearly 16% for the public sector while accounting for a whopping 89% in the private sector.

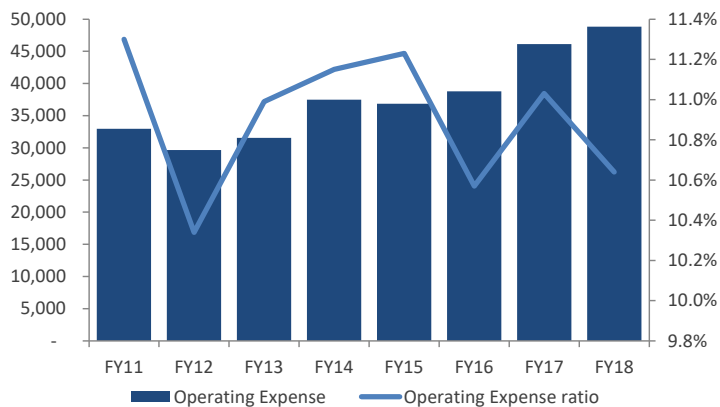
Chart 11: Gross Commission (Rs cr)



Source: IRDAI

Commission expense grew at a CAGR of 4.8% during FY11-18 i.e. from Rs. 18,280 cr in FY11 to Rs. 25,326 cr in FY18 (Source: IRDAI Handbook FY18). The commission expenses ratio (*commission expenses as a % of premiums*) fell to 5.5% in FY18 from 6.3% in FY11 primarily due to the rise of alternate channels to source business (*alternate channels of distribution such as bancassurance and the internet reduce costs and increase access to a wider customer base*).

Chart 12: Operating Expenses (Rs cr):



Operating expenses grew at a CAGR of 5.8% during FY11-18 i.e. from Rs. 32,942 cr in FY11 to Rs. 48,821 cr in FY18 (Source: IRDAI Handbook FY18). The operating expense ratio (defined as operating expenditure/total premium) witnessed an aggregate marginal decrease of 70bps to 10.6% in FY18 from 11.3% in FY11.

Note: Life: Operating Expense % to Premium

Source: IRDAI

Analysis of Select Life Insurance companies

Table 1: Select Metrics of Five Life Insurance Companies

Metric				YoY Growth	
	FY17	FY18	FY19	FY18	FY19
Total Premium (Rs cr)	79,778	96,067	116,538	20.4%	21.3%
Commission (Rs cr)	3,418	4,695	5,308	37.4%	13.0%
Expenses of Management (Rs cr)	12,454	14,422	17,337	15.8%	20.2%
Commission Exp Ratio	4.3%	4.9%	4.6%		
Expenses of Management Ratio	15.6%	15.0%	14.9%		

Sample includes SBI Life Insurance, ICICI Prudential Insurance, HDFC Life Insurance, Max Life Insurance and Bajaj Allianz Life Insurance

Source: Public Disclosures by Companies

Total premium growth has continued with the sample companies growing y-o-y by 21.3% in FY19 compared to 20.4% in FY18. The growth has been principally powered by 1) strong banking franchise (*movement in growth as well as absolute size in productivity and ticket size has been higher in bank branches compared to individual agents*) coupled with the rising importance of the alternative distribution channels, 2) faster expansion in protection business coupled with a consistent growth in savings (*especially ULIPs*) business and 3) targeting the younger demographic for insurance.

Growth in gross commission was slower as compared to the growth in total premium along with a moderation in the Commission Expense Ratio in FY19. In FY18, both of these metrics recorded a substantial increase. The rise can be accounted for the higher sale of policies which have a substantial higher upfront commission and lower renewal commissions. Further it is interesting to note that although the commission expense ratio has moderated, companies which have a strong bancassurance channel (*derive more than 50% of premium through this channel*) and a banking parent have recorded a lower commission expense ratio as compared to a company which too has a strong bancassurance channel but via a banking partner. The remaining company on the other hand, paid a significant share of its commission to the individual agents' channel (*includes POS presence under Individual Agents*) and recorded an increase in the commission expense ratio.

In FY19, total expenses have grown in line with growth in total premium. The expense of management ratio has been on a generally reducing trend reflecting both the cost improvement measures undertaken and the growing scale of the insurance companies. If the commission expenses are stripped from total expenses, two companies have operating expense ratio below 10%, while the balance three companies have reported double digit operating expense ratio. All

companies have reported that employee costs as the largest share of operating expenses in FY19, while four companies also reported advertisement as a substantially large operating expense; only one company spent less on advertisement and more on 1) legal charges and 2) stamp duty on policies.

Table 2: Movement in Solvency Margins

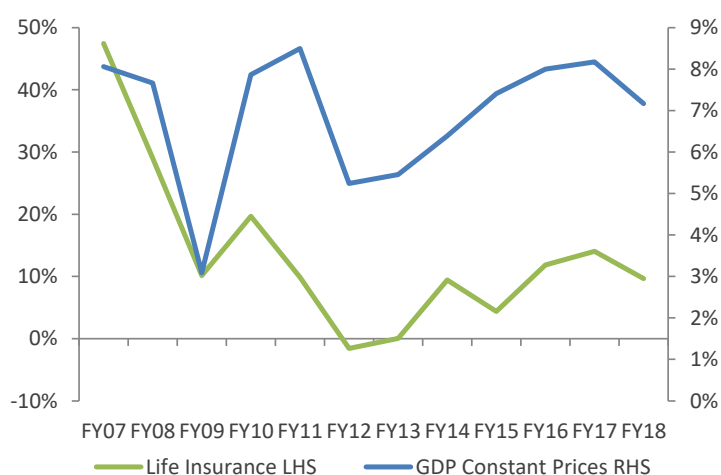
Company Name	Solvency Ratio		
	FY17	FY18	FY19
Life Insurance Co. 1	204.0%	206.0%	213.0%
Life Insurance Co. 2	280.7%	252.5%	214.9%
Life Insurance Co. 3	192.0%	192.0%	188.0%
Life Insurance Co. 4	309.0%	275.0%	242.0%
Life Insurance Co. 5	582.0%	592.2%	803.7%

Source: Public Disclosures by Companies

One of the important factors that influence insurance penetration is the capital requirement under the solvency margin. As per Insurance Act, 1938 every insurance company in India is mandated to maintain a Solvency Margin as per section 64 VA. All life insurance companies in India have complied with the stipulated required solvency ratio of 150%.

Outlook

Chart 13: Annual Growth Rate (in %)



Source: CMIE, IRDAI

Insurance demand is positively correlated with economic growth and grows at a multiple to the GDP. However, the outlook for the insurance industry is not just a function of the economic growth but industry specific factors such as distribution channels, also affect the premium growth.

CARE expects the life insurance segment to continue to grow at approximately 14-15% due to 1) higher demand for retirement products such as pension/annuity coming from an aging population coupled with low availability of government sponsored social security mechanisms and rising awareness of retirement planning, 2) growing awareness, 3) growing urbanization, 4) younger demographic opting for pure protection plans driving insurance coverage, 5) intense push to increase insurance coverage especially in rural populace, 6) product innovations/customization, 7) rise of multiple channels, and 8) continued tax benefits.

Some trends include expanding insurance distribution in rural areas, Indian companies expanding operations overseas and increased online selling of insurance products. However, frauds, high lapse-ratio, any unfavourable changes in macro-economic factors such as trade breakdown, unemployment and uncertainties in the regulatory landscape could be characterized as key challenges to the industry growth.