As the Pandemic Recedes, Life Insurance Sector to Shift Focus Back on Growth

March 31, 2022 I BFSI Research

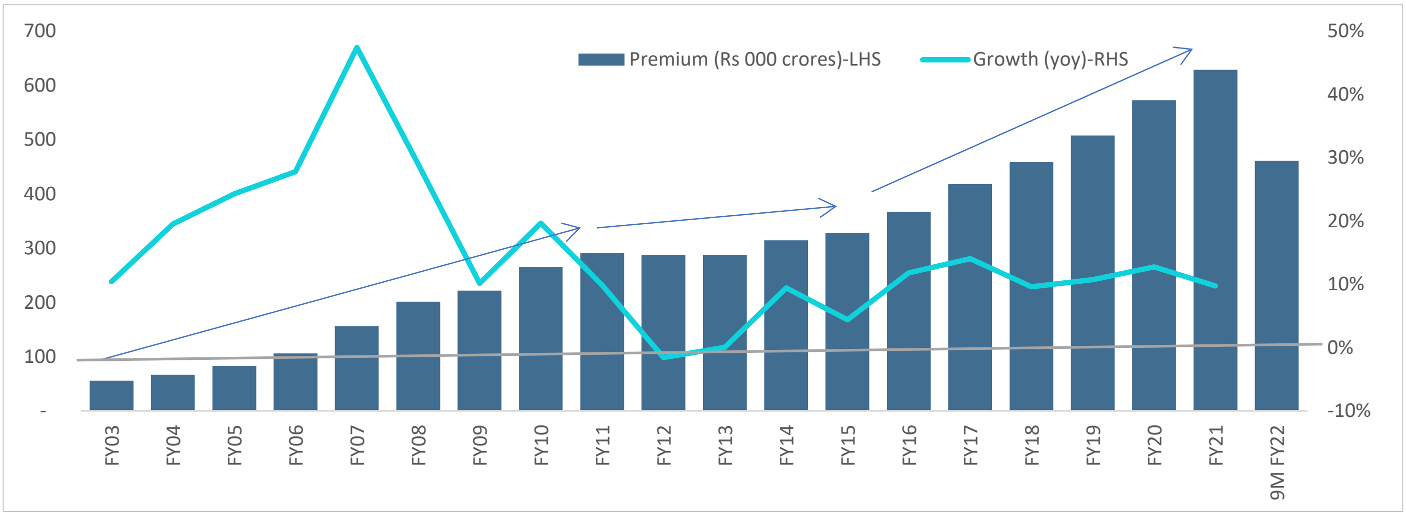
Summary

- The Indian life insurance sector has been growing substantially at a compound annual growth rate (CAGR) of more than 11% over the past few years, which is substantially faster than the average global growth rate. The prime drivers of this growth include a substantial increase in group insurance products coupled with innovations, customisation, and the development of strong distribution channels in the individual insurance segment.
- The gap between India's insurance density and penetration levels and the average for Asian economies indicates a substantial growth opportunity.
- Life insurance continues to dominate domestic insurance premium. Globally, the share of life insurance in total premium was approximately 50%, while the same for India was nearly 75%.
- Indian life insurance has a top-heavy market structure with the top five players holding over 85% market share and the remaining companies making up a long tail. This, along with public sector banks being required to reduce their stakes in some insurance companies due to their mergers, is likely to trigger consolidation in the segment.
- The primary focus of the life insurance industry in FY21 and a significant portion of FY22 was on the Covid-19 pandemic, but it's now expected to focus more on the growth story.
- Companies are expected to simplify the life insurance purchase experience and overall digital enablement further across the distribution channels. CareEdge expects the life insurance industry to continue to grow at 12-14% over a three-to-five-year horizon driven by group products, individual pension, and life cover products along with supportive regulations, rapid digitalisation, effective distribution, and improving customer services. However, frauds and lapse ratio are some of the key challenges.

Growth Trajectory of Indian Life Insurance

Since the life insurance industry was opened to the private sector in 2001, it has witnessed several changes (regulatory and structural) and has undergone a significant transformation. India's total life insurance premium reached Rs 6,28,731 crore in FY21 from Rs 156,076 crore in FY07 at a CAGR of 10.5% during FY07-21 due to rising household savings, income levels, increasing education, awareness, the rise of the middle class, tax benefits, product innovations by insurance companies, and entry of multiple distribution channels such as bancassurance.

Figure 1: Life Insurance Total Premium



Source: IRDAI, Company filings

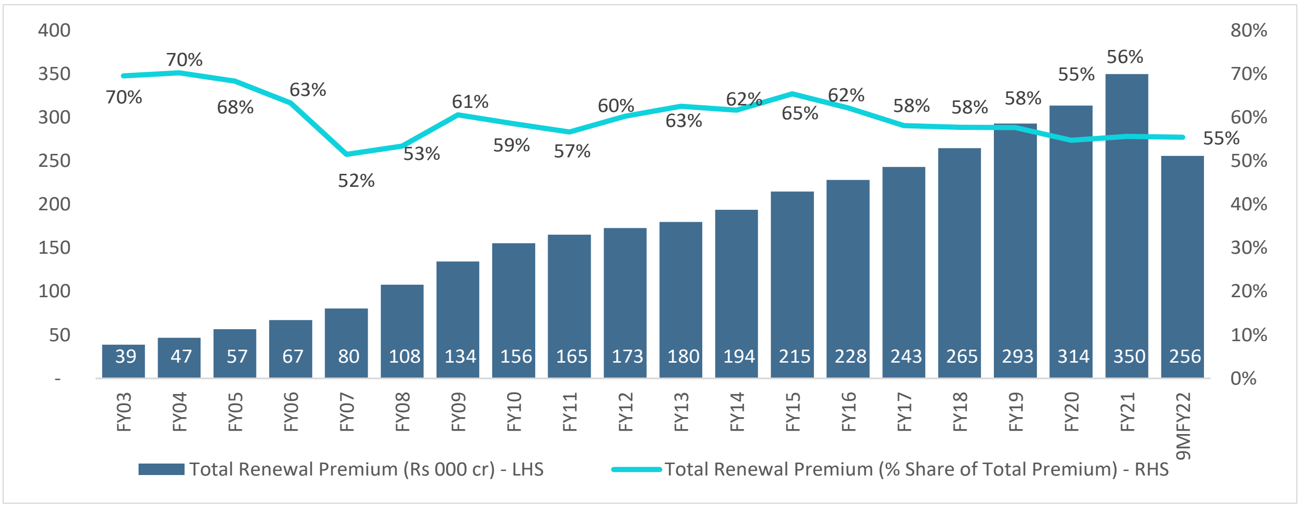
The above growth can be classified into three phases:

- **Phase I (FY01–FY08):** Before 2000, Life Insurance Corporation of India (LIC) was the only player operating in the industry. Post liberalisation, several private companies came in and all witnessed significant growth. Total premium rose sharply driven by ULIPs with a sustained capital-market appreciation and high upfront commission, especially for linked products.
- **Phase II (FY09-FY14):** Private insurers faced a larger impact of regulatory changes. Based on total individual first-year premium income, the market share of LIC witnessed an increasing trend from FY10 to FY14, while private players saw a declining market share trend during the same period. The 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 redesign them to comply with the new regulations, resulting in a sharp decline in product offerings. Subdued stock markets also reduced the appetite for linked products among customers
- **Phase III (FY15 onwards):** After the slowdown in the earlier period, from FY15, the industry began showing signs of revival, primarily due to the improvement in the performance of private players. LIC's first-year premium growth has been marginally lower at 15.3% vs 18.1% for the private companies for the FY15-FY21 period primarily due to the rise in distribution channels (bank and digital) of private players.

Dominated by LIC, over 80% of life insurance is non-linked premium, while the balance is linked premium where the private sector holds a larger share due to ULIP products. The shift in the premium market share can be attributed to several structural and regulatory changes. The private players underwent transformation leading to increased penetration, higher coverage, the rise of multiple channels (including agency, bancassurance, broking, direct, corporate agency), superior reach, and intensifying competitiveness in the market. The overall industry has also witnessed trends such as increased digital presence, the emergence of InsureTech for innovations around customer education & service/ products/ technology/ delivery systems for access.

Renewal Premium Accounts for more than half of Total Premium

Figure 2: Share of Renewal Premium in Total Premium



Source: IRDAI, Company filings

Life Insurance Dominates

The life insurance segment continues to dominate the domestic insurance industry premium. Globally, the share of the life insurance business in total premium was around 50%, while the same for India was 75%. However, its share has been declining gradually from 85.8% in FY07.

Figure 3: Share of Life Insurance in Total Insurance Premium

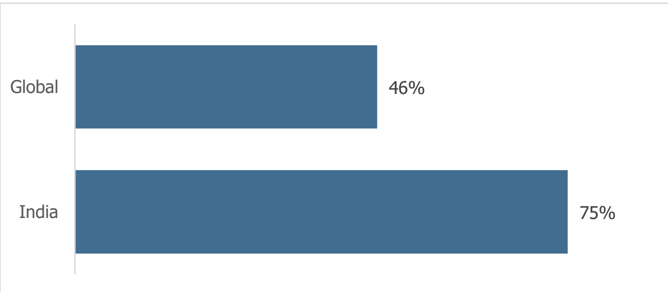
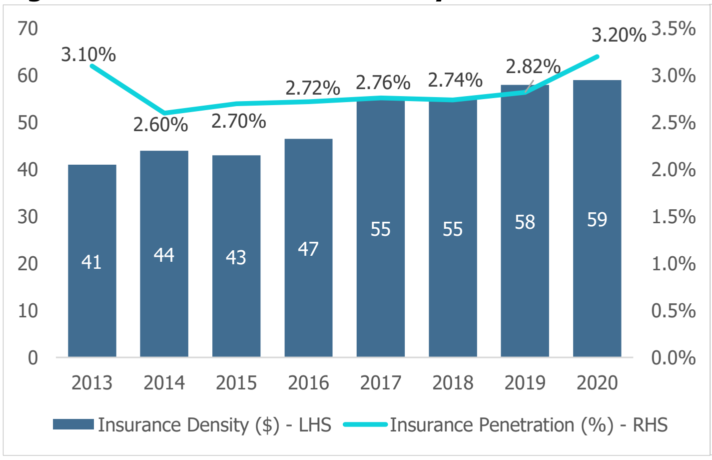
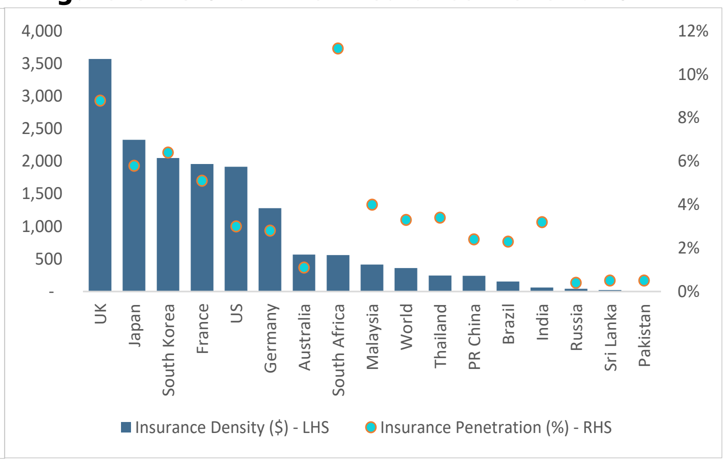


Figure 4: Life Insurance: Density and Penetration in



Source: IRDAI

Figure 5: Global Life Insurance Penetration

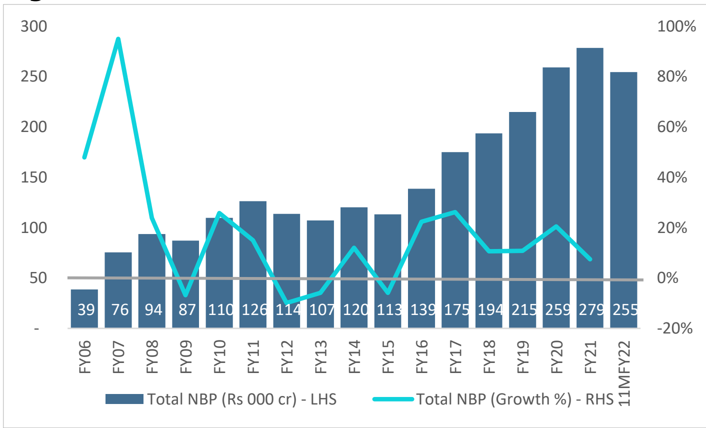


Source: IRDAI

Life insurance penetration (premium as a percentage of GDP) in India declined from a peak of 4.6% in CY09 to 2.5% in CY13 and recovered marginally later. The 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 redesign 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.

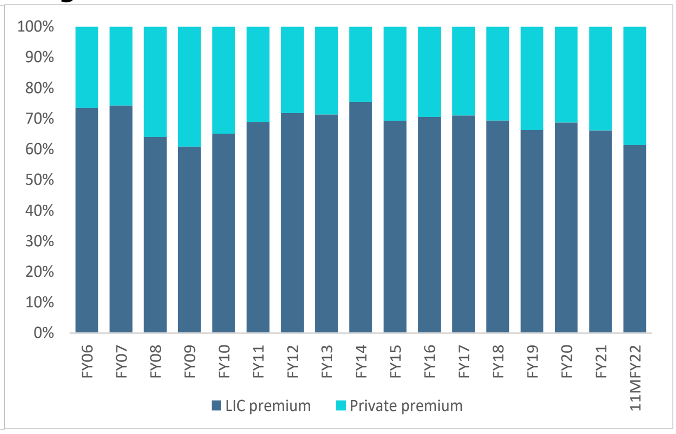
India continues to be an underpenetrated insurance market with a penetration of 3.2% in 2020, as compared to other countries and a global average of 3.33%. At $59 in 2020, the insurance density in India also remains exceptionally low as compared to other developed and emerging market economies as well as the global average. Both these indicators highlight the immense untapped development potential within the Indian insurance industry.

Figure 6: New Business Performance



Source: IRDAI

Figure 7: New Business Premium - LIC vs. Pvt

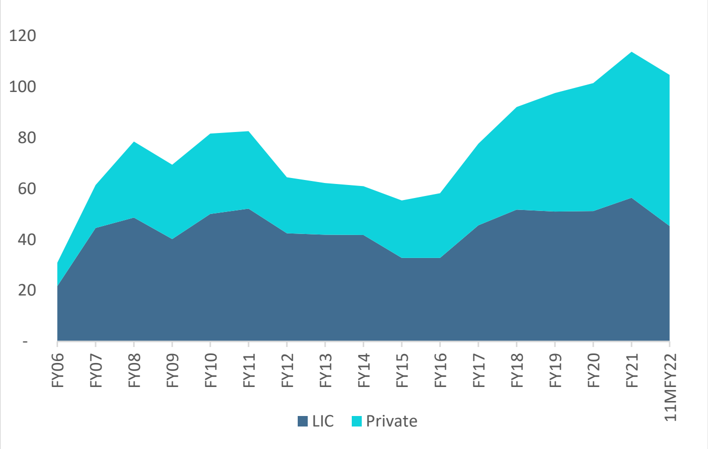


Source: IRDAI

The new business performance had witnessed robust growth at a CAGR of 14.1% for the FY04-21 period reaching Rs 278,699.9 crore in FY21. For 11M FY22, the life insurance sector's first-year premium grew by 8.4% compared to a marginal increase of 0.6% for 11M FY21. Due to the Covid-19 pandemic lockdown, premium was affected in FY21 and resultant different growth after the same, base effect may also be possible in monthly FY22 numbers.

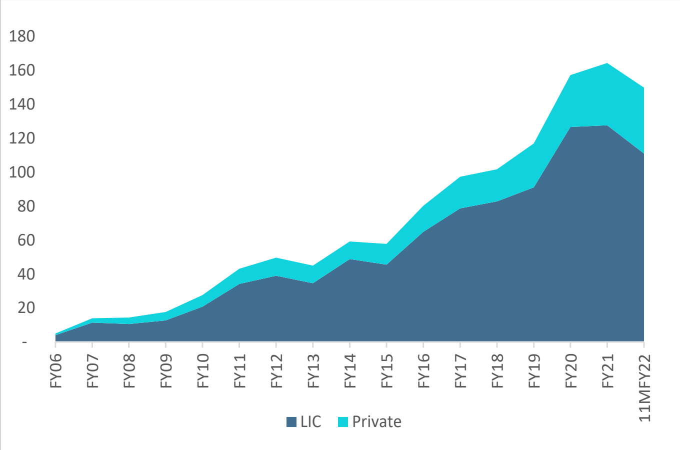
LIC's first-year premium income grew at a CAGR of around 13%, while the private sector premium income rose 16%. The share of public sector life insurers in first-year life insurance premium fell from 94% in FY03 to 74% in FY07 and further to 66% in FY21 and 61% in 11M FY22. However, it remains very formidable. 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) which is indicative of the fact that private companies have been targeting high-value policies.

Figure 8: New Business Performance – Individual



Source: IRDAI

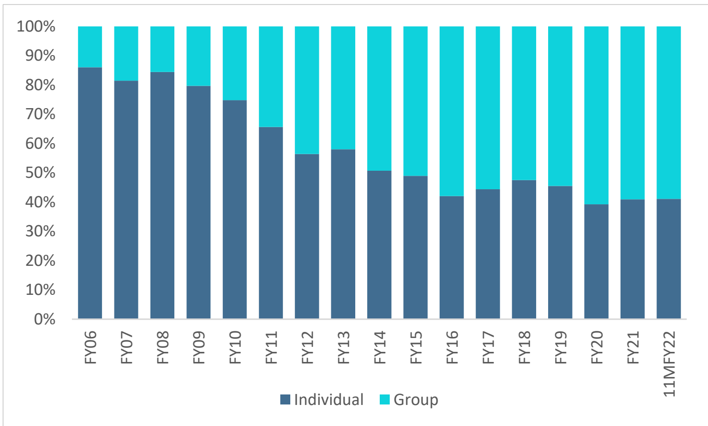
Figure 9: New Business Performance – Group



Source: IRDAI

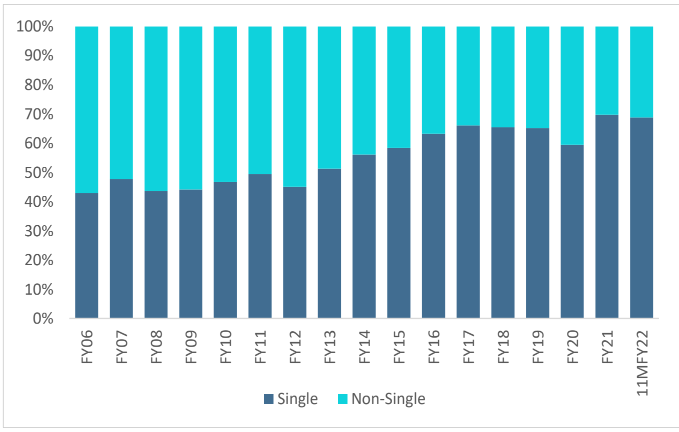
Aggregate individual premium reached Rs 113,824 crore in FY21 from Rs 81,734 crore in FY10 at a CAGR of 3.1% of this. While LIC hit Rs 56,407 crores in FY21 (CAGR of 1.1%), private companies brought in Rs 57,418 crore in FY21 (CAGR of 5.6%). Aggregate group premium reached Rs 164,454 crore in FY21 from Rs 27,557 crore in FY10 at a CAGR of 17.6%, of this LIC accounted for Rs 127,768 crore in FY21 (CAGR of 18%). Private companies had premium of Rs 36,686 crore in FY21 (CAGR of 16.6%).

Figure 10: New Business Performance – Individual vs. Group



Source: IRDAI

Figure 11: New Business Performance – Single vs. Non-single



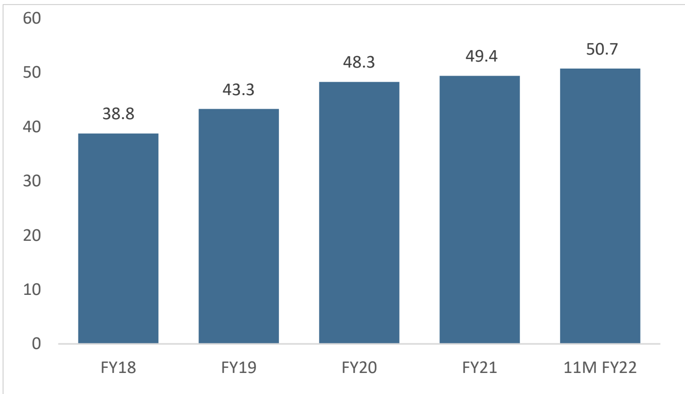
Source: IRDAI

In the earlier part of the period, individuals accounted for a substantial portion of the new business premium. It can be observed that group insurance's share rose with a corresponding rise in the share of the direct selling channel. Individual segment's share has been broadly steady for the last three years 11M FY22 individual premium reported a higher growth of 8.5% vs. an increase of 3.2% witnessed in 11M FY21, while group premium grew at 8.4% vs a fall of 1.1% for 11M FY21. Individual premium has held on to their market share in 11M FY22 vs last year but continue to remain smaller in size compared to group premium. The group premium continues to be larger than the individual premium, but the individual premium segment has been reducing its gap, year by year.

The share of single premium policies has been steadily increasing over the period and has reversed the earlier position when the non-single premium accounted for the larger share. The share of single premium has grown from 58% for

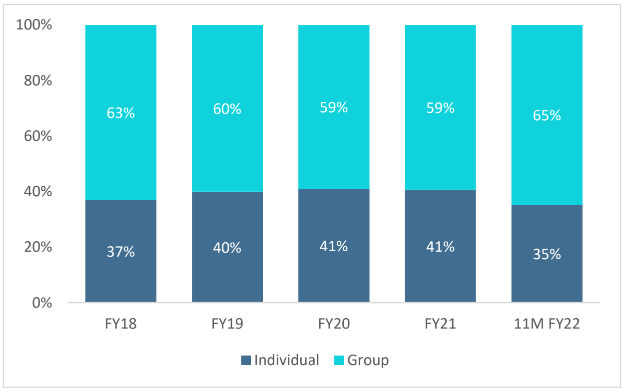
11M FY20 to 69% in 11M FY22. Most of the single premium policies are accounted for by LIC, especially in the group segment.

Figure 12: New Business Performance – Movement in Sum Assured (Rs lakh crore)



Source: IRDAI

Figure 13: New Business Performance – Movement in Sum Assured: Individual vs Group



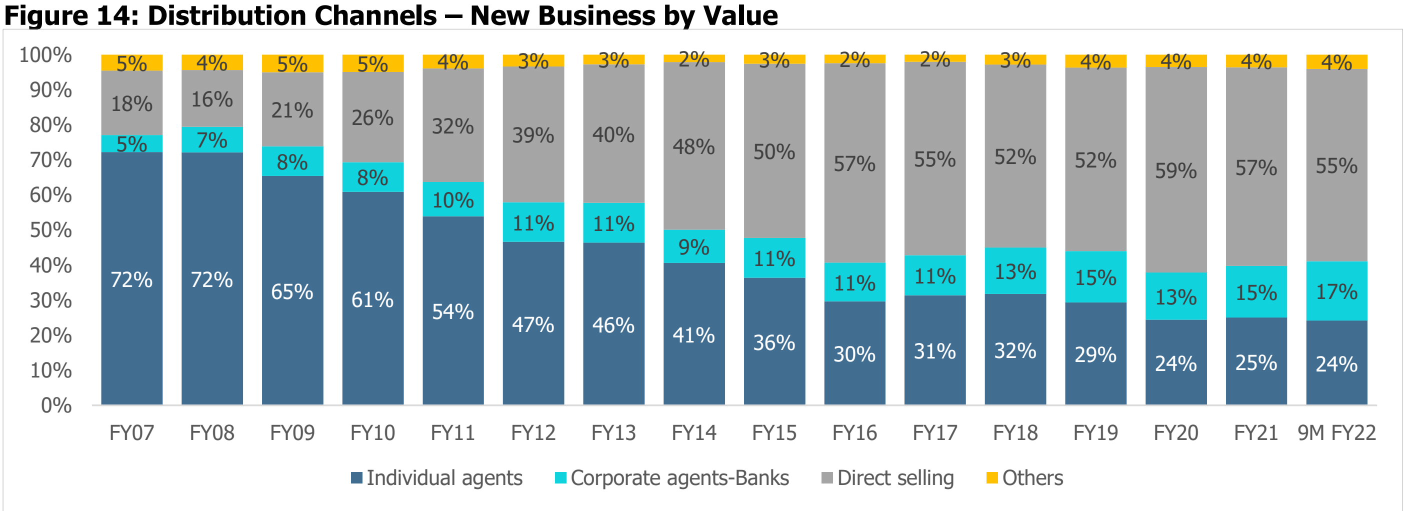
Source: IRDAI

The sum assured was increasing at a faster rate till FY20, however, due to the pandemic; the growth in sum assured has slowed. In Sum Assured, private companies continue to have a share of around 85% due to their focus on pure protection plans and a strong digital presence. The share of sum assured for the individual segment has shown an increase for the past four years (which had been driven by the rising demand for term plans which have been pushed by the private players), however, the trend seems to have reversed in the current year.

Distribution Channel Analysis

Marketing of insurance services is critical and complex due to the periodicity, claims, and brand switching costs that affect buying behaviour. Consequently, distribution is one of the key determinants of success for insurance companies. A variety of distribution channels are currently used to sell insurance products. These channels can broadly be classified into internet-led channels, company-led channels, bank-led channels, and agent-led channels. There has been a shift in the channel mix from the earlier agency-focused model to a more diversified distribution mix with digital channels coming to the fore.

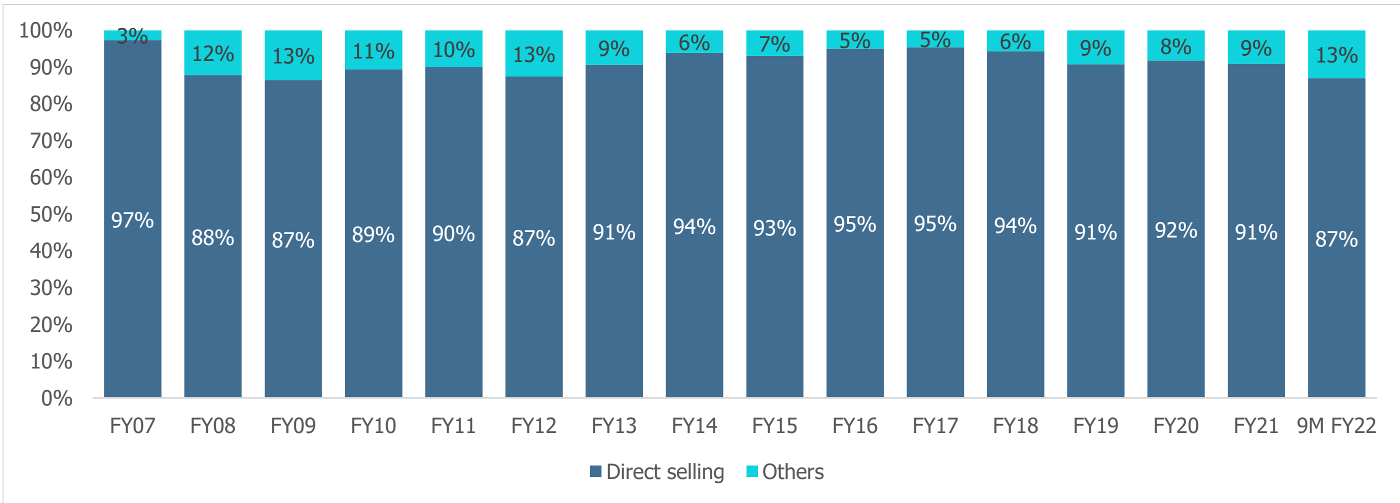
Figure 14: Distribution Channels – New Business by Value



Source: IRDAI, Company filings

The contribution of the Agency channel to the new business premium decreased from 72% in FY07 to 24% in 9MFY22. On the other hand, the share of banks in new business has gone up from 5% in FY07 to 17% in 9MFY22 and the direct selling channel's share has increased from 18% in FY07 to 55% in 9MFY22, primarily because of group business being sourced directly by the companies mainly LIC. The cap on ULIP charges, introduced in 2010, led to a rationalisation of owned agency networks and introduced a shift towards third-party channels. The well-developed banking sector in India and the nationwide presence of banks increased bancassurance's contribution to the total insurance business.

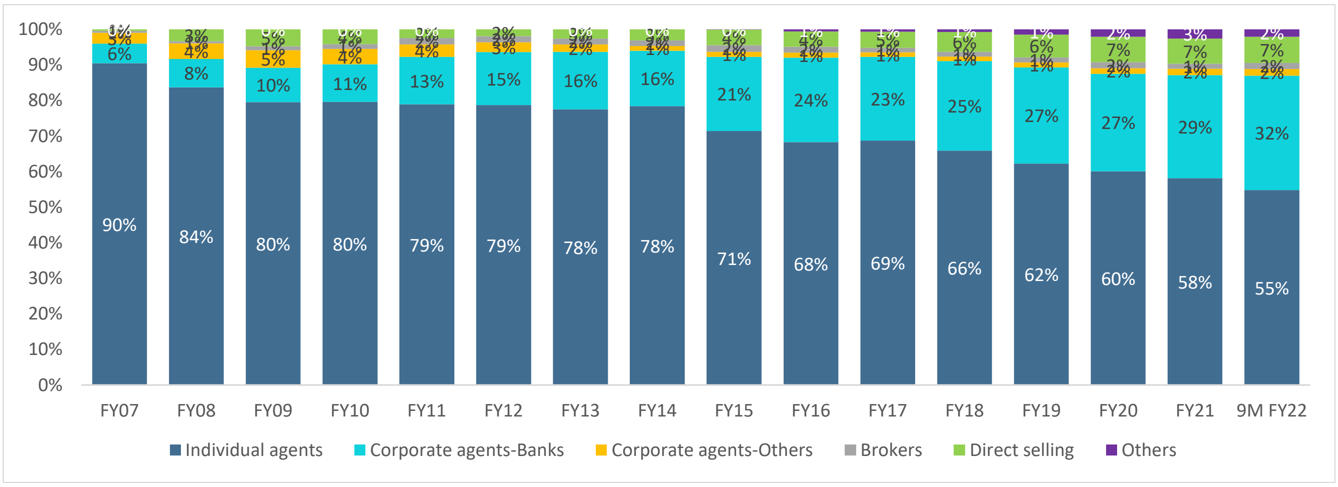
Figure 15: Distribution Channels for Group



Source: IRDAI, Company filings

Direct selling dominates the group business, and this indicates that the life insurers' in-house teams are responsible for these sales. However, it can also be seen that banks are emerging as a channel for these types of sales.

Figure 16: Distribution Channels for Individuals



Source: IRDAI, Company filings

Agency channel continues to dominate the individual business, albeit which has reduced from 90% to 55%, while bancassurance has increased from 6% to 32% indicating both the rise of alternate distribution channels and growth of private insurance companies in the sector. LIC generated over 90% of its new business premium through the Agency channel while the share of the Agency channel was close to 30% for the private sector. The proportion of individual new business premium sourced by LIC through the Agency channel has remained steady at a high of over 90% for more than the last decade indicating significant reliance on this distribution channel. While the share of Agency channels for private sector has reduced from over 60% in FY07 to around 30% in FY21 with the increasing presence of bancassurance.

Operational and technological changes have led to the development of multiple distribution channels in the insurance industry. Due to rising commissions in traditional channels such as agents and banks, insurance companies are developing alternate channels to drive growth at lower costs. This has led to the emergence of additional channels such as call centers, mobile, internet (web aggregators, Insurance Marketing Firms (IMF) and websites of insurance companies) and insurance marketing firms that are not tied to a single insurance company but can sell policies of multiple insurance companies. These alternative channels are primarily emerging in the individual segment.

Figure 17: New Business Premium by Alternate Channels (Rs crore)

	FY15	FY16	FY17	FY18	FY19	FY20	FY21	9M FY22
MI Agents	17	21	20	53	146	459	554	206
CSCs	0	1	2	2	2	1	7	150
Web-aggregators		0	46	68	162	270	385	260
IMF		0	15	41	63	68	161	124
On-line		303	418	499	1,106	1,470	1,795	1,155
Point of sale				31	55	41	56	22
Total	**18**	**325**	**501**	**694**	**1,534**	**2,310**	**2,959**	**1,917**
Share of NBP	0.02%	0.2%	0.3%	0.4%	0.7%	0.9%	1.1%	0.9%
Growth (% YoY)		1,756.9%	54.0%	38.7%	120.9%	50.6%	28.1%	

Source: IRDAI, Company filings

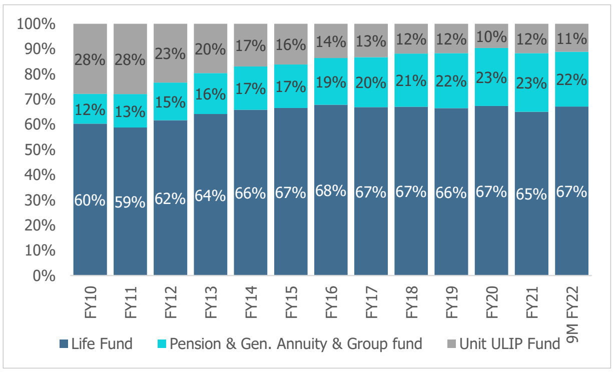
The development of alternative channels is also being driven by changes in customer behaviour, product preferences, and processes. Agency, direct selling, and bancassurance channels continue to remain the dominant distribution channels of the life insurance companies and are expected to contribute going forward. However, the alternate distribution channels are just starting to contribute and are expected to increase their share of the distribution pie. Further, the pandemic has caused insurance companies to fast-track digital options for other channels to drive sales.

Assets Under Management (AuM)

Figure 18: Movement in AuM (Rs 000 crore)

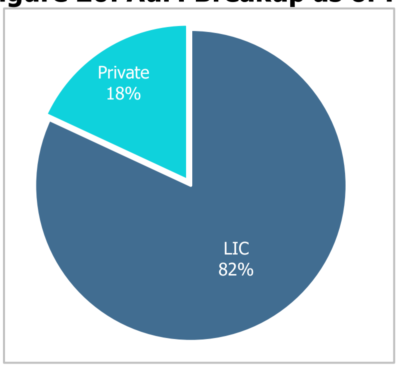
Source: IRDAI, Company filings

Figure 19: AuM – by Type



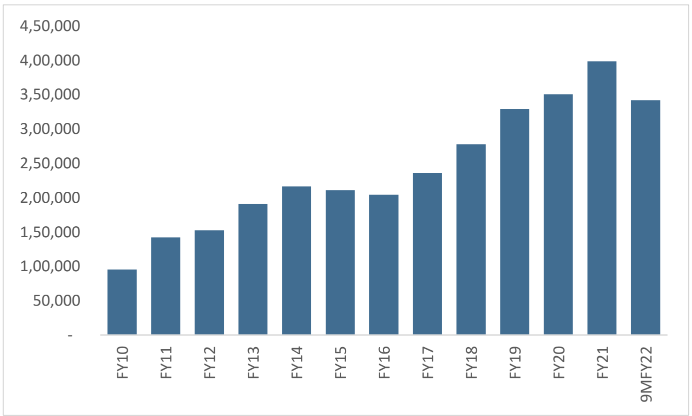
Source: IRDAI, Company filings

Figure 20: AuM Breakup as of FY21 – LIC vs Pvt.



The overall assets under management have grown more than 17 times from Rs 2,60,552 crore in FY03 to Rs. 44,79,973 crores in FY21 at a CAGR of 17.1%. Life fund with a current share of 67% (FY03 share: 88%) continues to have the bulk of assets under management. Pension/ Annuity fund has shown a consistent increase to 22% in FY18 (FY03 share: 12%). ULIP fund has been a curious case whose share had sharply increased from 0.1% in FY03 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 of 11% in 9M FY22.

Figure 21: Movement in Benefits Paid (Rs crore)

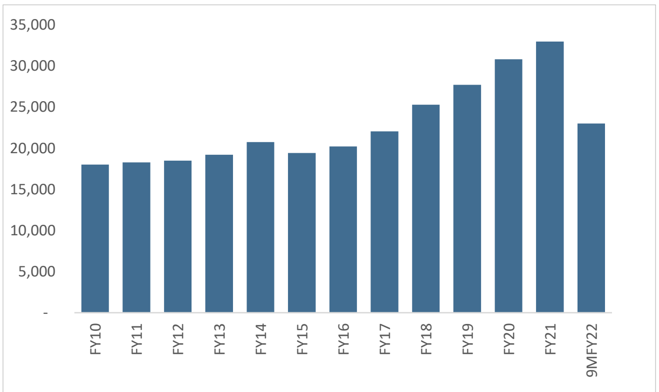


Source: IRDAI, Company filings

The life insurance industry paid benefits of Rs. 3,98,772 crores in FY21 (Rs 95,565 crore in FY10) which constituted 63% of the gross premium (36% in FY10). The benefits paid by the private insurers were Rs. 1,14,117 crores in FY21 constituting 51% of the premium underwritten (21% in FY10). LIC paid benefits of Rs. 2,84,655 crores in FY21, constituting 71% of the premium underwritten (Rs. 79,131 crores. in FY11, 43% of the premium underwritten). In 9M FY22, the impact of the pandemic is quite evident with the benefits pay-out standing at 86% of the FY21 level with private companies having a higher pay-out than LIC.

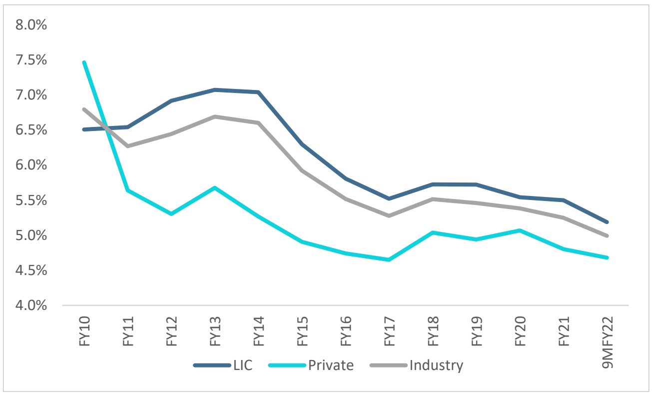
Movement in Gross Commission

Figure 22: Gross Commission (Rs crore)



Source: IRDAI, Company filings

Figure 23: Commission Expense Ratio

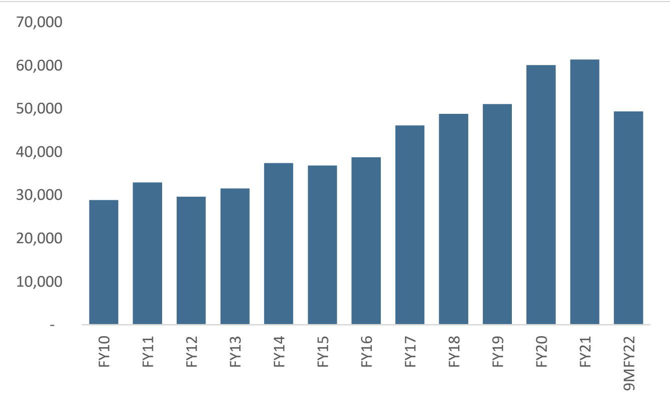


Source: IRDAI, Company filings

Commission expense grew at a CAGR of 5.6% during FY10-21 from Rs. 18,036 crore in FY10 to Rs. 32,994 crore in FY21. In general, the commission ratio has been trending down, which is indicative of the companies working to control the pay-out to various distribution channels. The commission expenses ratio (commission expenses as a % of premium) fell to 5.2% in FY21 from 6.8% in FY10 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) and which has continued for the 9M FY22 period.

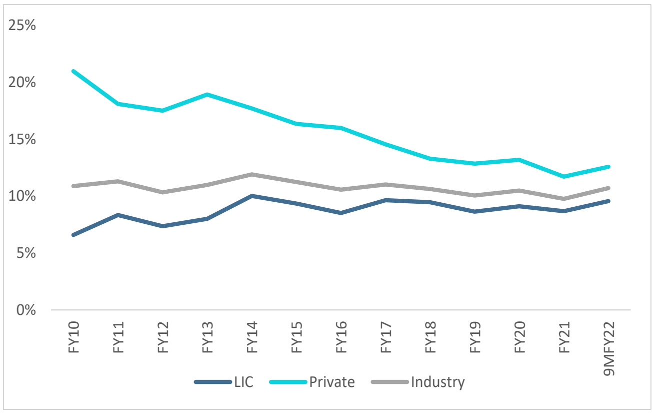
Movement in Operating Expenses

Figure 24: Operating Expenses (Rs crore):



Source: IRDAI, Company filings

Figure 25: Operating Expense Ratio



Source: IRDAI, Company filings

Operating expenses grew at a CAGR of 7.1% during FY10-21 i.e., from Rs. 28,906 crores in FY10 to Rs. 61,422 crores in FY21. The operating expense ratio (defined as operating expenditure/total premium) witnessed an aggregate decrease of 112bps to 9.8% in FY21 from 10.9% in FY10. Operating expenses have remained elevated in 9M FY22 and are 80% of the FY21 levels with private companies having a higher rate than LIC.

We have examined the factors behind the industry's growth such as income tax benefits, product innovations and customization, multiple distribution channels, competitive pricing, and adoption of technology and alliances; however, challenges such as pricing of term plans, persistency ratio, income thresholds for agents also need to be addressed to improve the vibrancy and industry growth as well as increasing insurance penetration & density.

Outlook

The outlook for the insurance industry is not just a function of the economic growth but industry-specific factors such as expansion in insurance penetration, evolution, and change in the share of various distribution channels, enabling regulatory movement, also affect the premium growth.

The primary focus of the life insurance industry in FY21 and a sizeable portion of FY22 was on the Covid-19 pandemic. However, with the country finally coming out of the pandemic's clutch, the industry is expected to focus more on the growth story going forward. CareEdge expects the life insurance industry to continue to grow at around 12-14% over a three-to-five-year horizon. The growth drivers include pandemic induced demand for protection plans (additionally repricing of these plans could also impact premium), younger demographic opting for pure protection plans driving insurance coverage, intense push to increase insurance coverage, especially in the rural populace, product innovations/customization, higher demand for retirement products such as pension/annuity coming from an ageing population coupled with low availability of government-sponsored social security mechanisms and rising awareness of retirement planning, and multiple channels being coupled with enabling digitalised payments infrastructure. However, large ticket ULIPs could be impacted as w.e.f. April 2021, income earned on contribution beyond Rs. 2.5 lakh per annum in ULIPs has become taxable thereby reducing the attractiveness of ULIPs and pushing fund flows to the mutual fund ELSS schemes.

Companies are expected to continue to focus on simplifying the life insurance purchase experience and overall digital enablement across the distribution channels while maintaining a razor-sharp focus on cost improvement to sustain margins. However, frauds, lapse ratio, any unfavourable changes in macro-economic factors, and uncertainties in the regulatory landscape could be characterized as key challenges to industry growth. Overall, the outlook is expected to be positive in the medium term.

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About:

CareEdge (CARE Group) is a knowledge-based analytical group that aims to provide superior insights based on technology, data analytics capability and detailed research methods. CareEdge (CARE Ratings Limited) is one of the leading credit rating agencies in India. It has an impressive track record of rating companies for almost three decades and has played a pivotal role in developing the corporate debt market in India. CareEdge provides near real time research on all domestic and global economic developments. The wholly owned subsidiaries include CareEdge Advisory & Research arm focused on providing advisory and consultancy services and CareEdge Risk solutions a platform that provides risk management solutions