Foreign Direct Investment and its Impact on Insurance Sector

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**Abstract**
In the insurance market, Foreign Direct Investments has helped in bringing about the saving habits among the masses which has resulted in creating assets of fixed nature. India being a country with an upcoming economy foreign investor view it as a striking investment opportunity, especially taking into consideration the rapid growth taking place in the country and the every growing need to increase investment in insurance sector. Insurance companies in India constantly face grave problems after witnessing years of high growth owing to expansions without much increase in earnings, constant increase in prices, reforms which are unduly delayed, and the market system with many weaknesses. With the sector facing all these problems, Indians government had decided to liberalize the sector by moving towards the direction of drastic reduction of trade barriers and lifting controls on certain aspects. The Government of India realizing the need to boost the insurance sector decided initially in the year 2005 decided to enhance the FDI in the sector which was then set as 26 percent to an enhanced rate of 49 percent. This rise in FDI was seen to have many implications for the economy of India.

**Keywords:** Foreign Direct Investment, Insurance sector, privatization, growth.
I. INTRODUCTION

Any desired increase in FDI is always to be viewed from different perspectives since it is considered to be double-sided sword. In this dissertation an attempt is made to identity the impact of foreign direct investment in the insurance sector by evaluating the positive and negative aspects of such investments.

Positive impact is evident in the sense that there has been more capital inflow, followed by new players coming into the country, used of latest technological applications, development of innovative concepts and ideas with respect to introduction of new insurance products by employing unique marketing strategy, improvement in employment opportunities for individuals resulting to overall growth and development of the insurance industry.

Though the inflow of such investments in the insurance sector is viewed as a appropriate measure, one should also bear in mind the consequences which may not be favourable. The consequences with negate this opinion includes the fact that this could possibly result in the form of repatriation of profits arising from such investments thereby finally resulting in neglect of social responsibility towards the country people apart from exposing indigenous players to higher levels of risk and competition.

When there is an unfounded increase in the ownership of business in the insurance industry by international players unfortunately, led the country to face the threats which were considered to be disproportionate in relation to the benefits to be enjoyed by developing country like India.

Foreign Direct Investment which typically involves the inflow of foreign capital to be invested in the any economy in order to increase its capacity to tap the potential are generally preferred when compared to other external sources of funding. External source of funding ultimately results in building debt for the economy whereas foreign direct investment does not result in creation of debt and is also considered to be not volatile with return depending to a great degree on the successful implementation of investor-funded ventures.

In order to grow and develop it economy, every country is compelled to make investment in competitive global business environment. FDI as an investment strategy serves a vital role in being a transparent and productive method of involving an international economic system that could rightly serve as a reagent in burning about growth in a country.

FDI inflow play a vital role in rescuing developing nations by creating a clear, widespread and effective framework for policy making by solving their need for going ahead with investments and thereby helping in developing human resources and the structural capacity to enforce the same.
Impact of FDI on Insurance Sector

The positive impact of FDI on insurance sector has been discussed below:

More capital Inflow

FDI could easily help India in getting the desired quantum of long-term capital funds required to make investments in infrastructure building which is vital to ensure India’s economic growth. The prime reason for Indian economy experiencing low growth rate is no doubt the lack of infrastructure. This deficiency could be easily handled with the help of funds brought into the country with the help of the funds that could be raised by the insurance industry. Insurance industry has the capacity to raise long-term funds from the common man as Insurance till date serves as the prime methods of carrying on long-term saving which could easily extent to over 30 years’ time period. Apart from this any FDI in the insurance sector could be taken as an indirect advantage for the Indian economy, which would make available ample long-term funds which could be used to accelerate the rate of growth in the Indian economy.

More Employment Opportunities

In the insurance industry the development scenario provides multiple job openings in the economy. Demand for marketing consultants, accounting specialists, human resources practitioners, statisticians etc. is rising. The sector also hires professionals in the latest specialization fields such as underwriting, litigation, accounting, actuarial accounting etc.

Higher Growth Rate

Any FDI made in the insurance sector is definitely likely to enhance the rate of penetration of insurance activities in India, as penetration made by the insurance sector is considered to be dreadfully minimum with the collection of insurance premium being just equal to 3 per cent of the Gross Domestic Product in India. This when compared with other countries of the world is seen to be averaging somewhere around 8 per cent. Thus, effort would be required on the part of MNCs to formulate a strategy through which extent of penetration could be increased by improved product creation, awareness for customers etc.

Linkage Effect

Insurance-related service-domains such as seminars, conferences, risk evaluation and ranking and risk management have evolved significantly enabling the industry to pursue the new sectors. In addition to this, the increase in insurance players will significantly boost related fields such as advertising, brand building, etc. which would in turn promote the ancillary industries.

Introduction of Innovative Products with Improved Customer Service

Inviting FDI in the insurance industry could, in many ways, be beneficial for customers. Increasing the FDI cap would positively affect a number of industries. Consumers will be able to obtain better, more innovative and more competitive products and better quality of service. They’ll have options open to make a smarter decision.
Optimum Utilization of Resources

India has a pool of wealth that are not being adequately used because of lack of money, lack of technology, etc. FDI aims to allow optimal resource use. International players have the resources, technologies, and skills necessary to make better use of the same.

Latest Technology

FDI also fetches new ways of drawing consumers in the insurance industry by offering various creative schemes. The new players have begun a wide range of goods that call for selling technologies based on needs.

Moving towards Global Practices

Insurance sector in India was at one point of time terribly staggering behind when compared with other economies of the world especially with respect to the extent of penetration. Thanks to the flow of FDI into the insurance sector, Today India is seen to be only 3.1 percent lagging behind the penetration level of insurance business in the UK which is 12.5 per cent, Japan's 10.5 percent, Korea's 10.3 percent, and the US's 9.2 percent. Currently FDI represents only Rs. 827 crores of the private life insurance companies' Rs.3179 crore capitalizations.

Healthy Competition

The insurance sector in India is staggering behind other economies of the world with respect to the basic steps taken to ensure penetration of insurance benefit. With India providing a cover of 3.1% to its people it is way behind the penetration percentage enjoyed by other countries. For example, it is seen to be 12.5% in the United Kingdom, 10.5% in Japan, 10.3% in Korea and 9.2% in the United States. At present, as far as India is concerned, FDI stands at Rs. 827 crores of the total capitalization figure of Rs.3179 crore made in private life insurance companies.

Infrastructure facilities

The primary aim of life insurance is to leverage collective assets for sustainable growth through long-term social and infrastructure investments. Opening the insurance sector to FDI would require tremendous influx of funds through the infrastructure.

Fresh approaches in Risk Management

The nation would also benefit from expanded FDI ceiling in the insurance industry by creating new employment, innovative risk management practices and product creativity.

NEGATIVE IMPACT

FDI & Efficiency of Insurance Companies

With the opening of this insurance market to private investment in 11999, an invite was made to allow private firms to invest a maximum of 26 per cent in the form of foreign equity in the insurance sector. Taking advantage of the invite, 12 private sector companies came forward to have tie-ups in the life insurance business. In comparison to the HDFC, which has 18.6 percent foreign equity, the other private
firms have 26 percent foreign equity. 8 private firms have joined general insurance, 6 of them have 26 per cent international funding.

Reliance and Cholamandalum Insurance companies are amongst the private players who have no investment in the form of FDI with respect to general insurance. Though the life insurance market leader LIC was able to achieve a business to the tune of having a surplus fund of Rs.9620 crores (after tax), the total loss of business by private life insurers reached a figure of Rs. 38633 lakhs.

In the year 2002-03, four out of eight private general insurance companies together recorded huge negative profits, with the Reliance Insurance company which without foreign investment, emerged as the most profitable player. On the other hand, the other six general insurance companies with the backup of foreign investments incurred a net loss amounting to Rs. 294 lakhs whereas the public sector general insurance companies all put together were able to achieve a total profit which after deduction of taxes amounted to Rs. 62570 lakhs.

Credibility of foreign companies

On account of the world witnessing a global financial crisis on account of which many companies which includes AIG, Lehman Brothers and Goldman Sachs failed miserably, the expectation that FDI will bring along with it the expertise of international companies which would be more professional for being absorbed by the existing system has become highly questionable. Even Prudential Financial Services (ICICI's partner in India) was in fact earlier challenged with an inquiry by U.S. Securities and Insurance Regulators based on contentions which related to the falsification of records by forgery of signatures which was possible on account of customers being requested to sign blank applications.

The matter came to light when it made a settlement amounting to $2.6 billion in order to pay off a class action case which sought to challenge a practice of selling false insurance policies in 1997 and had to pay a fine to the tune of $65 million fine to the State Insurance authorities in 1996. AMP ended its New Corporate Life activities in June 2003. And in 2002 the Royal Sun Partnership shut down its profitable companies.

A new study by a consultant, Mercer Oliver Wyman, showed that a whopping 60 billion Euros was short of funding for European life insurance firms. The situation in Germany, Switzerland, France and Britain is such that insurance companies face a lot of hardships on account of having to face the risk associated with capital insufficiency which is the result of volatility in the activities of equity and bond securities in the past, according to the study conducted by Mercer Oliver Wyman. Thus, it goes without saying that FDI in the Indian Insurance sector is without doubt going to expose the financial markets to the uncertain and speculative activities of the foreign insurance companies.
Repatriation of profits

Without doubt, FDI inflows favour the host nation, but the outflows in the form of tax remittances (investment gains that are repatriated to the country of origin) often adversely affect the region. Most of the sales go out of the home world.

Scope for channelizing savings

The primary roles of insurance business mobilization of funds at the national level and channelization of such funds into investments in various sectors of the economy so that the same is able to boost economic growth. Nevertheless, there continues to have been little major improvement in the accumulation of investments by the insurance industry, particularly though the insurance market liberalized in 1999.

The primary aim of life insurance is to leverage investments in long-term investment in social and services sectors for the economic growth. The same dream was argued that the insurance sector opening to require massive influx of funds into investments in building infrastructure. But sadly, more than fifty per cent of the programs offered could be classified as ULIPS where the savings go to the stock markets. According to a survey, during 2003-04, 95 percent of policies sold by Birla Sun Life and more than 80 percent of policies sold by ICICI Prudential were ULIP. As per the provisions of these programs, about half of these funds are invested in equity securities thus, imposing a restriction on the spending funds for infrastructural development.

At the other hand, as at 31.3.2003, Rs.40,000 crore was spent by LIC in power generation, developing roads, improving water supply, increasing housing and other social-sector facilities. Apart from this, IRDA statistics indicate the position of public sector life and non-life insurance undertakings in infrastructure spending to be greater than market share of such companies. Even though FDI limits were pegged at 26 per cent, contributions made by the insurance industry to the Indian transportation sector were seen to come mostly from the funds of only public sector insurance companies.

ISSUES IN FDI IN INSURANCE SECTOR

Efficiency of the organizations with FDI

With the opening of the insurance sector for private players in the year 1999, it gave them scope for having external valuation of up to 26 per cent. Soon after this, 12 private sector companies joined the business of disaster security. Apart from the HDFC, which has a remote interest of 18.6 cents, the various private-owned corporations have an external value of 26 per pound. As a result, defense reached 8 privately held companies, 6 of which have an average value of 26 per cent. If one was to accept fact, it should be noted that 6 remote-value private players cumulatively incurred a total loss of Rs. 294 lakhs.

Credibility of outside organizations

With the world being exposed to monetary emergency as a result of which firms like AIG, Lehman Brothers and Goldman Sachs crumbled, the contention that existed was that external organizations might stand to gain and demonstrate more skill in the situation which is highly disputable. Earlier, the Prudential Financial Services
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(ICICI's Indian accomplice) also confronted an inquiry by U.S. securities and protection controllers in view of claims that they had misrepresented reports and produced marks, and demanded that their customers sign clear structures. A consultant finds that European organisations for the defense of disasters shy around €60 billion of money.

According to the Mercer Oliver Wyman Study, companies in Germany, Switzerland, France and Britain are exposed to safety net suppliers on account of which they suffer from the ill effects of risky capital deficiency, which is an after-effect of formerly following irresponsible investment in valuation and bond instruments.

Consequently, FDI in India is sure to lead to an exposure of our monetary markets to foreign insurance agencies' uncertain and hypothetical movements when the diseases of handling these exercises are investigated in the propelled countries.

Greater channelization of sparing to protection

A prominent of the protection division's very vital responsibilities is to trigger national sparing and channel it into interests in various economic areas. Be that as it may, the extent to which the stimulation of funds by the protection part is concerned, even after the advancement of the protection part in 1999, does not seem to have happened to any huge change. In this case the private or public purpose did not possess the power to accomplish the objective.

Flow of assets to framework

The primary point in catastrophe safety is related to enabling funds for long-haul involvement in social and foundation divisions in order to boost the economy. A similar dream for opening the defense market will unleash enormous stream of funds into the system was contended. As it is, over 50% of the schemes they have on offer are typically ULIPS. When one investigates into the value markets IRDA figures, further it can be understood that the offering made to the general population division life and non-disaster protection organisations is underpinning interest in more prominent than their piece of industry as a whole.

Points of Interest of FDI in Insurance Sector

By having higher and greater protection the scope for growth in FDI would expand protection infiltration in India, where protection entry is terribly low with protection premium at around 3 per cent of GDP compared to around 8 per cent of normal worldwide. This would be better by MNCs advertising exertion, better item advancement, shopper training, etc.

In the benchmark measure of defense penetration, Heading Towards Multinational Activities Indian security advertises lingers behind various economies. India is well behind the UK's 12.5 percent at just 3.1 percent, Japan's 10.5 percent, Korea's 10.3 percent, and the US's 9.2 percent. For now, FDI is just referring about Rs. 827 of the Rs.3179 crores of private extra capitalizations. Provide Consumers with Cheaper Goods, More Options and Higher Service Rates From a variety of points of view, opening up the FDI in the Security market would be beneficial to buyers. Expanding FDI would in a good way impact a large measure of businesses.
IV. SUGGESTIONS AND CONCLUSION

The policy makers are suggested to ensure optimum use of funds and timely implementation of projects. As Indian rupee appreciation on the foreign market provides the policy makers with a golden opportunity to draw more FDI in Undeveloped projects relative to Brownfield spending. So, the government must invite Greenfield investments. Realization of approved is also observed. India should consciously work towards attracting more FDI to R&D as a means of reinforcing technological prowess and competitiveness in the country.

Many international studies have estimated that in the next ten years the insurance sector in India could grow by more than 125 per cent. India was actually recognized as one of the fastest developing protective markets. The present strategy aims to promote collaborative activities in the defense sector in order to assist the growth of the local safety net provider here. In addition, there is the risk that some remote guarantors will not be involved in contributing unless they have 100 percent ownership and the present arrangement will prevent them from choosing India as an insurance objective.

Insurance sector growth will also assist in the development of other sectors and in providing the government with capital for long-term infrastructure projects. Cross-country research also supports the rise in FDI limits as sector caps were higher than India for insurance only in China and a few other industries, though countries such as Brazil and Russia have higher sector caps than India in most industries.

The main strengths of our economy are heavy domestic demand, rural health, schooling, mobility, high savings, low export reliance, emerging middle class, favorable demographics, talent pool and intellectual capital. Some bottlenecks, however, started to emerge somewhere down the line, as we didn’t pay enough attention to reengineering and making our institutions contemporary with growing needs and changing environment. Creating an administrative and financing system and the current change is one of the core needs. FDI hiking marks a positive step in the right direction.

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