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Rural Market in India: An Unexplored Terrain

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# MICRO INSURANCE – MACRO COVERAGE

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***ABSTRACT***

*Insurance is the backbone of a country's risk management system. The insurance providers offer a variety of products in order to provide protection from risk and to ensure financial security. Micro insurance is the tool that protects rural as well as poor urban people by offering low cost insurance to mitigate their risk. . Micro-insurance is the lowest premium and low coverage insurance policies for people with low income. The products of micro insurance are designed with the objective of protecting people that are generally ignored by traditional insurance products. With the opening up of the economy and as per the regulation of IRDA, public as well as the private insurance companies try to expand their business in the rural market In this paper an attempt has been made to evaluate the present position of micro insurance in India, its various delivery mechanisms and its role in respect of risk mitigation and economic upliftment.*

***Keywords: Awareness, Delivery mechanisms, Economic upliftment, Micro-Insurance Products.***

## 1. Introduction

Micro insurance has been seen as one of the major risk managing tools for the poor and low income groups and a potential market for business. Experiences across countries in the world show that micro insurance has potential to reduce household risk impacts and to provide business opportunity. By offering a payout after the loss, it may avoid more costly ways of risk coping by the poor household and leaves their future income earning opportunities intact. The sense of security linked to being insured through micro insurance augment household welfare with positive impacts. Poverty and vulnerability among low income groups mainly stems from their poor risk management capacity and exclusion from the financial markets. Hence it is important to understand their need as well as demand for financial products including insurance. Many poor, rural and low income households may involve in activities or enterprises of smaller scale but higher risk and uncertainty. It makes them disadvantageous because they are more prone to economic and financial collapse. Under this situation it is interesting to analyze how micro insurance can play a meaningful role in household risk managing efforts, in rural credit and insurance market and providing business opportunity. In this regard focus is on current scenario of out-reach and efficacy of micro insurance in India, major factors that encourage and prevent growth of micro insurance and other related issues for achieving broader objectives such as financial inclusion and inclusive development.

There are today 27 general insurance and 24 life insurance companies in India. Keeping in mind concerns that a competitive, open environment could lead to the neglect of the rural and weaker sections of India, the Insurance Regulatory and Development Authority of India (IRDA) passed the

IRDA (Obligation of Insurers to Rural or Social Sectors) Regulations Act in 2002. After that, every insurance company was required to engage with the rural and social sectors by complying with mandatory obligations.

The IRDA regulations set rural insurance targets for each company. These require that 7 per cent of all life insurance business should be generated from the rural social sector in the first financial year, and this should increase annually to reach 18 per cent by the sixth financial year. For general insurance, 2 per cent of insured premium in the first financial year should be from rural social business, increasing annually to 5 per cent in the sixth year.

India is one of the first countries to adopt micro insurance formally through the Micro insurance Regulations Act in 2005. The regulation sets boundaries for the cost and coverage of the product and provides clarity about distribution mechanisms. Insurers in both the public and private sector, while meeting the obligations, have brought in significant innovations in products and processes to serve the poor and rural areas.

**2. Objectives -** The objectives of the study are

- To understand micro insurance.
- To study the role of micro insurance for economic upliftment of rural India.
- To understand the various risk coverage offered through its various policies.
- To identify activity the delivery mechanisms to promote micro insurance.
- To examine the problems for growth of micro insurance.
- To suggest some implementable suggestions for facilitation of desired growth and outcome of the micro insurance sector.

**3. Methodology -** The study is based on secondary data with reference to various journals, articles and other online resources.

**4. Understanding Micro insurance -** A micro-insurance policy is a general or life insurance policy with a sum assured of Rs.50,000 or less.

**4.1 A general micro-insurance product include**

- Health insurance contract
- Any contract covering belongings such as
- Hut
- Livestock
- Tools or instruments or
- Any personal accident contract
- They can be on an individual or group basis

**4.2 A life micro-insurance product is**

- A term insurance contract with or without return of premium
- Any endowment insurance contract or
- A health insurance contract
- They can be with or without an accident benefit rider and
- Either on an individual or group basis

There is flexibility in the regulations for insurers to offer composite covers or package products that include life and general insurance covers together.

**5. Intermediaries -** The micro-insurance portfolio has made steady progress. More life insurers have commenced their micro-insurance operations and many new products are being introduced every year. The distribution infrastructure has also been considerably strengthened and the new business has shown a decent growth, though the volumes are still small. Micro- insurance business is done through intermediaries like Non-Government Organisations, Self-Help Groups and Micro-Finance Institutions.

## 6. Micro insurance Delivery Models

One of the greatest challenges for micro insurance is the actual delivery to clients. Methods and models for doing so vary depending on the organization, institution, and provider involved. As Dubby Mahalanobis states, one must be thorough and careful when making policies, otherwise micro insurance could do more harm than good. In general, there are four main methods for offering micro insurance the partner-agent model, the provider-driven model, the full-service model, and the community-based model. Each of these models has their own advantages and disadvantages.

**7.1. Partner agent model**: A partnership is formed between the micro insurance (partner as MFI) scheme and an agent (insurance companies), and in some cases a third-party healthcare provider. The micro insurance scheme is responsible for the delivery and marketing of products to the clients, while the agent retains all responsibility for design and development. In this model, micro insurance schemes benefit from limited risk, but are also disadvantaged in their limited control. Micro Insurance Centre is an example of an organization using this model.

**7.2. Full service model**: The micro insurance scheme is in charge of everything; both the design and delivery of products to the clients, working with external healthcare providers to provide the services. This model has the advantage of offering micro insurance schemes full control, yet the disadvantage of higher risks.

**7.3. Provider-driven model**: The healthcare provider is the micro insurance scheme, and similar to the full-service model, is responsible for all operations, delivery, design, and service. There is an advantage once more in the amount of control retained, yet disadvantage in the limitations on products and services.

**7.4. Community-based/mutual model**: The policyholders or clients are in charge, managing and owning the operations, and working with external healthcare providers to offer services. This model is advantageous for its ability to design and market products more easily and effectively, yet is disadvantaged by its small size and scope of operations.

## 8. Challenges

Major challenges for insurance industry in India are low insurance intake, low renewal, lack of awareness and delivery channels, particularly for lower segments and in rural areas.
During last few years reduced demand particularly in non-life segment, low interest rates and the need for additional capital by many insurance companies accentuated the performance of the sector (IRDA 2009). As recent global economic downturn has affected the performance of insurance sector worldwide, it is also reflected in terms of two important insurance performance indicators such as

insurance penetration and insurance density. Insurance penetration measures the level of insurance activity relative to the size of the economy.

**8.1.** There are specific reasons for low demand for insurance in spite of intense need. Suppliers have their own concerns which help to explain why there have been so little efforts at market development. Consequently, the rural market is characterized by limited and inappropriate services, inadequate information and capacity gaps.

**8.2.** There are challenges in product design, which has resulted in a mismatch between needs and standard products on offer. Efforts at product development / diversification have been limited.

**8.3.** Pricing, including willingness to pay and the availability of subsidies, influence the market. In the absence of a historical data base on claims, premium calculations are based on remote macro aggregates and overcautious margins. Building and sharing claims histories can help in aligning pricing decisions with actuarial calculations, thereby reducing prices.

**8.4**. Difficulty in distribution is one of the most cited reasons for absence of rural insurance. The high costs of penetrating rural markets, combined with underutilization of available distribution channels, hinder the growth of rural insurance services. This adds to costs, both, managerial and financial. Like inclusive credit, inclusive insurance is expected to be a “low ticket” business, requiring volumes for viability.

**8.5** Cumbersome and inappropriate procedures inhibit the development of this sector.

**8.6** Contrasting perspectives of the insured and the insurers, lead to low customization of products and low demand for what is available.

## 9. Recommendations

### 9.1 Leveraging Existing Network for Micro-Insurance

It would be difficult for the insurers to establish a vast network for distribution of micro-insurance products. They need to utilize existing Government organizations, banks, MFIs, NGOs and SHGs to increase the outreach of micro-insurance to the poor. The advantages of these entities are that they find greater acceptability among the financially excluded, and with a better understanding of their needs are well equipped to advise them on the choice of products. In India with a vast rural population characterized by challenges and complexities, it makes sense to latch on to an existing mechanism operating in these Segments to lower costs and to help the insurer to leverage on the faith already generated by the entity. Hence it would be prudent to choose a partner-agent model for delivery where the insurer underwrites the risk and the distribution is handled by an existing intermediary. This model keeps the cost of insurance attractive enough for the poor to enter and remain in its fold even while addressing the concern of the insurers about the low returns of micro-insurance.

### 9.2 Linking Micro-credit with Micro-insurance

It is becoming increasingly clear that micro-insurance needs a further push and guidance from the Regulator as well as the Government. The Committee concurs with the view that offering microcredit without micro-insurance is bad financial behaviour, as it is the poor who suffer on account of such bad product design. There is, therefore, a need to emphasise linking of microcredit with micro-insurance. Linking micro-insurance with micro-finance makes good business sense. Further, as it helps in bringing down the inherent risk cost of lending, the Committee feels that

NABARD should be regularly involved in issues relating to rural and micro insurance to leverage on its experience of being a catalyst in the field of micro-credit.

### 9.3. Implementation Strategy for Micro-Insurance

The five major areas for formulation of strategies for effective implementation of micro-insurance programme can be the following:

#### 9.3.1 Human Resources Requirement and Training

As indicated earlier, the UNDP report states that there is a huge untapped market – of around 950 million people and nearly US$2 billion – for insurance in India. IRDA may consider putting in place an appropriate institutional structure for deciding on service packages including premia and formulating strategies for effective promotion of micro insurance. There is also a felt need for development, of both full-time and part-time staff, through effective training in insurance marketing and servicing concepts.

#### 9.3.2 Operations and Systems

To address the requirements of the huge market potential available, appropriate systems should be evolved for tracking client information, either manually or using technology. While a technology platform may take time for setting up, in the long-run, the same will be cost-effective and reliable. Similarly, the procedures for premium payments, claims and other services should be formalized along with increased customization of products to stimulate demand.

#### 9.3.4. Development of Adequate Feedback Mechanism

Keeping in view the diverse nature of market requirements, suitable mechanisms to collect market intelligence, collating and interpretation of the same, in a formally structured manner, is important for product development and process refinement.

Insurance companies should go beyond devising new products to improving their processes for building awareness, marketing enrollment, premium collection, claim settlement and renewal. For this they need use innovative channels such as business correspondents, SHGs, NGOs and MFIs as also cooperatives and mutual associations. Further, the use of technology such as mobile phones and ATMs for premium collection should be encouraged to keep transaction costs low.

#### 9.3.5. Development of Data Base

High costs of penetration and acquisition often leads to higher pricing of products, thereby impacting client outreach and market depth. Building up historical data base on risk profiles, claims, settlement ratios, etc., will facilitate in better pricing of products, based on actual rather than presumed risks. Besides enabling cost reduction, warehousing of such data will make the market more transparent for entry of more operators. The IRDA and the Government should help in provision of data such as human mortality and morbidity, weather parameters and livestock mortality/morbidity, on a timely, large sample and regular basis. This will lead to finer pricing on actuarial basis and eventually cut costs of insurance.

### 9.4 Consumer Education, Marketing and Grievance Handling

The micro-insurance sector is unique in the sense that there is an ongoing challenge to explain the concept and benefits to the insured. Creating awareness through use of pictorial posters, local folk arts and street theatres might be useful to explain the mechanisms of insurance. Local community-based organisations could organize premium collections, as they have better access to the local people. To make it more acceptable to the people, micro-insurance products, apart from covering only risks, should also provide an opportunity for providing long term savings (endowment).

### 9.5. Other Recommendations

#### 9.5.1. Product Development / Process Re-engineering

Customised product development to suit the varying requirements of the local populace is a pre-requisite. The processes / procedures are to be streamlined and simplified, to facilitate easier access for the rural poor. Information should be made available in vernacular for easy understanding of the terms on offer.

#### 9.5.2. Building Data Base

With a view to bringing down product costs, building data base of claim histories, risk profiles, etc., are to be undertaken. This will also help in aligning pricing decisions with actuarial calculations.

#### 9.5.3. Using Existing Infrastructure

Micro-insurance service providers can use the existing banking infrastructure and also adopt the agency-mode (NGOs, SHGs, NBFCs, etc.) for providing services, thereby leveraging on the existing physical branch network and reducing costs.

#### 9.5.4. Use of Technology

The technology platforms being envisioned to facilitate financial inclusion should enable micro-insurance transactions also. Towards this end, there is a need to integrate the various modules - savings, credit, insurance, etc. - into the technology framework so that holistic inclusive efforts are possible in the rural areas.

#### 9.5.5. Review of existing schemes

There are a large number of group life and health insurance schemes which are run by various central ministries and State Governments. The level of actual coverage in terms of claims preferred and settled in such schemes is disturbingly low. These schemes should be reviewed by an expert group set up by the IRDA.

**9.6**. The above are general recommendations. However, with reference to specific Segments, the following are the recommendations:

#### 9.6.1 Life Insurance

A wide range of products are available but penetration is really limited in rural areas. The procedural requirements at the time of entry and in case of claims settlement are cumbersome. The commission structure for agents is also heavily weighted in favour of getting new policies with very little incentive to service existing policies. In this regard, Micro Insurance Guidelines (MIG) 2005 issued by IRDA has provided for equal commission throughout the life of a policy and this will now remove the disincentive in servicing existing policy holders.

#### 9.6.2. Health Insurance

In case of Health Insurance, penetration level is even much lower than Life Insurance. The two categories viz., Critical Illness and Hospitalisation are the main product segments. Some State Governments have developed Health Insurance schemes which are still in very early stages. Mutual health insurance models have advantages of its members performing a number of roles such as awareness creation, marketing, enrolment, premium collection, claims processing, monitoring, etc. Under this arrangement, the costs of offering small-ticket health insurance gets significantly reduced. The high covariant risks such as epidemics will have to be taken care of by a mutual entity taking reinsurance for such risks. IRDA has also suggested that the capital requirements for stand-alone health insurance companies be reduced to Rs.50 crore as against Rs.100 crore for Life Insurance Companies.

#### 9.6.3. Crop Insurance

This is a very important risk mitigation arrangement for small and marginal farmers. However, the present scheme suffers from very serious implementation problems. Leaving the discretion to notify crops/regions to state governments has contributed to adverse selection. Further, claims settlement based on yield estimation has been cumbersome and the sampling area for crop cutting experiments is very large. An alternative model based on weather insurance has been attempted. Farmers are happier with it because of quick settlements. On the down side premium rates are very high. Further, due to low density of weather stations, the problem of large area averaging is a critical factor even with weather insurance. To counter this, there is a need for having a large number of smaller weather stations. Policies need to be evolved to make crop insurance universal, viz., applicable to all crops/regions and pricing actuarial.

**9.6.4. Livestock Insurance**

As in Life Insurance, the problem lie s in the process of enrolment and claims settlement. Several pilots indicate that the involvements of local organisations like SHGs, dairy co-operatives, NGOs and MFIs improves the quality of service, reduces false claims and expedites claims settlement. These experiences need to be studied and adopted by insurance companies.

**9.6.5. Asset Insurance**

This could cover a wide range including residential buildings, farm and non-farm equipments and vehicles. For poor households, insurance for a hut, irrigation pump, a handloom or a bullock cart could have considerable economic significance. Products are available but penetration levels are negligible. The main constraint seems to be lack of distribution channels appropriate for lower income groups. Involving local NGOs, MFIs, SHGs, etc. as distribution channels as well as facilitators of claim settlements would be quite useful.

**9.6.6**. Other ways to increase micro insurance coverage in rural areas would be (i) co-payment models; (ii) increasing client value with products such as health screening, tele-medicine, no claim discounts; (iii) mobile enrolments; (iv) exploring exciting distribution channels such as internet kiosks; and (v) introducing products such as weather-based insurance, rainfall-index insurance.

## 10. Conclusion

Micro-insurance is believed to work as a powerful risk management tool for low income and vulnerable groups by preventing them from falling into the poverty trap. But not much is known about outreach and efficacy of micro-insurance across regions and groups in India, though government plays a proactive role in providing insurance cover to the poor through subsidized insurance schemes and other programmes. The size and potential of micro-insurance market is enormous due a sizeable portion of poor and low income population who live without any formal insurance. Micro insurance is the need of the hour and a proper implementation will benefit everyone in the society. It is evident that this sector influenced by the rural and urban areas of weaker sections obligations. Micro insurance holds much hope for extension of protection to millions of resource-poor in India.

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