2018

IASbaba

[INDIAN ECONOMY-SET 5 BLOCK 1]

Integrated Learning Programme 2018 is a step towards 'Enabling a person located at the most remote destination a chance at cracking AIR 1 in UPSC/IAS'

Contents

Security Market in India

Note: Do not go deep into security market system. For examination point of you the associated topics are not that important baring few that will be discussed here. Focus on few terms and concepts only.

Industry & Infrastructure (part of economy) in detail will be covered post Prelims (Important for Mains) - Value Add will be provided once Economic Survey is released

History

Securities are financial instruments issued to raise funds. The primary function of the securities markets is to enable to flow of capital from those that have it to those that need it. Securities market help in transfer of resources from those with idle resources to others who have a productive need for them.

Securities Market in India is very well developed and this is largely due to several policy initiatives since 2000, which have created a vibrant environment for all types of investors. Today, India is second only to the United States in terms of number of listed companies.

The present capital market scenario features

- an advanced regulatory environment
- steadily increasing market capitalisation
- better allocation and mobilisation of resources
- a rapidly developing derivatives market
- a robust mutual fund industry
- increased issuer transparency.

As per the Securities Contracts (Regulation) Act, 1956, securities include

- shares
- bonds
- scrips
- stocks

- other marketable securities of like nature in or of any incorporate company or body corporate
- government securities
- derivatives of securities
- units of collective investment scheme
- interest and rights in securities
- security receipt
- any other instruments so declared by the central government.

1947

- Capital Issues (Control) Act, 1947

1956

- Securities Contracts (Regulation) Act, 1956
- Companies Act, 1956

1992

- Repeal of Capital Issues (Control) Act, 1992

SEBI Act, 1992 to:

- protect interest of investors
- promote development of securities market
- regulate the securities market

SEBI has powers

- to investigate and examine companies
- to visit their premises
- to inspect records and personnel and
- to impose penalties that are commensurate with any misconduct.

Primary and Secondary Markets

The primary market is concerned with the floatation of new issues of shares or bonds. The firms floating new issues to raise funds may be new companies or existing companies planning expansions.

The primary market is where securities are created. It's in this market that firms sell (float) new stocks and bonds to the public for the first time. For our purposes, you can think of the primary market as the market where an initial public offering (IPO) takes place. Simply put, an IPO occurs when a private company sells stocks to the public for the first time. The primary market is also the market where governments or public sector institutions raise money through bond offerings.

The important thing to understand about the **primary market is that securities are purchased directly from an issuing company.**

The secondary market commonly referred to as the "stock market." This includes the New York Stock Exchange (NYSE), Nasdaq and all major exchanges around the world. The defining characteristic of the secondary market is that investors trade among themselves.

That is, in the secondary market, **investors trade previously issued securities without the issuing companies'** involvement. For example, if you go to buy Microsoft stock, you are dealing only with another investor who owns shares in Microsoft. Microsoft is not directly involved with the transaction.

Stock Exchange

National Stock Exchange of India Ltd (NSE)

- The National Stock Exchange (NSE) is the leading stock exchange in India and the fourth largest in the world by equity trading volume in 2015, according to World Federation of Exchanges (WFE).
- **It began operations in 1994** and is ranked as the largest stock exchange in India in terms of total and average daily turnover for equity shares every year since 1995, based on annual reports of SEBI.

Bombay Stock Exchange (BSE)

The first and largest securities market in India, the Bombay Stock Exchange (BSE) was established in 1875 as the Native Share and Stock Brokers' Association.

Based in Mumbai, India, the BSE lists close to 6,000 companies and is one of the largest exchanges in the world. The BSE has helped develop the country's capital markets, including the retail debt market, and helped grow the Indian corporate sector.

Legislation to control Security Market in India

The four main legislations governing "the securities markets are:

(a) the SEBI Act, 1992 which establishes SEBI to protect investors and develop and regulate securities market;

(b) the Companies Act, 1956, which sets out the code of conduct for the corporate sector in relation to issue, allotment and transfer of securities, and disclosures to be made in public issues;

(c) the Securities Contracts (Regulation) Act, 1956, which provides for regulation of transactions in securities through control over stock exchanges; and

(d) the Depositories Act, 1996 which provides for electronic maintenance and transfer of ownership of demat securities.

Securities Contracts (Regulation) Act, 1956:

- It provides for direct and indirect control of virtually all aspects of securities trading and the running of stock exchanges and aims to prevent undesirable transactions in securities. It gives Central Government regulatory jurisdiction over (a) stock exchanges, through a process of recognition and continued supervision, (b) contracts in securities, and (c) listing of securities on stock exchanges.
- As a condition of recognition, a stock exchange complies with conditions prescribed by Central Government. Organised trading activity in securities takes place on a specified recognised stock exchange. The stock exchanges determine their own listing regulations, which have to conform to the minimum listing criteria set out in the Rules.

Companies Act, 1956:

- It deals with issue, allotment and transfer of securities and various aspects relating to company management. It provides for standards of disclosure in public issues of capital, particularly in the fields of company management and projects, information about other listed companies under the same management, and management perception of risk factors. It also regulates underwriting, the use of premium and discounts on issues, rights and bonus issues, payment of interest and dividends, supply of annual report and other information.

Companies Act, 2013:

The Companies Act 2013 is an Act of the Parliament of India which regulates incorporation of a company, responsibilities of a company, directors, dissolution of a company.

The Act has replaced The Companies Act, 1956 (in a partial manner) after receiving the assent of the President of India on 29 August 2013.

The Act came into force on 12 September 2013 with few changes like earlier private companies maximum number of member was 50 and now it will be 200. A new term of "one person company" is included in this act that will be a private company and with only 98 provisions of the Act notified.

New concepts

- One Person Companies (OPC)
- Women Directors (second proviso to sec 149(1) or 149 subsection read with rule 3 of companies (appointment and qualifications of directors rules, 2014)
- Corporate Social Responsibility
- Registered Valuers
- Rotation of Auditors
- Class Action
- Dormant Company sec 455(1)
- Fast Track Mergers
- Serious Fraud Investigation Office
- **One Person Company** is a company with only one person as a member. That one person will be the shareholder of the company. It avails all the benefits of a private limited company such as separate legal entity, protecting personal assets from business liability, and perpetual succession. One Person Company (OPC) is a Company registered with ONLY ONE PERSON as its shareholder. An OPC is classified as a private company under Companies Act.

- **Woman Director:** Every Listed Company and Public Company with paid up capital of Rs 100 Crores or more / Public Company with turnover of Rs 300 Crores or more shall have at least one Woman Director.
- **Corporate Social Responsibility Clause** (135): Every company having net worth of rupees five hundred crore or more, or turnover of rupees one thousand crore or more or a net profit of rupees five crore or more during any financial year shall constitute a Corporate Social Responsibility Committee of the Board consisting of three or more directors, out of which at least one director shall be an independent director.

Securities and Exchange Board of India (SEBI)

SEBI Act, 1992:

The Securities and Exchange Board of India (SEBI) is the regulator for the securities market in India. It was established in the year 1988 and given statutory powers on 30 January 1992 through the SEBI Act, 1992.

- The SEBI Act, 1992 was enacted to empower SEBI with statutory powers for (a) protecting the interests of investors in securities, (b) promoting the development of the securities market, and (c) regulating the securities market. Its regulatory jurisdiction extends over corporates in the issuance of capital and transfer of securities, in addition to all intermediaries and persons associated with securities market.
- It can conduct enquiries, audits and inspection of all concerned and adjudicate offences under the Act. It has powers to register and regulate all market intermediaries and to penalise them in case of violations of the provisions of the Act, Rules and Regulations made there under. SEBI has full autonomy and authority to regulate and develop an orderly securities market.

The Preamble of the Securities and Exchange Board of India describes the basic functions of the Securities and Exchange Board of India as **"...to protect the interests of investors in securities and to promote the development of, and to regulate the securities market and for matters connected there with or incidental there to".**

SEBI has to be responsive to the needs of three groups, which constitute the market:

- the issuers of securities
- the investors
- the market intermediaries.

SEBI has three functions rolled into one body: quasi-legislative, quasi-judicial and quasi-executive.

Depositories Act, 1996:

- The Depositories Act, 1996 provides for the establishment of depositories in securities with the objective of ensuring free transferability of securities with speed, accuracy and security by (a) making securities of public limited companies freely transferable subject to certain exceptions; (b) dematerialising the securities in the depository mode; and (c) providing for maintenance of ownership records in a book entry form. In order to streamline the settlement process, the Act envisages transfer of ownership of securities electronically by book entry without making the securities move from person to person.
- The Act has made the securities of all public limited companies freely transferable, restricting the company's right to use discretion in effecting the transfer of securities, and the transfer deed and other procedural requirements under the Companies Act have been dispensed with.

Prevention of Money Laundering Act, 2002:

- The primary objective of the Act is to prevent money-laundering and to provide for confiscation of property derived from or involved in money-laundering. The term money- laundering is defined as whoever acquires, owns, possess or transfers any proceeds of crime; or knowingly enters into any transaction which is related to proceeds of crime either directly or indirectly or conceals or aids in the concealment of the proceeds or gains of crime within India or outside India commits the offence of money-laundering.
- Besides providing punishment for the offence of money-laundering, the Act also provides other measures for prevention of Money Laundering. The Act also casts an obligation on the intermediaries, banking companies etc. to furnish information, of such prescribed transactions to the Financial Intelligence Unit-India, to appoint a principal officer, to maintain certain records etc.

Forward Market Commission

Note- FMC has been merged with SEBI in 2015

Merger of Forward Market Commission and SEBI

In the first ever merger of two regulators, commodities regulatory body Forward Markets Commission (FMC) merged with the capital markets watchdog SEBI.

This merger between the SEBI and the FMC was planned by the Congress Government and has its roots in the Union Budget 2014-15

The merger was precipitated with the National Spot Exchange Ltd. scam, which involved a payment crisis of more than Rs. 5000 crore. This was considered a regulatory failure by the FMC.

The merger was done to improve the market regulation in the country, in turn improving business environment.

The FMC has been regulating commodities markets since 1953, but lack of powers has led to wild fluctuations and alleged irregularities remaining untamed in this market segment.

This is the first major case of two regulators being merged.

Revamped Role of SEBI:

The commodity futures market in India is now supervised by SEBI, making for an integrated regulation of both the securities and commodities markets in India.

SEBI was set up in 1988 as a non-statutory body for regulating the securities markets, while it became an autonomous body in 1992 with fully independent powers.

FMC, on the other hand, has been regulating commodities markets since 1953, but lack of powers has led to wild fluctuations and alleged irregularities remaining untamed in this market segment.

This merger is a key test as the proposed merger of the insurance and pension regulators will hinge on the success of this.

What counts ultimately is the quality of regulation and the credibility and respect which a regulator draws from the market or those being policed. From that perspective, this will be a challenge for SEBI too.

This merger is not just a reversal of a trend but also a pointer to the way in which regulatory structures in India's financial markets are set to change.

Foreign Institutional Investor - FII

A foreign institutional investor (FII) is an investor or investment fund registered in a country outside of the one in which it is investing. Institutional investors most notably include hedge funds, insurance companies, pension funds and mutual funds. The term is used most commonly in India and refers to outside companies investing in the financial markets of India.

Foreign Institutional Investor (FII) means an institution established or incorporated outside India which proposes to make investment in securities in India. They are registered as FIIs in accordance with Section 2 (f) of the SEBI (FII) Regulations 1995. FIIs are allowed to subscribe to new securities or trade in already issued securities.

However, FII as a category does not exist now. It was decided to create a new investor class called **"Foreign Portfolio Investor" (FPI)** by merging the existing three investor classes viz. **FIIs, Sub Accounts and Qualified Foreign Investors**. Accordingly, SEBI (Foreign Portfolio Investors) Regulations, 2014 were notified on January 07, 2014 followed by certain other enabling notifications by Ministry of Finance and RBI.

In order to ensure the seamless transition from FII regime to FPI regime, it was decided to commence the FPI regime with effect from June 1, 2014 so that the requisites systems and procedures are in place before migration to the new FPI regime.

Foreign Portfolio Investor (FPI)

In India, the term “Foreign Portfolio Investor” refers to FIIs or their sub-accounts, or qualified foreign investors (QFIs).

- Portfolio Investment by any single investor or investor group **cannot exceed 10%** of the equity of an Indian company, beyond which it will now be treated as FDI.
- FIIs, Sub-Accounts and QFIs are merged together to form the new investor class, namely Foreign Portfolio Investors, with an **aggregate investment limit of 24%** which can be raised by the Company up to the applicable sectoral cap.
- All existing FIIs and Sub Accounts can continue to buy, sell or otherwise deal in securities under the FPI regime.
- All existing Qualified Foreign Investors (QFIs) may continue to buy, sell or otherwise deal in securities only till the period of one year from the date of notification of the FPI Regulation. In the meantime, they have to obtain FPI registration.

- Non-Resident Indians (NRIs) and Foreign Venture Capital Investors (FVCI) **are excluded from the purview of this definition.**
- FPIs are permitted to invest in Government Securities with a minimum residual maturity of one year. However, **FPIs have been prohibited from investing in T-Bills.**
- FPI can invest in privately placed bonds if it is listed within 15 days.

Qualified Foreign Investors (QFIs)

The Qualified Foreign Investor (QFI) is sub-category of Foreign Portfolio Investor and refers to any foreign individuals, groups or associations, or resident, however, restricted to those from a country that is a member of Financial Action Task Force (FATF) or a country that is a member of a group which is a member of FATF and a country that is a signatory to International Organization of Securities Commission's (IOSCO) Multilateral Memorandum of Understanding (MMOU).

QFI scheme was introduced by Government of India in consultation with RBI and SEBI in the year 2011, through a Union Budget announcement.

The objective of enabling QFIs is to deepen and infuse more foreign funds in the Indian capital market and to reduce market volatility as individuals are considered to be long term investors, as compared to institutional investors.

QFIs are allowed to make investments in the following instruments by opening a demat account in any of the SEBI approved Qualified Depository Participant (QDP):

- Equity and Debt schemes of Indian mutual funds,
- Equity shares listed on recognized stock exchanges,
- Equity shares offered through public offers
- Corporate bonds listed/to be listed on recognized stock exchanges
- G-Securities, T-Bills and Commercial Papers

QFIs do not include FIIs/Sub-accounts/ Foreign Venture Capital Investor (FVCI).

Participatory Notes (P-Notes)

P-Notes or Participatory Notes are Overseas Derivative Instruments that have Indian stocks as their underlying assets. They allow foreign investors to buy stocks listed on Indian exchanges without being registered. The instrument gained popularity as FIIs, to avoid the formalities of registering and to remain anonymous, started betting on stocks through this route.

Participatory notes are the financial instruments through which individual foreign investors or **hedge funds** who do not want to disclose their identity can invest in Indian markets, otherwise registration with SEBI is a must to get an exposure into Indian equities.

- Registered foreign institutional investors (FIIs), foreign banks and brokerages based in India issue P-notes to foreign investors and invest in Indian stocks on their behalf. Any dividends or capital gains collected from the underlying securities go back to the investors.
- While a common investor has to fill up several KYC (know your customer) forms, provide PAN number and proof of address, etc, a P-Note investor can invest anonymously. This makes it a 'legal' way to route unaccounted wealth in Indian equities, thus feeding the black money monster.
- Other than politicians, bureaucrats or business-persons, even terror financiers are feared to misuse the P-Note route to fulfill illegal objectives.
- A flurry of suggestions SIT made to tackle the black buck menace, including cancelling the participation in the Indian markets by way of P-notes altogether.
- Taking cues from the suggestions, SEBI has now made it mandatory for the P-Notes holders to adhere to Indian Know your customer (KYC) or anti-money laundering (AML) norms.
- SEBI has also put curbs on the transfer-ability of P-notes between two foreign investors. Further, it has also increased the frequency of reporting by P-notes issuers.
- Brokerage Angel Broking said the new set of rules is likely to tighten the round tripping of money by Indian investors, but might see some slowdown in the incremental funds flow in to Indian markets.
- The brokerage, however, believed foreign investors with a long term horizon in India should have no issues adhering to the new set of norms.

Concerns

The primary reason why P-Notes are worrying is because of the anonymous nature of the instrument as these investors could be beyond the reach of Indian regulators. Further, there is a view that it is being used in money laundering with wealthy Indians, like the promoters of companies, using it to bring back unaccounted funds and to manipulate their stock prices.

Measures

SEBI has taken a number of steps to tighten rules on P-Notes.

- From January 2011, FIIs have had to follow KYC norms and submit details of transactions.
- In 2014, new rules on foreign portfolio investors (FPIs) made it mandatory for those issuing P-Notes to submit a monthly report disclosing their portfolios. This led to a decline in the number of entities issuing P-Notes.
- More recently, SEBI mandated that in addition to KYC, the anti-money laundering rules (AML) will also be applicable to P-Note holders. Earlier, a P-Note holder had to adhere to KYC or AML norms of just their home jurisdiction.
- SEBI also issued norms on transferability of P-Notes between two foreign investors and increased the frequency of reporting by P-Note issuers.
- In a recent development, on July 8, 2017, SEBI issued circular banning FPIs from issuing Participatory Notes for investing in equity derivatives. At the same time, FPIs can issue PNs to overseas investors if the equity derivatives investments are used for hedging the equity shares held by them. This means that a foreign investor can make investment in equity derivatives only if he purchases an equal value of shares in the cash segment. Effectively, this step will help to avoid speculative investment by foreign investors using PN in derivatives. SEBI also instructed ODI-issuing FPIs to liquidate such ODI instruments prior to the timeline of 2020.

Current Scenario

Note: You can use these data for Mains

Investments in the Indian capital market through participatory notes (P-notes) plunged to an over eight-year low of Rs1.23 lakh crore at September-end in view of stringent norms put in place by the Securities and Exchange Board of India (SEBI).

- Over the past few months, SEBI has taken several measures to stop the misuse of the controversy-ridden participatory notes. In July, the markets regulator notified stricter P-notes norms stipulating a fee of $1,000 that would be levied on each instrument to check any misuse for channelizing black money.

- Also, SEBI prohibited FPIs from issuing such notes where the underlying asset is a derivative, except those which are used for hedging purposes. The move was a follow-through of SEBI's board approval of a relevant proposal in June. These measures were an outcome of a slew of other steps taken by the regulator in the recent past.

- In April, SEBI had barred resident Indians, NRIs and entities owned by them from making investment through P-notes. The decision was part of efforts to strengthen the regulatory framework for P-notes, which have been long seen as being possibly misused for routing black money from abroad.

Financial Action Task Force (FATF)

The Financial Action Task Force (FATF) is an inter-governmental body established in 1989 by the Ministers of its Member jurisdictions. The objectives of the FATF are to set standards and promote effective implementation of legal, regulatory and operational measures for combating money laundering, terrorist financing and other related threats to the integrity of the international financial system. The FATF is therefore a "policy-making body" which works to generate the necessary political will to bring about national legislative and regulatory reforms in these areas.

- The Financial Action Task Force (FATF) is such global standard setting body for anti-money laundering and combating the financing of terrorism (AML/CFT).

- The FATF was formed at the efforts of the OECD, which is a group of the developed countries.

- At present, the FATF has 37 member countries and 2 regional organizations (GCC and EU), representing most major financial centres in all parts of the globe.

- India joined FATF as 34^{th} member in 2010.

TERMS TO KNOW

HEDGE FUND

Hedge funds are alternative investments using pooled funds that employ numerous different strategies to earn active return for their investors.

A hedge fund is a pool of money that takes both short and long positions, buys and sells equities, initiates arbitrage, and trades bonds, currencies, convertible securities, commodities and derivative products to generate returns at reduced risk. As the name suggests, the fund tries to hedge risks to investor's capital against market volatility by employing alternative investment approaches.

- One aspect that has set the hedge fund industry apart is the fact that hedge funds face less regulation than mutual funds and other investment vehicles.

In order to understand 'hedge funds' as investment, let us take a hypothetical example.

- Suppose a hedge fund company like **'IASbaba'** has a money manager named **Baba**.
- **Baba** struck an agreement with the investors that **30% of all profit will be his income**. But he will charge **30% only when the returns are over 7.5% per annum**.
- Suppose the returns to investors are 4% in year 2017-18, then **Baba** will not charge money.
- The value of minimum return (like 7.5%) is generally based on rate of inflation prevailing in the host country. In India the average inflation in last 30 odd years has been close to 7.5%, **so IASbaba** sets target to give returns above 7.5%. If returns are not above 7.5%, then **Baba** will not charge anything. (This is a big assurance to the investors)
- **The higher is the assured returns more investors will be attracted to invest in that hedge fund.**
- The only condition of hedge fund is that, beyond a minimum returns, the profit will be shared by the money manager (Baba). The partnership agreement of IASbaba also allows Baba to invest in any investment option. Starting from real estate, equity, mutual funds, post office savings, precious metals, or anything legal. With these preconditions, the **money manager Baba** will start investing investors' funds and generate profits.

INITIAL PUBLIC OFFER (IPO)

- Initial public offering is the process by which a private company can go public by sale of its stocks to general public. It could be a new, young company or an old company which decides to be listed on an exchange and hence goes public.
- Companies can raise equity capital with the help of an IPO by issuing new shares to the public or the existing shareholders can sell their shares to the public without raising any fresh capital.

Going public raises a great deal of money for the company in order for it to grow and expand. Private companies have many options to raise capital – such as borrowing, finding additional private investors, or by being acquired by another company. But, by far, the IPO option raises the largest sums of money for the company and its early investors. Some of the largest IPO's to date are:

- Alibaba Group (BABA) in 2014 raising $25 billion
- American Insurance Group (AIG) in 2006 raising $20.5 billion
- VISA (V) in 2008 raising $19.7 billion
- General Motors (GM) in 2010 raising $18.15 billion
- Facebook (FB) in 2012 raising $16.01 billion

Angel Investors and Venture Capitalists

Angel investors invest mostly as individuals, while venture capitalists are structured companies comprising of several individual investors.

Angel investors invest their own money into businesses, but venture capitalists invest money contributed by several investors.

Because they are individuals, angel investors are usually unable or unwilling to fund businesses that require huge funds. Venture capitalists, on the other hand can fund businesses that require millions of dollars, since they are holding funds from several individuals.

Angel investors may be willing to "hands-off" your business if they have nothing relevant, aside the capital to contribute. But venture capitalists will always require board seats and complex deal terms including the ability to control subsequent financings.

Angel investors tend to believe in the entrepreneur and invest in them as a person. Venture capitalists, being less emotional and more process involved, mainly evaluate deals and make offers.

An angel investor fund businesses for motives beyond financial gains (such as social responsibility and community involvement). A venture capitalist is obligated to maximize investors' returns and outperform other venture capitalists; in order to attract even more investors.

Angels tend to avoid follow-up investments out of fear of losing more money if the business fails. Venture capitalists, on the other hand, usually invest additional funds at later stages to assist with growth.

Angel investors are found in virtually all industries, and they have diversified portfolios. Venture capitalists are involved in limited industries (mostly technology and infrastructure), and they have limited portfolios.

INSURANCE IN INDIA

In India insurance was mentioned in the writings of ***Manu (Manusmrithi), Yagnavalkya (Dharmasastra) and Kautilya (Arthashastra).***

Insurance industry in India has seen a major growth in the last decade along with an introduction of a huge number of advanced products.

Insurance sector in India plays a dynamic role in the wellbeing of its economy. It substantially increases the opportunities for savings amongst the individuals, safeguards their future and helps the insurance sector form a massive pool of funds.

With the help of these funds, the insurance sector highly contributes to the capital markets, thereby increasing large infrastructure developments in India.

The Indian Insurance Sector is basically divided into two categories – **Life Insurance and Non-life Insurance.**

The Non-life Insurance sector is also termed as General Insurance. Both the Life Insurance and the Non-life Insurance is governed by the **IRDAI (Insurance Regulatory and Development Authority of India).** This government organization thoroughly monitors the entire insurance sector in India and also acts like a custodian of all the insurance consumer rights. This is the reason all the insurers have to abide by the rules and regulations of the IRDAI.

The Insurance sector in India consists of total 57 insurance companies. Out of which 24 companies are the life insurance providers and the remaining 33 are non-life insurers. Out which there are seven public sector companies.

Life insurance companies offer coverage to the life of the individuals, whereas the non-life insurance companies offer coverage with our day-to-day living like travel, health, our car and bikes, and home insurance. Not only this, but the non-life insurance companies provide coverage for our industrial equipment's as well. Crop insurance for our farmers, gadget insurance for mobiles, pet insurance etc. are some more insurance products being made available by the general insurance companies in India.

The life insurance companies have gained an investment prospectus in the recent times with an idea of providing insurance along with a growth of your savings. But, the general insurance companies remain reluctant to offer pure risk cover to the individuals.

The Future of Insurance Sector in India

Though LIC continues to dominate the Insurance sector in India, the introduction of the new private insurers will see a vibrant expansion and growth of both life and non-life sectors in 2017-18. The demands for new insurance policies with pocket-friendly premiums are sky high. Since the domestic economy cannot grow drastically, the insurance sector in India is controlled for a strong growth.

With the increase in income and exponential growth of purchasing power as well as household savings, the insurance sector in India would introduce emerging trends like product innovation, multi-distribution, better claims management and regulatory trends in the Indian market.

The government also strives hard to provide insurance to individuals in a below poverty line by introducing schemes like the

- Pradhan Mantri Suraksha Bima Yojana (PMSBY)
- Rashtriya Swasthya Bima Yojana (RSBY) and
- Pradhan Mantri Jeevan Jyoti Bima Yojana (PMJJBY)
- Atal Pension Yojana
- Varishtha Pension Bima Yojana 2017 (VPBY 2017)

Introduction of these schemes would help the lower and lower-middle income categories to utilize the new policies with lower premiums in India.

With several regulatory changes in the insurance sector in India, the future looks pretty awesome and promising for the life insurance industry. This would further lead to a change in the way insurers take care of the business and engage proactively with its genuine buyers.

Some demographic factors like the growing insurance awareness of the insurance, retirement planning, growing middle class and young insurable crowd will substantially increase the growth of the Insurance sector in India.

Pradhan Mantri Suraksha Bima Yojana (PMSBY)

An Analysis (Will be helpful in Mains)

It is a flagship social security scheme called 'Pradhan Mantri Suraksha Bima Yojana' (PMSBY) which **is an accidental death and disability insurance scheme.**

A large part of the Indian population lives in rural areas and most of them are not covered under any kind of social security scheme. A large section of this population has not even gained the benefits of the banking system and most are still unaware of various governmental schemes that are launched from time to time.

To correct this serious anomaly in the lives of ordinary and poor people, the Pradhan Mantri of India launched the PMSBY scheme in Kolkata on 9 May, 2015 along with two other insurance- and pension-related schemes.

Uniqueness

There are two aspects of PMSBY that make it different in its offering and approach.

- Firstly, it is the sheer size and depth of inclusion to bring and get covered the maximum number of people under this scheme, which kind of makes it very ambitious and challenging. Today, if an earning member of a family becomes permanently disabled or dies an accidental death, his or her family faces a life in penury and hardship, with no protection or support from any institution or group. By joining the PMSBY scheme and by paying a nominal premium **of Rs. 12/- per person per year**, he or she will get an **insurance cover for a sum of Rs. 2,00,000/- (two lakh)** in case of accidental death or **permanent full disability or a sum of Rs. 1,00,000/- (one lakh) in case of partial but permanent disability.** The scheme will be valid for a year and it can be renewed every year.
- A lot of government social security schemes have not received a very positive response from people due to lack of financial system infrastructure at a nearby location and moreover, the paperwork involved in opening accounts or making claims was too much for them to handle. Even the leakages in the system resulted in large sections remaining excluded from the benefits of these schemes. This has now been largely addressed by the present government that has made extensive use of technology to augment its social scheme delivery and monitor mechanisms. All the payments will be directly credited to the beneficiary's account with no scope for leakages.

Eligibility

- Any person between the **age of 18 and 70** with a savings bank account and Aadhaar Card can join the scheme.

Tax Benefit

- The entire premium paid by the subscribers will be tax free under Section 80C. Furthermore, all the proceeds received up to Rs. 1,00,000/- (one lakh) will be exempted from tax under Section 10(10D).
- For all the proceed amounts exceeding Rs. 1,00,000/-, a TDS at the rate of 2% of the total proceeds will apply if Form 15H or Form 15G is not submitted to the insuring agency.

Pradhan Mantri Jeevan Jyoti Bima Yojana (PMJJBY)

Pradhan Mantri Jeevan Jyoti Bima Yojana (PMJJBY) is a one-year life insurance scheme, renewable from year to year, offering coverage for death.

The cover under PMJJBY is for death only and hence benefit will accrue only to the nominee. PMJJBY is a pure term insurance policy, which covers only mortality with no investment component.

- PMJJBY is available to people in the age group of 18 to 50 years.
- Under PMJJBY scheme, life cover of Rs. 2 lakhs is available at a premium of Rs.330 per annum per member and is renewable every year. In the case of a joint account, all holders of the said account can join the scheme provided they meet its eligibility criteria and pay the premium at the rate of Rs.330 per person per annum.
- Risk cover under PMJJBY is applicable only after the first 45 days of enrolment. In other words, insurers do not have to settle claims during the first 45 days from the date of enrolment. However, deaths due to accidents will be exempt from the lien clause and will still be paid.

Rashtriya Swasthya Bima Yojana

Rashtriya Swasthya Bima Yojana (RSBY) a Health Insurance Scheme for the Below Poverty Line families with the objectives to reduce OOP expenditure on health and increase access to health care.

RSBY was launched in early 2008 and was initially designed to target only the Below Poverty Line (BPL) households, **but has been expanded to cover other defined categories of unorganised workers,** covering:

- Building and other construction workers registered with the Welfare Boards Licensed Railway Porters
- Street Vendors
- MNREGA workers who have worked for more than 15 days during the preceding financial year
- Beedi Workers
- Domestic Workers
- Sanitation Workers
- Mine Workers
- Rickshaw pullers
- Rag pickers
- Auto/Taxi Driver

Since 1st April, 2015, the Scheme Rashtriya Swasthya Bima Yojana (RSBY) has been transferred to Ministry of Health & Family Welfare on "as is where is" basis. Ministry of Health & Family Welfare is administering and implementing the scheme through a decentralized implementation structure at the State level.

RSBY has two fold objectives:

- To provide financial protection against catastrophic health costs by reducing out
- To improve access to quality health care for below poverty line households of pocket expenditure for hospitalization and other vulnerable groups in the unorganized sector

The beneficiaries under RSBY are entitled to hospitalization coverage up to Rs. 30,000/- per annum on family floater basis, for most of the diseases that require hospitalization.

The coverage extends to maximum five members of the family which includes the head of household, spouse and up to three dependents. Additionally, transport expenses of Rs. 100/- per hospitalisation will also be paid to the beneficiary subject to a maximum of Rs. 1000/- per year per family.

The beneficiaries need to pay only Rs. 30/- as registration fee for a year while Central and State Government pays the premium as per their sharing ratio to the insurer selected by the State Government on the basis of a competitive bidding.

Atal Pension Yojana

Atal Pension Yojana (APY), a pension scheme for unorganised sector workers such as personal maids, drivers, gardeners etc, was launched in June 2015 by the government. This social security scheme was introduced as a replacement to previous government's Swavalamban Yojana NPS Lite, which wasn't well accepted by people.

APY aims to help these workers save money for their old age while they are working and guarantees returns post retirement. The scheme also promises a co-contribution by Central Government of 50% of the total prescribed contribution by a worker, up to Rs. 1000 per annum, but only to those who joined APY before 31.12.2015. Further, this co-contribution would be made only for 5 years, from FY 2015-16 to 2019-20 in the eligible cases subject to conditions mentioned below.

You are eligible for the Atal Pension Yojana if you are:

- An Indian citizen
- Have a valid bank account
- Are between 18 and 40 years of age.

Guaranteed monthly pension for subscribers, ranging from Rs. 1,000 to Rs. 5,000 per month.

Government of India (GoI) will also co-contribute 50% of the subscriber's contribution or Rs. 1,000 per annum, whichever is lower.

The Government co-contribution is available for those who are not covered by any Statutory

Social Security Schemes and is not an Income Tax payer.

Varishtha Pension Bima Yojana 2017 (VPBY 2017)

- It is a part of Government's commitment for financial inclusion and social security.
- The scheme will be implemented through Life Insurance Corporation of India (LIC) during the current financial year to provide social security during old age and protect elderly persons aged 60 years and above against a future fall in their interest income due to uncertain market conditions.
- The scheme will provide an assured pension based on a guaranteed rate of return of **8% per annum for ten years,** with an option to opt for pension on a monthly / quarterly / half yearly and annual basis.
- The differential return, i.e., the difference between the return generated by LIC and the assured return of 8% per annum would be borne by Government of India as subsidy on an annual basis.

Insurance Regulatory and Development Authority (IRDA)

The Insurance Regulatory and Development Authority of India (IRDAI) ***is an autonomous, statutory agency*** tasked with regulating and promoting the insurance and re-insurance industries in India.

- It was constituted by the Insurance Regulatory and Development Authority Act, 1999, an Act of Parliament passed by the Government of India.
- The agency's headquarters are in Hyderabad, Telangana, where it moved from Delhi in 2001.
- IRDAI is a 10-member body including the chairman, five full-time and four part-time members appointed by the government of India.

Significance of Social Security and Insurance

Article 41 of Directive Principles in Indian constitution asks the state to "within the limits of its economic capacity and development," make effective provision for securing the right to work, to education and to public assistance in cases of unemployment, old age, sickness and disablement, and in other cases of undeserved want." Article 42 says the state shall make provisions for securing just and humane conditions of work and for maternity benefits.

Significance of social security and insurance cover:

- High cost of out of pocket expenditure on health in India means families lying above the BPL falling into the BPL category in wake of illness because of lack of any social security.
- Presence of large unorganized sector. Many surveys suggest that only that in the formal sector, 8 per cent of India's workforce, enjoys social security. Over 91 percent of workers, over 39.5 crore workers, are in the informal sector.

Recently launched schemes and plans:

- Atal Pension Yojana- which caters mainly to the people who are part of unorganised sector.
- Jeevan Jyoti Yojana
- National Pension Scheme and Pradhan Mantri Suraksha Bima Yojana
- Pradhan Mantri Jan Dhan Yojana- Leading to financial inclusion making insurance policies and social security schemes to reach to the poor.
- Maternity Benefit Act providing social security to women.

Are they effective?

- Schemes like PMJDY have proved to be a successful one as millions of Indians have created bank accounts under it. Similarly, Pradhan Mantri Fasal Bima Yojana is a scheme which has been one of the most comprehensive insurance schemes.

However, the implementation and structure of above schemes are not very effective because of following issues:

- Bureaucratic delays and administrative apathy.
- Multiplicity of schemes.
- Lack of awareness among the needy ones.
- Banking professional not sensitive to needs of poor when it comes to insurance schemes and generating awareness.

India spends 1.4 percent of its GDP on social protection, among the lowest in Asia, far lower than China, Sri Lanka, Thailand, and even Nepal. Also only 17% of Indians have insurance.

Given the significance and importance of these schemes India needs to bring in national insurance policy.

Analysis of Insurance Sector in India

Government's policy of insuring the uninsured has gradually pushed insurance penetration in the country and proliferation of insurance schemes are expected to catapult this key ratio beyond 4 per cent mark by the end of this year, reveals the ASSOCHAM latest paper.

The government is considering allowing 100 per cent foreign direct investment in insurance broking with a view to giving a boost to the sector and attracting more funds.

The FDI policy, at present, allows 49 per cent foreign investment in the insurance sector that encompasses insurance broking, insurance companies, third-party administrators, surveyors and loss assessors as defined by the Department of Industrial Policy and Promotion.

The Union Budget of 2017-18 has made the following provisions for the Insurance Sector:

- The Budget has made provisions for paying huge subsidies in the premiums of Pradhan Mantri Fasal Bima Yojana (PMFBY) and the number of beneficiaries will increase to 50 per cent in the next two years from the present level of 20 per cent. As part of PMFBY, Rs 9,000 crore (US$ 1.35 billion) has been allocated for crop insurance in 2017-18.
- By providing tax relief to citizens earning up to Rs 5 lakh (US$ 7500), the government will be able to increase the number of taxpayers. Life insurers will be able to sell them insurance products, to further reduce their tax burden in future. As many of these people were understating their incomes, they were not able to get adequate insurance cover.
- Demand for insurance products may rise as people's preference shifts from formal investment products post demonetisation.
- The Budget has attempted to hasten the implementation of the Digital India initiative. As people in rural areas become more tech savvy, they will use digital channels of insurers to buy policies.

The Government of India has taken a number of initiatives to boost the insurance industry. Some of them are as follows:

- Government of India launches Pradhan Mantri Vaya Vandana Yojana, a pension scheme which will provide guaranteed 8 per cent annual return to all the senior citizen above 60 years of age for a policy tenure of 10 years.

- The Union Cabinet has approved the public listing of five Government-owned general insurance companies and reducing the Government's stake to 75 per cent from 100 per cent, which is expected to bring higher levels of transparency and accountability, and enable the companies to raise resources from the capital market to meet their fund requirements.
- The Insurance Regulatory and Development Authority of India (IRDAI) plans to issue redesigned initial public offering (IPO) guidelines for insurance companies in India, which are looking to divest equity through the IPO route.
- IRDAI has allowed insurers to invest up to 10 per cent in additional tier 1 (AT1) bonds that are issued by banks to augment their tier 1 capital, in order to expand the pool of eligible investors for the banks.
- The Insurance Regulatory and Development Authority (IRDA) recently issued guidelines for PE funds' investment in insurance companies stipulating norms including investment period and percentage of holding. The guidelines set a ceiling of 10% in insurance companies for investors. As an investor, a fund can invest up to 10% of the paid up equity of an insurance company.
- The Indian investors, including PE funds, jointly should not hold more than 25% of paid up equity share capital of the company. In case of the PE investment through SPV, the minimum shareholding of promoters and promoter group should at all times be maintained at 50% of the paid up equity capital. In cases where the minimum holding is less than 50%, it should be maintained at those levels.

Road Ahead

- The future looks promising for the life insurance industry with several changes in regulatory framework which will lead to further change in the way the industry conducts its business and engages with its customers. Insurance Penetration mark is expected to cross 4 per cent mark in the year 2017 as it has shown a continuous increase in the year 2014 and 2015 with market penetration rate of 3.3 per cent and 3.44 per cent respectively.
- The country's insurance market is expected to quadruple in size over the next 10 years from its current size of US$60 billion.
- Demographic factors such as growing middle class, young insurable population and growing awareness of the need for protection and retirement planning will support the growth of Indian life insurance.

Do you know?

- After GST, insurance sector comes under 18% Tax slab.

THINK!

- Of the four GST slabs—5%, 12%, 18%, 28%—insurance falls under the 18% slab, as against the previous service tax of 15%. Given the scenario, how will the goods and services tax (GST) impact the growth momentum of this industry?