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MICRO INSURANCE: AN INNOVATIVE DIMENSION TO UNLOCK FINANCIAL INCLUSION IN INDIA

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Abstract
Poverty is not just a state of deprivation but has latent vulnerability For India to reach its rightful place as a developed nation it must financially empower its entire population. A key element of this empowerment is a base risk cover that covers elements of life, disability and health. This empowerment can only be achieved through the collaborative efforts of the government, regulators and private enterprises, which must be able to build commercially viable and scalable models for financial inclusion. The key issues and challenges impending growth of financial inclusion in India from the perspective of the key stakeholders - the un-reached customer, the distribution intermediary and the insurance company, can be addressed by way of structural regulatory and policy changes coupled with extensive leverage of emerging technologies. Micro insurance should, therefore, provide greater economic and psychological security to the poor as it reduces exposure to multiple risks and cushions the impact of a disaster. There is an overwhelming demand for social protection among the poor. Micro insurance in conjunction with micro savings and micro credit could, therefore, go a long way in keeping this segment away from the poverty trap and would truly be an integral component of financial inclusion. The suggested measures will aid in increasing financial inclusion through micro insurance penetration in our country which can be achieved through focused efforts and suitable partnerships across the industry and government bodies.

Key words: Financial Inclusion, Micro Insurance, IRDA.

Overcoming poverty is not a gesture of charity. It is an act of justice. It is the protection of a fundamental human right, the right to dignity and a decent life. While poverty persists, there is no true freedom.

Sometimes it falls upon a generation to be great. You can be that great generation. Let your greatness blossom. Of course, the task will not be easy. But not to do this would be a crime against humanity, against which I ask all humanity now to rise up."

- Nelson Mandela

"The test of our progress is not whether we add more to the abundance of those who have much; it is whether we provide enough for those who have too little."

- Franklin D. Roosevelt

Introduction

Financial inclusion is now one of the most talked about agendas towards holistic development of the country. With the thrust towards financial inclusion by the Narendra Modi government to achieve all round growth of society, micro insurance is poised to play an important role in it.

Micro insurance is essential to ensure financial support for the large chunk of rural and urban poor population in the country, especially when it comes to insuring their lives or property for a small quantum of premium.

Objectives of the Study

1. To understand the basic concepts and growth of financial inclusion and micro insurance in India.
2. To conduct a systematic analysis of issues and challenges impeding financial inclusion and micro insurance in India.
3. To provide some useful recommendations and suggestions to include micro insurance as a innovative tool for the financial inclusiveness in India.

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Review of Literature

There have been many past studies relating to micro insurance and financial inclusion and its role Bell (1990) and Kochar (1997) claim that the role of commercial banks in promoting rural development has been limited. Some more of such studies that help to understanding the financial inclusion are

Rajan and Zingales (1998) examined whether financial development facilitates economic growth by scrutinizing one rationale for such a relationship that financial development reduces the costs of external finance to firms. They find this to be true in a large sample of countries over the 1980

Dsrijanani (2013) assessed Micro insurance a safety net of the poor, assessed a no of risks faced by women could be minimized through Micro insurance by leveraging existing networks for MI linking micro credit with MI and ensure widening outreach of MI products to the rural poor.Amrutha varshini and B Suresh (2013) analysed the cause for low penetration level of MI and identify the preferred MI in india and suggested that the main reason is due to low premium amount.

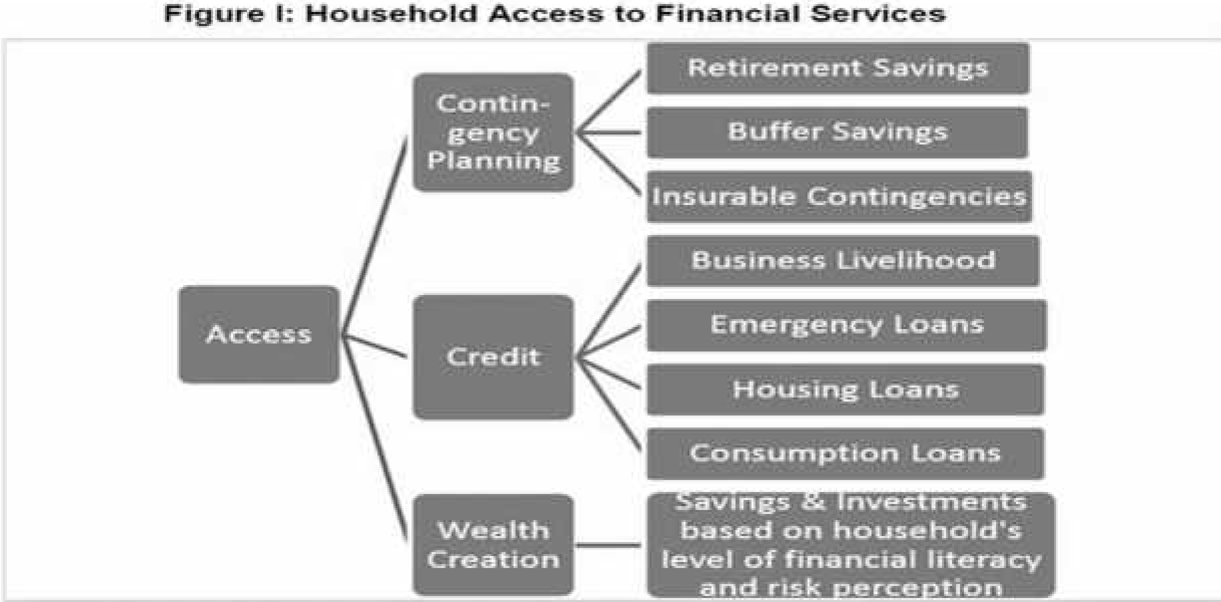
Rashed Al Hasa (2007) published and assessed the reducing vulnerability of the poor through social security products through market survey explored the existing MI products and their target clients of MFI/NGOs and explore the possibility of building allowances.Ikechukwu Ach Mfon Sampson UKpong assessed the role of Micro Insurance: A veritable product diversification option for Micro Finance Institutions by personalizing MI products and to increase and imbibe more faith to increase the confidence

Premasis Mukherjee 2010 experimented a lot with microinsurance, the sector is still driven by supply-led interventions. Moreover, the insurance providers, still, seek government subsidies and donor funding in order to achieve financial viability in preference to designing market-led, sustainable schemes.*NP Mohapatra and Pankaj Kumar (2013)*Pillars of Financial Inclusion : Remittances , Micro Insurance and Micro Savings

Financial Inclusion

Financial Inclusion, refers to universal access to a wide range of financial services at a reasonable cost. These include not only banking products but also other financial services such as insurance and equity products

Figure I: Household Access to Financial Services



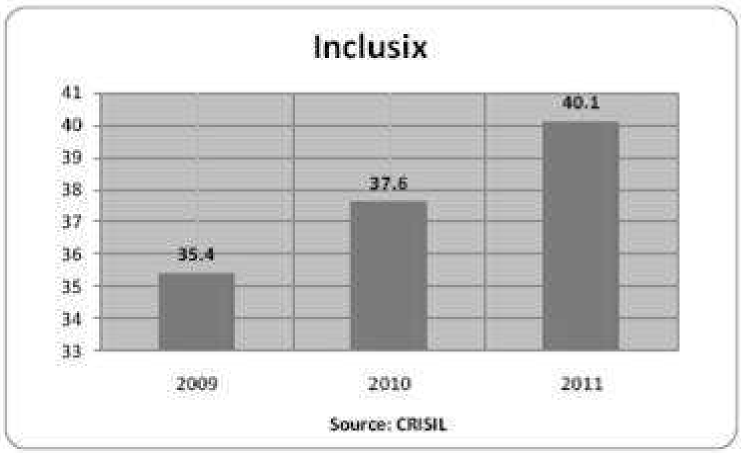
Source: A Hundred Small Steps - Report of the Committee on Financial Sector Reforms (Chairman : Dr. RaghuramRajan).

Source: The Committee on Financial Sector Reforms, Chairman: Dr.Raghuram G. Rajan). Household access to financial services is depicted in Figure 1.

The essence of financial inclusion is to ensure delivery of financial services which include - bank accounts for savings and transactional purposes, low cost credit for productive, personal and other purposes, financial advisory services, insurance facilities (life and non-life) etc.

Why Financial Inclusion ?
Financial inclusion broadens the resource base of the financial system by developing a culture of savings among large segment of rural population and plays its own role in the process of economic development. Further, by bringing low income groups within the perimeter of formal banking sector; financial inclusion protects their financial wealth and other resources in exigent circumstances. Financial inclusion also mitigates the exploitation of vulnerable sections by the usurious money lenders by facilitating easy access to formal credit.

Chart 3: CRISIL - Inclusix



Source: The CRISIL Inclusix indicate that there is an overall improvement in the financial inclusion in INDIA

Micro Insurance
The draft paper prepared by the Consultative Group to Assist the Poor (CGAP) working group on micro-insurance defines micro-insurance as "the protection of low income households against specific perils in exchange for premium payments proportionate to the likelihood and cost of the risk involved." Micro Insurance is commonly defined as a financial arrangement intended to protect the low income people against specific perils in exchange for regular premium payments proportionate to the likelihood and cost of risk involved.

Micro Insurance industry has seen strong growth in recent years with average annual growth rate of approximately 10 percent. Industry practitioners however estimate the only 5 percent of the potential market is covered and that there is a high degree of variability in terms of risk and geographical coverage, leaving large segments of the worlds poor population with limited or no access to insurance

Micro Insurance in India
India's complex social security system comprises of seven components- EPFO Schemes, Civil Service Schemes, Public Sector Enterprises Schemes, Occupational Pension Schemes, Voluntary Tax Advantaged Scheme, Schemes for Unorganized Sector, social insurance and Micro pension. As one of the seven components of India's social security system, micro pensions can play a useful role if they are brought into the mainstream of the financial system. In order to implement the commitment to provide social security to the unorganized sector, the Government of India, among other measures, constituted the National Commission for Enterprises in the Unorganized Sector (NCEUS) under the control of the vide Ministry of Small Scale Industries.

Social Security for the Unorganized Sector:

1. Total employment in the Indian economy: 457 million.
2. Unorganized Sector: 395 million (86% of workforce); Organized: 28 million 14%)(January, 2005, NCEUS)

3. More than 85% of all rural workers get wages below the minimum standard of Rs.66 per day. As per a Supreme Court verdict, all those who do not get statutory minimum wage should be presumed to be treated as bonded labor.
4. Lack of comprehensive protection of minimum work conditions as well.
5. This has serious repercussions across socio-economic dimensions.
6. India currently has more than 260 million people below the Poverty Line, which amounts to around 26.1% of the total Indian population and even they have no social security cover.

Demand for Micro-Insurance

The ILO (2004) has recently prepared an inventory of micro-insurance schemes operational in India. Based on this list some of the observations are made below:

- Available cover 5.2 million people.
- •Most insurance schemes (66%) are linked with micro finance services provided by specialized institutions (17 schemes) or non-specialized organizations (17 schemes). Twenty two percent of the schemes are implemented by community-based organizations, and 12% by health care providers.
- Life and health are the two most popular risks for which insurance is demanded: 59%
- of schemes provide life insurance and 57% of them provide health insurance.
- Twenty-five out of 37 schemes received some external funds to initiate their schemes. Twenty out of 32 schemes received external technical assistance in the form of advisory services, technical services, training or even referral services for their schemes.

Most schemes (74%) operate in 4 southern States of India: Andhra Pradesh (27%), Tamil Nadu (23%), Karnataka (17%) and Kerala (8%), and the two western States (Maharashtra (12%) and Gujarat (6%)) account for 18% of the schemes.

Potential Market Size of Micro Insurance in India

Types of Insurance	Market Size
LIFE	Rs.15.39 to 20.14 billion per year
HEALTH	Rs.13.42 to 17.89 billion per year
CROP	Rs.9.76 to 13.01 billion per year
LIVE STOCK	Rs.5.86 to 8.2 billion per year
TOTAL MICRO INSURANCE MARKET	Rs.62.30 to 84.27 billion per year
PENSION FOR UNORGANISED WORKFORCE	Rs.201.3 billion (US$2.5billion) per year

Source: "Potential and Prospects of Microinsurance in India; UNDP Regional Centre of Human Development Unit 2009, "Pension Reforms for Unorganised Sector; ADB, 2006 and IIMS DataWorks Survey 2008.

Issues and Challenges impeding financial inclusion in India

The essence of financial inclusion is in trying to ensure that a range of appropriate financial services is available to every individual and enabling them to understand and access those services. With a view to understanding the extent of exclusion, the Committee perused data put out by various sources. The summary of conclusions is indicated below

Extent of Exclusion – NSSO Survey 59th Round

(a) **General**

- 51.4% of farmer households are financially excluded from both formal / informal sources. Of the total farmer households, only 27% access formal sources of credit; one third of this group also borrow from non-formal sources. Overall, 73% of farmer households have no access to formal sources of credit.

(b) **Region-Wise**

- Exclusion is most acute in Central, Eastern and North-Eastern regions – having a concentration of 64% of all financially excluded farmer households in the country. Overall indebtedness to formal sources of finance alone is only 19.66% in these three regions.

(c) **Occupational Groups**

- Marginal farmer households constitute 66% of total farm households. Only 45% of these households are indebted to either formal or non-formal sources of finance. About 20% of indebted marginal farmer households have access to formal sources of credit. Among non-cultivator households nearly 80% do not access credit from any source.

(d) **Social Groups *:***

- Only 36% of ST farmer households are indebted (SCs and Other Backward Classes - OBC - 51%) mostly to informal sources. Analysis of the data provided by RBI thru' its Basic Statistical Returns reveal thatcritical exclusion (in terms of credit) is manifest in 256 districts, spread across 17 States and 1 UT, with a credit gap of 95% and above. This is in respect of commercial banks and RRBs.

Thus, there are different estimates of the extent of inclusion thru' formal sources, as the reference period of the data is not uniform. Consequently, this has had an impact on quantifying the extent of levels of exclusion.

Major Road blocks to Financial Inclusion

There are certain underpinning problems of financial inclusion which are briefly stated as under

1. **Poverty**
   Hinders the inclusiveness of any economy. Person with the low income cannot buy financial products and services with his adequate income.
2. **Ignorance**
   Low level of awareness and understanding of products caused by lack of appropriate marketing or low level of financial literacy.
3. **Geographic Environment**
   With lack of infrastructure to cover the vast geographical spread of rural areas with more than half a million villages is difficult to achieve and because of that there has been uneven distribution.
4. **Cultural and Psychological barriers**
   Barriers such as language perceived/ actual racism and suspicion or fear of financial institution is also obstructing factor
5. **Bankers Aversion for Financial inclusion**
   Even though no banker openly expresses his aversion for financial inclusion process overtly it can be noticed that they are averse to it in view of the cost aspects involved in opening of no frill accounts

Issues impeding Micro Insurance

Micro-insurance should provide greater economic and psychological security to the poor as it reduces exposure to multiple risks and cushions the impact of a disaster. In 2003, GoI constituted a Consultative Group on Micro-Insurance to examine existing insurance schemes for rural and urban poor. The report of the consultative group has brought out the following key issues:

- Micro-insurance is not viable as a standalone insurance product.
- Micro-insurance has not penetrated rural markets. Traditional insurers have not made much headway in bringing micro-insurance products to the rural poor. (In addition, the Committee feels that micro insurance has not penetrated even among the urban poor).

Challenges from the Perspective of Key Stakeholders
Un-insured Target Customer

- Design of micro-insurance products must have the features of simplicity, availability, affordability, accessibility and flexibility.

The Committee studied four different models for delivering micro-insurance services to the targeted clientele, viz., the Partner-Agent Model, Full Service Model, Community Based Model and Provider Model

Challenges from the Perspective of Key Stakeholders
Un-insured target customer

- Low product awareness

- Aversion to purchase of an intangible asset
- Perception of insufficient benefits
- Product not suitable for specific strata or business needs
- Time for claim settlement too long as compared to the urgency when required
- Lack of trust in the insurer to honour claim

Distribution Intermediary

- Hinterland population spread over a large area
- Lack of sufficient incentives to cover operations cost
- Lack of training and understanding of product fitment to customer needs
- Risk of losing respect in the local community if the insurer does not honour a claim

Insurance Company

- High transaction cost against low ticket size
- Poor documentation (such as Identity card, age, address proof)
- Largely un-banked target customers
- Risk of adverse selection
- Lack of actuarial data for risk analysis and pricing

Strategy for Building an Inclusive Financial Sector

Overall strategy for building an inclusive financial sector may be based on :

- Effecting improvements within the existing formal credit delivery mechanism;
- Suggesting measures for improving credit absorption capacity especially amongst marginal and sub marginal farmers and poor non-cultivator households.
- Evolving new models for effective outreach, and
- Leveraging on technology based solutions.

Potential Solutions to Further Increase Penetration and Scaling-Up Micro Insurance Business

The IRDA Micro insurance Guidelines, 2005 may permit MF-NBFCs to offer micro insurance services as agents of regulated life and non-life insurance companies.

Leveraging the Existing Network for Micro-Insurance

To economise on costs and to increase the outreach of micro-insurance to the poor, the insurers need to utilize existing Government organisations and NGOs, having greater acceptability among the financially excluded. The partner-agent model for delivery where the insurer underwrites the risk and the distribution is handled by an existing intermediary, seems apt in this scenario.

Linking Micro Credit with Micro Insurance

The Committee concurs with the view that offering microcredit without micro-insurance is financial behaviour fraught with risk. There is, therefore, a need to emphasise linking of microcredit with micro-insurance. 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 microcredit.

Implementation Strategy for Micro-Insurance

The Committee has identified major areas for formulation of strategies for effective implementation of micro-insurance programmes as explained in the following paragraphs Human Resources Requirement and Training.

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 claims, premium payments / renewals and other services should be formalized along with increased customization of products to stimulate Demand.

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.

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.

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.

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

Technology – The Driving Force for Low-Cost Inclusion Initiatives
Technological developments in the recent past have provided the perfect launch pad for extending banking outposts to remote locations without having to open bank branches. This could be achieved by leveraging technology to open up channels beyond branch network and create the required banking footprints to reach the unbanked so as to extend banking services similar to those dispensed from branches.

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.

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.

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.

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 weighed 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.

Health Insurance
In case of Health Insurance, penetration level is even much lower than Life Insurance. The two categories viz., Critical Illness and Hospitalization are the main product segments. Some State Governments have developed Health Insurance schemes which are still in very early stages. The Committee has observed that the 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 co-variant risks such as epidemics will have to be taken care of by a mutual entity taking re-insurance for such risks.

Crop Insurance
This is a very important risk mitigation arrangement for small and marginal farmers. However, 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.To make it more effective, there is a need for having a large number of smaller weather stations. The Committee recommends that policies be evolved to make crop insurance universal, viz., applicable to all crops/regions and pricing actuarial.

Livestock Insurance
As in Life Insurance, the problem lies in the process of enrolment and claims settlement. Several pilots indicate that the involvement of local organisations likes SHGs, dairy co-operatives, NGOs and MFIs improves the quality of service, reduces false claims and expedites claims settlement. The Committee recommends that these experiences be studied and adopted by insurance companies.

Asset Insurance
This could cover a wide range including residential buildings, farm and nonfarm equipments and vehicles. The main constraint seems to be lack of distribution channels appropriate for lower income groups. The Committee again recommends that involving local NGOs, MFIs, SHGs, etc. as distribution channels as well as facilitators of claims settlements would be quite useful.

Conclusion
Micro-insurance is a key element in the financial services package for people at the bottom of the pyramid. The poor face more risks than the well-off, but more importantly they are more vulnerable to the same risk. Usually, the poor face two types of risks – idiosyncratic (specific to the household) and covariate (common, eg., drought, epidemic, etc.). To combat these risks, the poor do pro-active risk management – grain storage, savings, asset accumulation (specially bullocks), loans from friends and relatives, etc. However, the prevalent forms of risk management (in kind savings, self-insurance, mutual insurance) which were appropriate earlier are no longer adequate.

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