


India's insurance reforms: A bold transformation, but not without challenges

Aravind Venugopal | 3 min read | 24 Nov 2024, 07:36 PM IST

Composite licences will allow insurers to operate across both life and non-life businesses.

SUMMARY

India's insurance industry stands on the brink of a revolution as the government proposes allowing 100% foreign direct investment, which could transform the sector.

 [Gift this article](#)

India's insurance industry, long seen as an underpenetrated yet promising market, is poised for a major transformation with the government's proposal to permit 100% foreign direct investment (FDI) in insurance companies and introduce composite licences. These reforms, if implemented effectively, could catalyze significant changes in the sector, attracting fresh capital, improving competition, and enhancing accessibility for consumers.

A landmark move

The proposal to allow 100% FDI in the insurance sector marks a pivotal moment in the liberalization of India's financial services. Historically, foreign insurers were mandated to have Indian partner(s), with the maximum permissible foreign ownership capped at 74%. This structure, while aimed at safeguarding domestic interests, often deterred global insurance players from fully committing to the Indian market.

The proposed removal of the 74% cap will not only encourage global insurers to enter the market but also provide existing foreign investors the flexibility to expand their stakes or operations.

One of the most anticipated outcomes of this move is the infusion of much-needed capital into the sector. Insurance companies require significant investments to build robust operations, develop innovative products, and scale their reach to underserved areas.

The Reserve Bank of India's reluctance to expose balance sheets of banks to non-core businesses such as insurance, coupled with a low private investment climate, had starved the sector of much needed capital to drive penetration.

With foreign insurers now able to establish wholly owned subsidiaries, the sector is likely to see enhanced financial strength, paving the way for product innovation and technological advancement.

The success of this reform hinges on the regulatory framework within which foreign investors will be permitted to hike their shareholding. For instance, foreign investors have the option of acquiring up to 74% or 100% (and nothing in between) in private banks.

Regulations must eschew such an approach and leave it to investors to determine their level of shareholding and focus on ensuring that Indian operations are sufficiently ring fenced from global operations of insurers. Imposing overly restrictive conditions could dilute the attractiveness of the reform and, a transparent and investor-friendly approach could solidify India's position as a lucrative destination for global insurers.

Composite licences: Efficiency and expansion

Another significant proposal is the introduction of composite licences, which would allow insurers to operate across both life and non-life business lines.

Currently, companies are required to hold separate licences for these categories, leading to operational silos and inefficiencies. The ability to offer a broad spectrum of products under a single license is expected to streamline operations, reduce redundancy, and improve customer experience.

Composite licences will also enable insurers to present a comprehensive suite of offerings to customers without approaching them repeatedly for similar data points. This will not only enhance efficiency but also build stronger, more cohesive relationships with policyholders.

The integration of life and non-life insurance products under a unified framework can encourage cross-selling opportunities, making insurance offerings more attractive and tailored to consumer needs.

However, this transition is not without its share of challenges. Many insurers in India operate through joint ventures with foreign partners, often splitting life and non-life operations between different entities. Aligning these arrangements under a composite licence model could require renegotiations and strategic realignments, which may be complex and time-consuming.

Nonetheless, these hurdles should not deter the implementation of a concept whose benefits far outweigh the challenges.

The government and the Insurance Regulatory and Development Authority of India (IRDAI) will provide detailed operational guidelines on critical areas such as capital requirements, product structuring, and regulatory compliances under the composite licence framework.

Regulations must avoid an approach that will result in insurers being forced to create operational and product silos for different lines of business and must instead afford insurers maximum flexibility on such matters. Clarity in these aspects will be instrumental for incumbents and new players to adopt the new regime.

The road ahead: Enhanced penetration and inclusion

India's insurance penetration remains below the global average, underscoring the need for bold reforms to make insurance more accessible and affordable. The proposed changes—permitting 100% FDI and introducing composite licences—are steps in the right direction. These aim to not only attract foreign capital but also foster greater competition within the sector.

Innovation in product offerings, improved service standards, and competitive pricing arising from greater competition will ultimately benefit customers. These, in turn, could make insurance a more appealing option for a larger segment of the population, contributing to higher penetration rates.

Additionally, the infusion of capital and expertise from global players can bolster the industry's capacity to adopt advanced technologies, such as artificial intelligence and data analytics, for risk assessment, claims management, and customer engagement.

(Aravind Venugopal is partner at Khaitan & Co)

