Compliance to the observations made in the evaluation report
I. List of parameters taken for studying the performance of General Insurance Business in India

The performance of General Insurance Business in India has been studied in the current research through sixteen variables. They are

1. Underwriting Premiums
2. Claims Management
3. Commission
4. Operating Expenses
5. Underwriting Profit
6. Gross Investments
7. Gross Investment Income
8. Claim Ratio
9. Net Assets
10. Net Liabilities
11. Current Assets
12. Current Liabilities
13. Net Solvency
14. Solvency Ratio
15. Liquidity Ratio
16. Net Profit

Whereas detailed explanations of these variables are given in Chapter-II and also in Chapter III, a brief explanation to the effect may be given as follows:

1. Underwriting premiums

The premiums collected by insurance business have been used as a performance measurement yardstick of the insurance business since ages. These premiums
assume two forms—gross and net. Whereas some experts prefer to use Gross premiums as the measure of performance, others prefer to use Net premiums as the performance measurement tool. The current study has accepted the ‘net premiums’ as a study variable. The net premiums have been calculated after deducting the premiums receivables pertaining to the subsequent years. Inclusion of net premiums as a performance measurement variable in the study is guided by the fact that it reflects the quantum of business activity undertaken by the business house in any given financial year. The net premium income has been analyzed in the study through Tables 3.1 and 3.2 and Figures 3.1, 3.2 and 3.3 in Chapter-III.

2. Claims management

The claim management, translated into Net claims, is the second dimension along which the performance of the general insurance business in India has been measured in the study. Net claims are the actual claims after deducting the claim settlements pertaining to the previous year(s). As the net claim reflects the aggregate payout for the year, it reflects the basic foundation of risk management mechanism in place. Claims being the largest outflow of funds for any insurance player, prudent management of claims is instrumental in achieving the operational excellence of the player. Tables 3.3 and 3.4, and Figures 3.4, 3.5 and 3.6 in Chapter-III of the study deal with the analysis of net claims as a performance measure indicator for the general insurance business in India.
3. **Commission**

'Commission payout' has been used as the third performance measurement variable in the study. Commission, as included in the study, reflects the amount of commission playable after taking into account the commission payable on subsequent renewals of premium. Hence in several cases, commission has been found to be in negative figure reflecting the commission unpaid due to non renewal or delay in renewals. As commission is an expense having a direct bearing on the premium underwritten, it is taken as an influencing factor for measuring the gross income generated by the insurance business from underwriting activities. Tables 3.5 and 3.6, and Figures 3.7, 3.8 and 3.9 in Chapter-III of the study contain the analysis of commission as a performance measure indicator for the general insurance business in India.

**Operating expenses**

The fourth variable included in the study to measure the performance is the operating expenses. Operating expenses reflect the indirect expenditures incurred by the general insurance companies to carry on their business activities. These expenses include selling cost, issuance cost, administrative cost, investment cost and the portfolio maintenance cost. The reason for inclusion of operating expense as a performance variable lies with the fact that this is a major expense for the insurance companies particularly in the privatized era and that an increase in the operating expenses may lead to an increase in the premium income as increased operating expenses gives a thrust to increase in sales, thus leading to increased volume of underwriting. Tables 3.7 and 3.8, and Figures 3.10, 3.11 and 3.12 in Chapter-III contain the analysis on operating expense as a performance measure indicator for the general insurance business in India.
**Underwriting profit**

Underwriting profit (and loss) has been taken as the fifth performance measurement variable. Underwriting profit refers to the gross income earned from the underwriting activity after excluding all direct and indirect expenses of running the general insurance business. The gross underwriting profit is the profit obtained after meeting the net premiums, claims, net commission and operating expenses. It excludes the investment income from its purview.

The gross underwriting profit in the study has been calculated as follows:

\[
\text{Gross Underwriting Profit} = \text{Net premiums} - \text{Claims} - \text{Net commission} - \text{Operating Expenses}
\]

Moreover, Tables 3.9 and 3.10, and Figures 3.13, 3.14 and 3.15 in Chapter-III contain the analysis on underwriting profit (and loss) as a performance measure indicator for the general insurance business in India.

**Gross Investments**

Investments are the reflections of the soundness of portfolio held by the insurance companies. The IRDA has categorized the avenues of investments for the general insurance companies in six categories with the ceilings specified for the investments. These are central government investments, state government and other approved central government securities, housing and fire fighting equipments, infrastructure investments, and investments
subject to exposure norms and other than approved investments. For the study, all these investment avenues have been taken as the sixth major study variable.

Tables 3.11 and 3.12, and Figures 3.16, 3.17 and 3.18 in Chapter-III contain the analysis on the gross investments as a performance measure indicator for the general insurance business in India.

**Gross investment income**

The study has included the gross investment income as another study variable as it reflects the soundness of the investment portfolios of the insurance companies and the returns reaped during the financial year from such investments. The ability of the insurance companies to manage external risk as associated with income from investment and hence it has been included in the study as the performance indicator. Tables 3.13 and 3.14, and Figures 3.19, 3.20 and 3.21 in Chapter-III contain the analysis with respect to investment income.

**Claims ratio**

The claims ratio is an indicator of the payout demanded by the insured over the premiums underwritten. This ratio, which has been taken as the eighth performance indicator, reflects the soundness of the risk coverage given to the insurance buyer considered from the angle of the seller of the insurance products and the consequent effectiveness of the firm's risk management mechanism, given that lesser this ratio is, better is the firm's performance. The claims ratio has been calculated in the study by dividing Net Claims by Net Premium and the corresponding discussion on the trends has been made in Tables 3.15 and 3.16, and Figures 3.22, 3.23 and 3.24 in Chapter-III.
Net assets

Net assets are the pool of all long term assets of the general insurance companies. These assets reflect the long term financial soundness of the company, hence have a great bearing on the risk management complexion of the company and hence have been included as a variable of the studying the performance. Tables 3.17 and 3.18, and Figures 3.25, 3.26 and 3.27 in Chapter-III deal with analysis of net assets as the ninth performance parameter.

1. Net liabilities

The net liabilities are the total outstanding long term liabilities of the company during the year. The net liabilities have a great bearing on the overall solvency position of the organization. For the general insurance companies in India, the net liabilities have been calculated and the trend analyzed through Tables 3.19 and 3.20, and Figures 3.28, 3.29 and 3.30 in Chapter-III.

Current assets

The current assets of any organization reflect the short term liquidity of the organization. As the underwriting activity and investments have a direct bearing on the liquidity position of the organization, the study has included current asset as another performance variable. For the study all the assets of the organization apart from investments that can be converted into cash at a short notice has been categorized as current assets. Further, Tables 3.21 and 3.22, and Figures 3.31, 3.32 and 3.33 in Chapter-III deal with the trends in current assets the general insurance business in India.
Current liabilities

The amount of money payable apart from claims at any moment of time during the business operations has been categorized as current liabilities. As the current liabilities have a direct impact on the liquidity position of the organization, it has been included as a performance variable in as much as lesser the current liabilities in comparison to current assets, better is the short term liquidity position of the firm. The trend against current liability as the performance parameter has been discussed in Tables 3.23 and 3.24, and in Figures 3.34, 3.35 and 3.36 in Chapter-III.

Net solvency

The net solvency is the indicator of the long term financial position of the organization. Though it is the difference between the net assets and net liabilities, the IRDA provided the following regulatory guidelines for calculation of solvency:

i. 20% of net premiums, 30% of net claims or 50crores whichever is higher.

ii. The required solvency has to be at least 150% of the solvency as calculated above.

For the purpose of the present study, the required solvency as stated under clause(ii) above prescribed by IRDA has been included as a performance measure and discussed in Tables 3.25 and 3.26, and in Figures 3.37, 3.38 and 3.39 in Chapter-III of the study.

Solvency ratio

The solvency ratio is the ratio of net assets maintained in relation to the net liabilities. It represents the firm's capability to meet its long term obligations during a given financial year. The solvency ratios of the general insurance sector as whole and the individual players have been analyzed in Tables 3.27 and 3.28, and in Figures 3.40, 3.41 and 3.42 in Chapter-III.
Liquidity ratio

The net liquidity ratio is the indicator of the organization's capability of meeting short term requirements of funds. It is the ratio of the current assets and current liabilities. Its importance can be understood from the fact that the underwriting of the insurance business as well as investments is directly related to the liquidity position of the organization. The performance of general insurance business in India in terms of liquidity position has been analyzed in Tables 3.29 and 3.30, and in Figures 3.43, 3.44 and 3.45 in Chapter-III.

Net profit

The net profit being a reflector of ultimate business outcome has been included as another study variable, the sixteenth variable to measure the performance of general insurance business in India. For the study the net profit denotes the profit after tax of the organization. It takes into account the gross underwriting profit and the investment income apart from the other appropriations of tax. Tables 3.31 and 3.32, and Figures 3.46, 3.47 and 3.48 in Chapter-III deal with analysis on net profits.

The factor analysis, conducted on the above listed sixteen variables to determine the most influencing variables that determine the performance of general insurance business in India, has revealed that out of the sixteen variables only five variables, namely, gross investments, net liabilities, net solvency, current assets and current liabilities have significant bearing on the performance of the general insurance business in India.
II. Risk management

The risk management aspect has been dealt with in the study under two broad dimensions such as identification of the kinds of risk to which general insurance business in India are subject to which has been put under the heading (4.1) Risk in general insurance business and risk management mechanism which has been put under the heading (4.2) risk management mechanism in general insurance business. As mentioned therein, general insurance business in India as a whole is exposed to two broad categories of risk, namely, (1) Financial Risk and (2) Non financial Risk.

Included under the financial risk category are four different kinds of risk, namely, capital risk, asset liability management risk, insurance risk and credit risk. Similarly, there are two individual risks, namely, enterprise risk and operational risk which fall under the non financial category of risk. Further, under each of the different sub categories of risk, there are several individual risks to which the general insurance business in India is exposed to as depicted in the chart that follows:
Risk Factors.

Financial Risk
- Capital Risk
  - Capital structure risk
  - Capital adequacy risk
- Asset/Liability management risk
  - Exchange rate risk
  - Interest rate risk
  - Investment risk
- Insurance risk
  - Underwriting risk
  - Catastrophic risk
  - Reserve risk
  - Pricing risk
  - Claims management risk
- Credit risk
  - Reinsurance risk
  - Policy holder risk
  - Brokers risk
  - Claims recovery risk
  - Other debtors risk

Non Financial Risk
- Enterprise risk
  - Reputation risk
  - Parent risk
  - Competitor risk
- Operational risk
  - Regulatory risk
  - Business continuity risk
  - IT Obsolescence risk
  - Process risk
  - Regulatory compliance risk
  - Outsourcing risk

Each of the categories of risk as mentioned above has been discussed in the present study in Chapter IV under various sections and subsections.

The risk management mechanism adopted by the insurer, i.e., the general insurance companies assume two dimensions namely, (1) Risk based capital management technique and (2) Reserving which have been discussed in the study under the broad subheading 4.3: Risk management techniques adopted by the insurer as contained in Chapter IV. It may however be mentioned here that the board of directors (BOD) have a pivotal role to play followed by the management in managing the risk under both risk based capital management technique and reserving technique.

Whereas, the board, i.e., BOD has five roles to play, the management has six roles as depicted in the chart that follows.
### Role of BOD and Management in managing risk

<table>
<thead>
<tr>
<th>Role of BOD</th>
<th>Role of Management</th>
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</thead>
<tbody>
<tr>
<td>1. review and approve management's risk philosophy, and the risk management policies recommended by the company's management;</td>
<td>1. develop and recommending the management's risk philosophy and policies for approval by the board of directors;</td>
</tr>
<tr>
<td>2. review periodically management reports demonstrating compliance with the risk management policies;</td>
<td>2. establish procedures adequate to the operations, and monitoring and implementing the management programs;</td>
</tr>
<tr>
<td>3. review the content and frequency of management's reports to the board or to its committee;</td>
<td>3. ensure that risk is managed and controlled within the relevant management program;</td>
</tr>
<tr>
<td>4. review with management the quality and competency of management personnel appointed to administer the risk management policies; and</td>
<td>4. ensure the development and implementation of appropriate reporting system, and a prudent management and control of existing and potential risk exposure;</td>
</tr>
<tr>
<td>5. ensure that the audit regularly reviews operations to assess whether or not the company's risk management policies and procedures are being adhered to and to confirm that adequate risk management processes are in place.</td>
<td>5. ensure that audit regularly reviews the operation of the management program;</td>
</tr>
<tr>
<td></td>
<td>6. develop lines of communication to ensure the timely dissemination of management policies and procedures and other management information</td>
</tr>
</tbody>
</table>
III. Suggestions

1. The study reveals that there is interdependency among the public and private sector players with respect to premiums, claims, commissions and operating expenses indicating, for example, a rise in premium income of the public sector players is accompanied by a corresponding fall in the premium incomes of the private sector players. Moreover the individual players under both public and private sector compete with each other for the same business. It is therefore felt that if the players are allotted with specific business segments and may be specific geographical area even, the competition among the players for the same business will come down and even get eliminated and as a result of which the individual player will be able to concentrate by orienting all its resources, physical and financial, to the allotted business and geographical sector thus enhancing the individual players performance.

   It may therefore be recommended that more emphasis be given on creating special players for different sectors such as agriculture, automobile, health, aviation, commercial, engineering and export and import (EXIM). This will bring the much needed focus on pricing, specialized commission models, operational efficiency and claims management procedures of the specific sectors and also will decrease the competition.

2. The study has further revealed that the public sector players have adopted a more aggressive and diversified approach to investing their pool of funds in other approved securities where as the private sector players are adopting apparently a more conservative approach to building their investing portfolio by investing mostly into
central government securities resulting a wide disparity in the earnings of the two categories of players. The difference in the approach of investment may be because of the long existence of the public sector players in the insurance business with huge capital base and proven expertise compared to the private sector players who are young by any parameters, be it capital or expertise.

It may therefore be recommended that the private sector should adopt a more dynamic strategy for the investment by investing more in other approved sectors in order to have a balanced portfolio.

3. It is found that the investment ceiling fixed by the IRDA is the same for the private and the public sector players. As the private sector players are relatively new to the general insurance business with limited corpus, meeting the ceiling may be difficult for them. It may therefore be recommended that a lenient view by lowering the ceiling for investment may be adopted with a corresponding policy change by the IRDA for the private sector players.

4. The outstanding commission is found to be increasing over the years with a resultant increase in underwriting losses. Whereas the phenomena is true for both the private and the public sector players, comparatively the private sectors are in the back foot as such it is recommended that players of both the sectors formulate a more pro active strategy such as reminder about the premium, service at door step, and offering discounts may be adopted.

5. The players in both public and private sector have been incurring fluctuating underwriting losses over the period of study, which indicates the operational
inefficiency. This may be improved by decreasing the outstanding commissions, better risk assessment for ensuring lesser claims and decreasing the operating expenses.

6. The regulatory body IRDA should formulate different solvency margins for public and private sectors which will not only help the private players to have operational efficiency but also will help in reducing their consistent underwriting losses.

7. Since the segments of fire, marine and miscellaneous have interdependency, as revealed in the study over the public and private sectors, it may be recommended that the policy decisions of the players be based on a holistic view rather than taking decisions in isolation as regards a particular segment.

IV. ACTION PLAN

1. For policy changes (Macroeconomic measures)
   a. Critical review of performance of the players by IRDA for formulating policy decisions
   b. Meeting of industry representative especially of the private sector with IRDA

2. For players (Microeconomic measures)
   a. Employee motivation
   b. Reduction of operating cost
   c. Proper risk assessment before underwriting the risk to minimize the claims, for example, agririsk assessment through weather and acreage rather than weather alone as per the present practice.