Chapter II

Scenario of the Life Assurance Industry
2.1 The Indian Life Assurance sector

Until the year 2000, the entire life insurance business in India was with the public sector. With financial reforms in the insurance sector and the opening up of this sector, all the private entities entered the business and there was strong competition. A number of foreign insurance companies in both life and non-life segment entered by way of joint ventures with an equity stake of up to 26 percent in the local companies. Approx. Rs. 8.7 billion was brought in by these companies through foreign investments, with the extant provision of 26 per cent foreign capital. The Indian insurance market was growing at an annual rate of 21.9 per cent (IRDA, 2005).

With the progress of reforms in the year 2000, the Insurance market at India was flooded with a number of players. In the year 2005, the insurance market in India, accounted for less than one percent of the global insurance market. However, studies indicated that India’s insurance market would grow rapidly in the next 10 years. In terms of ‘insurance penetration ratio (defined as ratio of insurance premium to GDP), a key indicator of the spread of insurance coverage and insurance culture, India is behind by international standards. The penetration ratio was less than one per cent in 1990s and it improved to 4.8% by end-March 2006. Based on the given penetration ratio, in a country with more than 1.2 billion population, a vast majority of population remains uninsured, especially in rural and semi-urban areas. (IRDA 2006).

Of the total new policies issued, the share of private sector sharply increased and the public sector insurers’ share declined. This implied an increased preference towards the private sector insurers. The existing insurance business is by and large concentrated in and around the towns, cities and metros and still a vast majority of rural areas and even people in urban unorganized sector are yet to be covered.
2.2 Life products before and after deregulation

In the past, the LIC had three commonly sold policies in the market for life insurance: whole life, endowment and money-back policies. The number of new policies sold each year went from about 0.95 million a year in 1957 to 26.97 million in 2003. The total number of in-force policies went from 5.42 million in 1957 to 141 million by March 2003. Following the entry of the private insurers, there was a proliferation of products. According to the Annual Report of the IRDA, 116 life products were offered by life insurance companies in India as of 31 March 2002. However, many products across different companies were very similar, if not identical.

Types of Life Assurance Policies

- **Whole life policies** - Cover the insured for life. The insured does not receive money while he is alive; the nominee receives the sum assured plus bonus upon death of the insured.

- **Endowment policies** - Cover the insured for a specific period. The insured receives money on survival of the term and is not covered thereafter.

- **Money-back policies** - The nominee receives money immediately on death of the insured. On survival the insured receives money at regular intervals during the term. These policies cost more than endowment policies.

- **Annuities / Children's policies** - The nominee receives a guaranteed amount of money at a pre-determined time and not immediately on death of the insured. On survival the insured receives money at the same pre-determined time. These policies are best suited for planning children's future education and marriage costs.

- **Pension schemes** - are policies that provide benefits to the insured only upon retirement. If the insured dies during the term of the policy, his nominee would receive the benefits either as a lump sum or as a pension every month.
2.3 Private and Public Sector Life Assurance firm(s)

The Insurance industry earlier comprised of only two state insurers. Life Insurers i.e. Life Insurance Corporation of India (LIC) and General Insurers i.e. General Insurance Corporation of India (GIC) GIC had four subsidiary companies. The first batch of licenses was issued by the Insurance Regulatory and Development Authority (IRDA) in 2001.

Following companies operated in the Life Assurance sector as in the year 2006.

1. Bajaj Allianz Life Insurance Company Limited
2. Birla Sun Life Insurance Co. Ltd
3. HDFC Standard Life Insurance Co. Ltd
4. ICICI Prudential Life Insurance Co. Ltd
5. ING Vysya Life Insurance Company Ltd.
6. Life Insurance Corporation of India
7. Max New York Life Insurance Co. Ltd
8. Met Life India Insurance Company Ltd.
9. Kotak Mahindra Old Mutual Life Insurance Limited
10. SBI Life Insurance Co. Ltd
11. Tata AIG Life Insurance Company Limited
12. Aviva Life Insurance Company India Limited
14. Bharti AXA Life Insurance Company Ltd.
2.4 Competition

Even when market liberalisation was at an early stage, it produced significant changes on various levels of the industry. The most evident of these was the strong growth among private sector companies. In the 2003 financial year, private life assurance companies collectively accounted for 14% of gross premiums, up from 9.5% in 2002 and 3% in 2001. In growth terms, the 70% surge in premiums received by private sector insurers was far more than the 7.1% registered by their public sector counterparts. Within private companies, both ICICI Lombard (General Insurers) and Bajaj Allianz (Life Insurers) were the market leaders with market shares of around 3%, followed by Tata AIG. Several factors accounted for the market penetration by private insurers. First was their ability to develop new distribution channels to rival the existing distribution network of the government organization. They were particularly successful in forming bancassurance partnerships while direct marketing and online distribution became were also popular. At that time, the IRDA introduced a new legislation that allowed new forms of intermediaries like co-operative societies and brokers as distribution channels. The private companies were more innovative and introduced competitive products with specialized features.

2.5 Diversification in life insurance activities – focus on modes of distribution

In today's scenario, insurance companies must move from merely selling insurance to marketing it as an essential financial product. The distributors play a dual role – as trusted financial advisors for the clients and trusted business associates for the insurance companies.

An insurer needs to think about the appropriate distribution channel to reach its target customer as well as the product that it is going to sell. The choice of customer and the nature of product influence the distribution structure. However in India, joint ventures are formed such that distribution structures are often pre-determined by the nature of
partners. For instance, if one of the partners in a tie-up is a bank, the focus is commonly on Bancassurance whereas if the joint venture is one with a corporate house, the majority business is through the agency channel. The insurer's decision on product features; pricing and target market is highly influenced by the distribution structure that the joint venture is in.

Prior to the formation of the IRDA, the insurance products were dispensed mainly through the following traditional major channels: (1) development officers, (2) individual agents and (3) direct sales staff. The other forms of channels such as corporate agents including bancassurance, brokers (an independent agent who represents the buyer, rather than the insurance company, and tries to find the buyer the best policy by comparison shopping), internet marketing and telemarketing were added on a professional basis in line with the international practice later on.

2.5.1 Agency as a channel of distribution

Agency, as a channel of insurance distribution involves selling insurance policies through tied agents which are hired by insurance companies on a commission basis. Prior to 2000, the Life Insurance Corporation of India ("LIC") was the only player in the Indian insurance market and it emphasized on hiring agents to sell its insurance policies. At that time, LIC had around 800,000 agents across the country and agency was the core distribution channel in the insurance market, when the market was opened up to new entrants. Agency still forms an important part of the distribution network for many companies as it is a channel that delivers top-line growth. This form of distribution has its own challenges.

- There is a shortage of qualified candidates willing to enter an agency career on a full-time basis. As most of the agents are part timers, the productivity levels are very low due to their low levels of commitment and involvement. Companies with a highly expanding agency channel have productivity levels of one or even less than one policy sale per agent per month.
• There are difficulties in imparting agency training and education in remote parts of the country and there are costs involved in retaining agents, and lowering agent turnover.

• The levels of agency commissions create situations where agents try to sell larger numbers of policies, without considering the needs of the policyholders. This leads to high lapse rates of policies. The average number of transactions conducted by agents is very low (by international standards). A large proportion of them do not have access to telephones, electricity or computers. For some companies, turnover of agents has become a major concern.

The above issues along with a need to beat the competition have made it necessary for insurers to diversify into alternative channels of distribution.

2.5.2 Bancassurance as a channel of distribution

Bancassurance, *i.e.*, banc + assurance, refers to banks selling the insurance products. Bancassurance term first appeared in France in 1980, to define the sale of insurance products through banks' distribution channels (*SCOR 2003*). This term is familiar among the European countries as banks selling insurance products in most of these countries are a common feature. Banks are being used as an effective alternate channel to distribute insurance products either as 'stand-alone insurance products' or 'add-ons to the bank products' by way of combining the insurance with typical banking products/services. According to IRDA, ‘bancassurance’ refers to banks acting as corporate agents for insurers to distribute insurance products. Literature on bancassurance does not differentiate if the bancassurance refers to selling of life insurance products or non-life insurance products. The term bancassurance does not just refer specifically to distribution alone. Other features, such as legal, fiscal, cultural and/or behavioural aspects also form an integral part of the concept of bancassurance (*SCOR 2003*).
The concept of Bancassurance originated in France and is a predominant source of insurance business there. The degree of integration in various Bancassurance models is given in the table below:

<table>
<thead>
<tr>
<th>Distribution Agreements</th>
<th>Strategic Alliances</th>
<th>Joint Ventures</th>
<th>Financial Service Group</th>
</tr>
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<tbody>
<tr>
<td>- Banks distribute life insurance products stand-alone or bundled with bank products in return for fee income.</td>
<td>- A higher degree of integration in product development service provisions and channel management.</td>
<td>- Clear mutual ownership of products and customers.</td>
<td>- Operations and systems can be fully integrated.</td>
</tr>
<tr>
<td>- No or little sharing of customer database.</td>
<td>- Possible sharing of customer database.</td>
<td>- Sharing of customer databases</td>
<td>- A high capability to leverage on banks existing customer and other service priorities.</td>
</tr>
<tr>
<td>- Limited investments</td>
<td>- Requires investments in IT and Sales Personnel.</td>
<td>- Requires strong and long-term commitments from both sides.</td>
<td>- One-stop financial services.</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>- Potential for fully integrated products.</td>
</tr>
</tbody>
</table>

Source: Swiss Re Sigma 2002

A survey by LIMRA identified the following ten elements for success of bancassurance:
2. Sales Staff Management/Training.
3. The Branch Network/Geographical Coverage.
4. Bank and Insurance products form a complementary range.
5. Single view of the customer.
8. Integration of the bank and insurance organizations producing a single culture.
9. Providing advice/solutions, not selling products (taken from the presentation of Marielle Theron at the SwissRe India CEO Summit, 2003).
2.6 Bancassurance in various foreign countries

The strategy of bancassurance has been highly successful in Europe. France and Portugal are stated to be most successful in bancassurance wherein as much as 70% of the insurance products were sold through the banking channel alone followed by Spain where more than 59% of the insurance products were being sold through the banks. In countries such as Belgium and Italy, the bancassurance concept picked up only since the late 1990s. As opposed to the above, in the UK and the Netherlands the concept of bancassurance was less popular although banks sold the insurance products. In Germany the system of universal banking is predominant and bancassurance is not very popular. Most important factors for the success or otherwise of bancassurance in most of these countries cited in the literature is the favourable legal system in the respective country, supported by the availability of strong banking infrastructure coupled with the banking culture. The system of ‘relationship banking’ has contributed significantly in building up of bancassurance. A flexible banking system catering to understand the needs and requirements of the customers intimately is considered to be best suited for bancassurance. In other words, ‘stronger the bank - customer relationship’ higher the prospects for bancassurance. Above all, the reputation of the banks was also stated to have played a key role popularising the concept of bancassurance. Fiscal factors in the form of tax incentives also played crucial role in some countries such as France (SCOR 2003). Despite areas of conflict such as ‘conflict of interest’ and substitution rather than complimentary effect, Bancassurance has been successful in many countries.

2.6.1 Europe and the United Kingdom

In this part of the world, more than half of the insurance business is transacted by banks. In France, Portugal and Spain, banks handle over half of life insurance business. Selling through banks is found to be more cost effective and efficient than selling through other channels. Average time taken to realize the benefits is given as 3 years. Average cost saving is 21.2% and expected revenue gain is 4.4%. Bancassurance has been a successful model in the European countries contributing 35% of premium income in the
European life insurance market. It contributes over 65% of the life insurance premium income in Spain, 60% in France, 50% in Belgium and Italy. (year 2005) In France, there is no tax advantage via bancassurance however it has a longer history than the United States dating back to the implementation of the Second Banking Directive of the European Union in 1986. In France, the sale of insurance products is mainly handled by bank employees, where as in markets such as Germany and Switzerland, bancassurers utilize their own sales force to promote their products at an allied bank.

The two main business models implemented in Life European bancassurance are the integrated model and the advice-based model.

**Integrated model** - this is the most common model in Southern Europe, banking and insurance activities are closely integrated, sales of insurance products are performed by branch staff and the insurance products are designed specifically to fit in the bank’s culture.

**Advice-based model** - more often implemented in Germany or the United Kingdom, sales are usually done by dedicated insurance advisers and insurance products are very similar to products sold through other channels. An analysis of performance indicators shows that the integrated model performs better from both commercial and cost points of view.

### 2.6.2 United States of America

In the United States, the banks were earlier not allowed to sell insurance due to the restrictions imposed by Glass-Stegall Act of 1933. As a result of this life insurance was primarily sold through individual agents, who focused on wealthier individuals, leading to a majority of the American middle class households being under-insured. With the repealing of this Act in 1999, banks were permitted to distribute insurance and cater to the large middle class segment. The most common structure of a Bancassurance tie-up in Latin America begins with approximately equal ownership of the joint-venture insurance company by the partners.
From the US corporate customer’s point of view, bancassurance is perceived as adding little value. A survey of senior-level financial executives at 444 US companies, conducted by the Association for Financial Professionals, revealed that 70% of respondents reported a preference for an insurance company that has not combined with a bank or securities firm, while only 14% said that they would use a bank that has merged with an insurance company for the purchase of insurance products.

2.6.3 Bancassurance at Asia

A growing number of alliances, mergers and acquisitions and joint ventures between banks and insurance companies show the increasing importance and contribution of Bancassurance at Asia. Bancassurance has evolved as a model that complements and even challenges the traditional agency sales model for marketing of insurance. In Asia there are three basic routes to the partnership with the level of integration of the insurer and the distributor being the main distinguishing feature. Most bancassurance deals in Asia involve only distribution agreements. Joint ventures are popular in places where foreign insurers can enter the market only with a domestic partner. Most bancassurers offer life insurance products and the major sales drivers are the bank staff. The main life insurance products sold include term and whole life products. Foreign insurers are more inclined to enter into Bancassurance agreements with local partners.

In many Asian countries, bancassurance has become an important channel but, unlike in some countries in Continental Europe (e.g., Portugal, France, Spain, Belgium), it is not the main channel of distribution of insurance. Countries with relatively high bancassurance share of life insurance distribution are Hong Kong (25%), Singapore (15%), Thailand (12%) and Malaysia (11%) in 2001. (Source: Leo Puri’s presentation at the Swiss Re CEO Summit). In other countries in the region, such as China, Indonesia and the Philippines, the share of bancassurance was rather small (5% or less in 2001). Some other factors also play a role such as Banks seeking ways to raise additional earnings without commitment of additional capital in a low interest rate environment; increased competition; reducing margin. Insurance Companies are seeking new customers using
new distribution activities to reach such segment. Distribution agreements were at 69% in the structural models for Bancassurance distribution at Asia, Joint Ventures at 17% and Financial Services Group 14 % as per information from Swiss Re in 2002

For the Asian insurance markets the proliferation of Bancassurance implies

- Growth of multi-channel distribution.
- Separation of distribution and manufacturing of insurance products.
- The ability to tap into the large customer base of banks to be an important performance parameter
- Increased benefit to product innovation from the development of Bancassurance
- “Greenfield” startup operations without the need to recruit a large number of agents
- Financial institutions to leverage on Bancassurance to compete for household financial assets
- Increased focus on distribution rather than clubbing with manufacturing.
- Ability of insurance companies and banks together to tap into the large customer base.

Information on Bancassurance distribution in some of the Asian insurance markets is given below:

2.6.3(a) Singapore

Singapore was the pioneer of Bancassurance business in Asia. Bancassurance accounted for 24% of new life insurance sales by ‘weighted’ premium income in Singapore in 2002.

2.6.3(b) China

In China, the regulatory enforced maximum arrangement fee of 8% and this has led to the vast majority of sales to date being single premium. Foreign brokers in China operate only in the form of representative offices or risk managers / insurance consultants. The traditional agent-led distribution channel continues to be a major distribution channel for insurers. However, insurers are experimenting with alternative distribution channels.
More and more insurers are using multiple distribution channels to balance the needs of different groups of consumers against the cost of distributing their products and services.

2.6.3(c) Japan

The first phase of deregulation of bancassurance in Japan began on April 1, 2001. Known as the Big Bang, the deregulation of insurance had started since the year 1096 in most parts of the world. The range of products that banks could distribute was expanded from October 1, 2002. One of the first products that banks could sell was credit life. As from April 2001, banks in Japan are allowed to sell long term fire, long term disability and long term credit life policies connected with housing loans as well as overseas travel accident insurance. The list was further expanded from October 2002 to include personal pension insurance, zaiket savings (asset formation), individual annuity, accident insurance and zaiket savings personal accident insurance. There is near monopoly of agents in Japan and it holds a large share of the region’s premium pool.

2.6.3(d) Thailand

Thai banks can broker life and non-life insurance products under a brokerage license from Insurance Department under the Ministry of Commerce.

2.7 Bancassurance at India

Bancassurance as a concept first began in India with the opening up of the insurance industry to private sector participation in December 1999, which saw the entry of 20 new players – with 12 in the life insurance sector and 8 in the non-life sector. As in 2006, there were 14 life insurance companies with approx. 40 national level and 100 regional level bancassurance alliances. The Indian Bancassurance market has seen a number of strategic alliances between banks and insurance companies with a common vision of distribution reach, costs, geographical spread and target audience. By 2010, Bancassurance is likely to contribute 30 per cent to the overall pie of insurance business.

The points below give background information on Bancassurance at India
1. The RBI has laid down three options for banks to take part in insurance business. The first option is for financially strong banks to form joint ventures with insurers. Banks that are not considered strong enough can invest 10% of their networth or INR Rs. 50 crores whichever is lower. Finally banks can enter into distribution agreements with insurers where banks work as Corporate Agents on behalf of the insurance companies.

2. In the 2001 Report on Currency and Finance, the RBI laid down its views in more concrete term. “The Reserve Bank, in recognition of the symbiotic relationship between banking and the insurance industries, has identified three routes of banks’ participation in the insurance business, viz., (i) providing fee-based insurance services without risk participation, (ii) investing in an insurance company for providing infrastructure and services support and (iii) setting up of a separate joint-venture insurance company with risk participation. The third route, due to its risk aspects, involves compliance to stringent entry norms. Further, the bank has to maintain an ‘arms length’ relationship between its banking business and its insurance outfit.

3. For banks entering into insurance business with risk participation, the prescribed entity (viz., separate joint-venture company) also enables to avoid possible regulatory overlaps between the Reserve Bank and the Government/IRDA. The joint-venture insurance company would be subjected entirely to the IRDA/Government regulations.”

4. In India, the local regulations encouraged the development and promotion of this channel. At India, banking is still in the 'brick and mortar' model, as most of the customers still walk into the bank branches. This enables the bank staff to have a personal contact with their customers, which is very essential for insurance selling.

5. In the absence of financial planners in India, traditionally the bank managers act as investment advisors to their customers, especially in smaller towns and cities. Due to the proximity, the seller can provide solutions based on the detailed profile of a customer. Moreover, the bank manager would intend to further develop the trust bestowed on him by offering the right kind of insurance solutions.
6. The bank network - especially the public sector and cooperative bank branches are spread across the length and breadth of the country with 65,000 plus branches. This enables the insurance companies to reach out to each and every individual in the country who needs life insurance.

7. Banks with their huge networks and large customer bases give insurers an opportunity to grow quickly without heavy initial startup expenses and overhead runs.

8. Regulations require certain proportions of sales to the rural and social sectors selling through traditional methods to these sectors can be inefficient and expensive. Tying up with a bank with an appropriate customer base can give an insurer relatively cheap access to such sectors.

9. In India, as elsewhere, banks are seeing margins decline sharply in their core lending business. Consequently, banks are looking at other avenues, including the sale of insurance products, to augment their income.

10. The sale of insurance products can earn banks very significant commissions (particularly for regular premium products). In addition, one of the major strategic gains from implementing bancassurance successfully is the development of a sales culture within the bank. This can be used by the bank to promote traditional banking products and other financial services as well.

11. In addition to acting as distributors, several banks have recognised the potential of insurance in India and have taken equity stakes in insurance companies. This is similar to the United Kingdom and elsewhere where banks started off as distributors of insurance and moved to a manufacturing role with fully owned insurance subsidiaries.

12. In India, there are a number of reasons why bancassurance could play a natural role in the insurance market. First, banks have a huge network across the country. Second, banks can offer fee-based income for the employees for insurance sales. Third, banks are culturally more acceptable than insurance companies. Some bank products have natural complementary insurance products. For example, if a bank gives out a home loan, it might insist on a life insurance cover so that in case of death of the borrower, there is no problem in paying off the home loan. Similarly,
a car loan could only be given if comprehensive auto insurance is taken out on that particular car. (*Tapen Sinha 2005*)

Bancassurance partnerships for Insurance companies at India is given below:

<table>
<thead>
<tr>
<th>Banking partner</th>
<th>HDFC Standard Life</th>
<th>Union Bank of India, Indian Bank, HDFC Bank</th>
</tr>
</thead>
<tbody>
<tr>
<td>ICICI Prudential Life</td>
<td>Federal Bank, ICICI Bank, Bank of India, Punjab &amp; Maharashtra Cooperative Bank, Allahabad Bank, South Indian Bank, Citibank, Lord Krishna Bank, Goa State Co-operative Bank, Indore Paraspahakari Bank and Jalgaon People’s Co-operative Bank, Shamrao Vithal Co-operative Bank</td>
<td></td>
</tr>
<tr>
<td>Birla Sun Life</td>
<td>Citibank, Deutsche Bank, IDBI Bank, Development Credit Bank, Bank of Rajasthan, Bank Muscat, Catholic Syrian Bank Ltd., Andhra Bank, Karur Vysya Bank Ltd.</td>
<td></td>
</tr>
<tr>
<td>TATA AIG Life</td>
<td>HSBC, Citibank, IDBI Bank, Union Bank of India</td>
<td></td>
</tr>
<tr>
<td>Om Kotak Mahindra</td>
<td>None</td>
<td></td>
</tr>
<tr>
<td>SBI Life</td>
<td>SBI, BNP Paribas</td>
<td></td>
</tr>
<tr>
<td>ING Vysya Life</td>
<td>Vysya Bank, Bharat Overseas Bank</td>
<td></td>
</tr>
<tr>
<td>Allianz Bajaj Life</td>
<td>Standard Chartered Bank, Syndicate Bank</td>
<td></td>
</tr>
<tr>
<td>MetLife</td>
<td>Dhanalakshmi Bank, J &amp; K Bank, Karnataka Bank</td>
<td></td>
</tr>
<tr>
<td>AMP Sanmar</td>
<td>Manjeri cooperative, Perunthalmanna Bank, Nilambur Bank (all Kerala based)</td>
<td></td>
</tr>
<tr>
<td>Aviva Life</td>
<td>ABN Amro, American Express, Canara Bank, Lakshmi Vilas Bank</td>
<td></td>
</tr>
</tbody>
</table>

*Information updated from newspaper sources and websites of the respective banks and insurance companies as on March 2004*

13. The first feature of the above table is the “natural partnerships”. Eg. HDFC Standard Life is linked to HDFC Bank, ICICI Prudential Life with ICICI Bank. The second focus area is the proliferation of banks partnering with single insurance companies. Insurance companies targeted different market segments by affiliating with banks that focus on niche banking. An example is Aviva Life. It has developed a three-layered strategy. The first layer is an affiliation with ABN Amro and American Express which cater to high net-worth urban customers. The second layer is an affiliation with Canara Bank. Through this nationalised bank
with 2400 branches, it reaches customers across the length and breadth of the country. The third layer, at a regional level, is an affiliation with Lakshmi Vilas Bank focusing on region-specific customers. This affiliation helps them to reach customers in rural and semi-urban centres in Tamil Nadu and Andhra Pradesh. Another feature is that some insurance companies such as Allianz Bajaj have different banking partners in the life sector and the non-life sector. The same is true for several other companies. Some banks have affiliations with several insurance companies. For example, Citibank appears in the lists of a number of life and non-life insurance companies. It may be that the bank has only Referral Arrangements with several insurance companies but not acting as corporate agents for them. This fact will become more important as a warning by the RBI that banks should not adopt any restrictive practice of forcing its customers to choose a particular insurance company becomes an issue in the future. (Tapen Sinha 2005)

2.7.1 Bancassurance distribution strategies

Life insurers adapt different strategies when choosing bancassurance partners. Some insurers, such as ICICI Prudential, have tied up with a large number of public and private sector banks (including ICICI Bank), as well as several cooperative banks. Birla Sun Life, on the other hand, selected only a few banks within each of the above categories. Similarly, Aviva, which sourced the majority of its business through bancassurance, has tied up with five banks combining public sector, private sector and foreign banks, a strategy that provides access to a variety of geographical regions and customer profiles.

2.7.2 Bancassurance Models at India

Most of the bancassurance relationships in India started with a ‘referral’ type arrangement, where bank staff provide leads to a specialist insurance company sales
force, in return for which, the bank receives a ‘fee’. Although this model is still adopted by some insurers, the banking and insurance regulators consider it a ‘misuse of personal customer data’ collected by referral agents of insurance companies posted at bank branches. The main alternative model is more bank-centric in its sales approach. Banks have to obtain a corporate agency license to permit bank staff to distribute insurance. In this model, bank staff carries out the selling activities, and the bank receives a commission for the sales as per the corporate agency agreement.

The distribution agreements on which these models are reliant typically have durations ranging from one to 10 years. Most agreements are loosely worded, without the bank partners paying much attention to the customer servicing responsibilities in the post-sale phase. Some banks have taken a more committed approach, taking an equity stake in a new joint venture life insurance company.

I. Structural Classification

a) Referral Model

Banks intending not to take risk adopt ‘referral model’ wherein they merely part with their client data base for business lead for commission. The actual transaction with the prospective client in referral model is done by the staff of the insurance company either at the premise of the bank or elsewhere. Referral model is a simple arrangement, wherein the bank, while controlling access to the clients database, parts with only the business leads to the agents/ sales staff of insurance company for a ‘referral fee’ or commission for every business lead that was passed on. This model is suitable for almost all types of banks including the RRBs/cooperative banks and even cooperative societies both in rural and urban. There is greater scope in the medium term for this model.

b) Corporate Agency

The other form of non-risk participatory distribution channel is that of ‘corporate agency’, wherein the bank staff is trained to appraise and sell the products to the customers. Here the bank as an institution acts as corporate agent for the insurance products for a fee/ commission. This is more viable and appropriate for most of the mid-sized banks in India as the rate of commission is higher than the referral arrangement.
This, however, is prone to reputation risk of the marketing bank. There are also practical difficulties in the form of professional knowledge about the insurance products. Besides, resistance from staff to handle totally new service/product is there. This is overcome by intensive training to chosen staff along with suitable incentives in the banks coupled with selling of simple insurance products in the initial stage. This model is best suited for majority of banks including some major urban cooperative banks because neither there is sharing of risk nor does it require huge investment in the form of infrastructure and yet could be a good source of income.

c) Insurance as Fully Integrated Financial Service/ Joint ventures
Apart from the above two, the fully integrated financial service involves much more comprehensive and intricate relationship between insurer and bank, where the bank functions as fully universal in its operation and selling of insurance products is just one more function within. This includes banks having a wholly owned insurance subsidiary with or without foreign participation. In India, ICICI bank and HDFC banks in private sector and State Bank of India in the public sector, were the pioneers in this type of bancassurance model and have acquired a sizeable share in the insurance market. The great advantage of this strategy is that the bank could make use of its full potential to reap the benefit of synergy and therefore have economies of scope. This is suitable for larger banks with sound financials and better infrastructure. Even if the banking company forms as a subsidiary and insurance company is a holding company, this could be classified under this category, so long as the bank is selling the insurance products along side the usual banking services. As per the extant regulation of insurance sector the foreign insurance company could enter the Indian insurance market only in the form of joint venture, therefore, this type of bancassurance seems to have emerged out of necessity in India.

II. Product-based Classification
i) Stand-alone Insurance Products
In this case bancassurance involves marketing of the insurance products through either referral arrangement or corporate agency without mixing the insurance products with any
of the banks' own products/services. Insurance is sold as one more item in the menu of products offered to the bank's customer, however, the products of banks and insurance will have their respective brands too, e.g.,

**ii) Blend of Insurance with Bank Products**

This strategy aims at blending of insurance products as a 'value addition' while promoting the banking products. Thus, banks could sell the insurance products without any additional efforts. In most times, giving insurance cover at a nominal premium/fee or sometimes without explicit premium does act as an added attraction to sell the bank's own products, e.g., credit card, housing loans, education loans, etc. Many banks in India, in recent years, are aggressively marketing credit and debit card business, whereas the cardholders get the 'insurance cover' for a nominal fee or (implicitly included in the annual fee) free from explicit charges/premium. Similarly the home loans / vehicle loans, etc are also bundled with the insurance cover as an additional incentive.

**2.7.3 Outlook of bancassurance development**

Despite bancassurance being a new feature to the Indian insurance market, it is becoming a key channel for the distribution of insurance products. One major catalyst has been the flexibility of IRDA in prescribing the relevant regulatory framework. The previous restriction requiring all corporate agencies (such as a bank) to undertake 100 hours of agency training has been criticized as impractical. Revisions to regulations have seen this requirement narrowed to be applicable only to designated persons within the corporate agencies, thus removing one of the key obstacles to the proliferation of bancassurance in India. In April 2004, insurance companies in India were interviewed on the outlook of their share of distribution through bancassurance over the next five years. For private life insurance companies, the average response was that they expect 35% of their products to be sold through banks within five years. There was a wide variation among the responses from different insurance companies, ranging from as low as 20% to as high as 75%. These findings suggest that the development of bancassurance will accelerate. *(Source: Study done by Dr. Tapan Sinha Swiss Re)*
2.7.4 Share of bancassurance sales

Bancassurance has been growing very rapidly in India. Within the first two years (2002 – 2004), the share of insurance business distributed through bancassurance went up from zero to 20% of new business in the private sector. The table below provides a view on the rapid growth of bancassurance in India. It gives the Bancassurance business conducted by various companies in the above period.

<table>
<thead>
<tr>
<th>Company</th>
<th>% of policies</th>
</tr>
</thead>
<tbody>
<tr>
<td>ICICI Prudential Life</td>
<td>15% in 2002. 22% in 2003</td>
</tr>
<tr>
<td>SBI Life</td>
<td>15% in 2002. 50% in 2003</td>
</tr>
<tr>
<td>Birla Sun Life</td>
<td>25% in 2002. 40% in 2003</td>
</tr>
<tr>
<td>INV Vysya Life</td>
<td>10% in 2002</td>
</tr>
<tr>
<td>Aviva Life</td>
<td>50% in 2002. 50% in 2003</td>
</tr>
<tr>
<td>Allianz Bajaj Life</td>
<td>25% in 2003</td>
</tr>
<tr>
<td>HDFC standard Life</td>
<td>10% in 2002. 30% in 2003</td>
</tr>
<tr>
<td>MetLife</td>
<td>25% in 2002</td>
</tr>
</tbody>
</table>

Source: Newspaper reports – various dates

2.8 Bancassurance – What is in store for Customers?

In insurance business the question of trust plays an important role, especially due to the inbuilt requirement of a long term relationship between the insurer and the insured. In India, for decades, customers were used to the monopolistic attitude of public sector insurance companies, despite there were many drawbacks in their dealing, they enjoyed customer confidence, this trend continues even now mainly due to their Government ownership. The void between the less known newer private insurance companies and the prospective insured could be comfortably filled by the banks because of their well established and long cherished relationship. Above all, customers prefer to have a consolidation and delivery of all financial services at a single window in the form of ‘financial super market’, irrespective of whether financial or banking transactions, because such availability of wide range of financial/ banking services and products relieves the customers from the efforts of scouting for a separate dealer for each service/ product.
2.9 Why Banks are motivated to enter Insurance Business

Some of the reasons are as follows;
(1) Overstaffing problem can be reduced (2) Banks seek to retain customer loyalty by offering them an expanded and more sophisticated range of products (than simple bank deposits of few varieties). (3) Insurance distribution will increase the fee-based earnings of banks. (4) Fee-based selling helps to enhance the levels of staff productivity in banks. This is a key driver for raising motivation among bank employees.

Banks have some in-built advantages in some of these areas. (1) Banks can put their energies into the small-commission customers that insurance agents would tend to avoid. (2) Banks’ entry in distribution helps to enlarge the insurance customer base rapidly. This helps to popularize insurance as an important financial protection product. (3) Bancassurance helps to lower the distribution costs of insurers. A study by Tillinghast, Towers and Perrin in the UK shows that the cost of selling insurance through direct sales force is approximately twice as high as the cost of selling through bancassurance. However, the cost of selling the products through independent financial advisers is approximately the same as bancassurance (quoted in Sigma 7/2002). Acquisition cost of insurance customer through banks is low. Experience in Europe has shown that bancassurance firms have a lower expense ratio. This benefit could go to the insured in the form of lower premiums.

There are a good number of theoretical reasons as to why banks are in the insurance market in India. The bank gains in terms of

1. Improved profit margins which are reduced due to competition and falling interest rates affecting the core operations
2. Effective utilization of the resources (human & infrastructural)
3. Greater fee based income adding to the non-interest income
4. Exploiting the huge base of customers they have on their retail banking operations
5. Some way of asset securitization by selling insurance as an add-on to the customers availing advances from bank
6. Value addition in their services
7. A futuristic plan for banks to transform themselves from mere providers of banking products to the position of individual financial counselors on retail basis

Chapter summary

The Life Assurance Industry globally is facing changing scenarios in terms of modes of operation and those of distribution channels. There are three basic distribution agreements for insurance products viz referral arrangement, corporate agency and joint ventures. The degree of integration is dependent on mutual consent between the bank and the insurance company partnership.

Although the drivers for the development of bancassurance in India are similar to other countries in Asia Pacific, the main difference is the size of the banking network available and the relatively small number of life insurance players. Banks are seeing margins decline on their core banking businesses and are, therefore, seeking alternative sources of fee income. The insurance companies are looking to diversify distribution channels and move away from an over-reliance on agency.

The large size of the banking sector in India provides opportunities to reach certain sectors (for example rural India, with approximately 50 per cent of the 65,000 or so bank branches located in these areas) or target markets. The diversity of potential opportunities should allow insurance companies to experiment with different distribution models.
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