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## Research Paper

## ROLE OF LIC IN NATION BUILDING-A REVIEW

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### ABSTRACT

**I**n 1956 when the former Finance Minister Shr. C D Deshmukh introduced the insurance bill, said “ Nationalization of insurance industry has been a long felt need in order that the interests of the insuring public and industry could be safeguarded, the country’s economy promoted and more funds are provided for economic development”.

If we take each and every aspect of this nationalization bill and subsequent creation of LIC, there is no doubt that the purpose was amply met. I salute C D Deshmukh and others for positioning this August institution and also other executives for taking this Institution in a very safe guarded path.

**KEYWORDS:** *economy, savings, insurance, economic development, social sector*

### INTRODUCTION

Since 1956 this Institution has done an excellent service to the Nation in providing affordable insurance and provided a useful channel for mobilizing the savings of the public, especially the middle class people. These savings are utilized for a number of infrastructure projects, uplift of social sector and also helped the Government to meet her fiscal deficit target. Hence every segment of the Society was benefitted by this organization.

The insurance sector was opened up in 2000 after the IRDA Bill was approved. 16 years have passed since then. New player came to the market. Today we have 23 private players.

### DISCUSSION

Before 2000, LIC used to offer only endowment policies and very few money back and pure life cover policies. There were some pension products also. When the opening up of the market, a number of new products including unit-linked products were introduced. Combining the globalization and opening up of the Indian economy, Indian customers were introduced to

various types of other non-traditional insurance products available in many other countries, in particular USA, UK etc.. In the last 15 years, LIC introduced unit-linked, money back, creditor insurance products etc. By this process, LIC has amply met the changing pattern of consumers’ demand and withstood the competition successfully. It is very important to note that LIC accounts for about 75 per cent of the life insurance industry’s first year premium. The durable contribution of LIC in the economic development of India is substantial. LIC has not only contributed in growth numbers but also in the quality of life of Indians. Hence both through quantum and through quality LIC has made her contributions. Let me take this opportunity to elaborate them.

- a. Savings are important drivers of growth. Even among savings, financial savings are assuming more importance. The premium collected by LIC from households account for a substantial portion of financial savings of the households. LIC collected Rs. 75,083 crore as premium during



- 2004-05 and this has increased to Rs. 2,66,225 crore in 2015-16. This premium collection accounts for a significant proportion of financial savings of the households.
- b. Savings are transformed into investments. These investments are made both as direct or through financial instruments in subscribing to loan capital, where the money invested is used for development purposes. The Life Fund of LIC is Rs 20, 57, 625 crore at March end 2016. About 90 per cent of this investment is made via securities and about 7 per cent by way of loans against policy documents and other investments account for about 3 per cent. A careful analysis of the investment made by LIC clearly shows that whenever the market needs a push and support, LIC stands ready. Moreover her investment helped not only the stock market but also Government security market. This clearly proves the important position enjoyed by LIC in the investment scenario of India.
  - c. Infrastructure development is backbone of our growth picture. LIC's contribution in infrastructure development is well documented. In 2015-
- 16, LIC has invested Rs 23, 564 crore under infrastructure projects. On an average, during 2004-05 to 2010-11, about 50 per cent of the infrastructure investment was for power sector, housing -25 per cent, water supply and sewerage 7 per cent and others about 10 per cent. In the later years, power sector -10 per cent, housing 45 per cent, water -5 per cent and other 40. Even under infrastructure development, the share of rural sector is substantial.
- d. Entrepreneurial development is key for innovation and industrial development. Many years back, LIC introduced 'key man policy' so that companies can retain the key persons so that their competitive position could not be diluted. Many joint stock companies, which are run on the name of one or two persons benefitted a lot from these innovative product. When the sector was opened up, many private sector life companies introduced mis product.
  - e. In the present way of life, younger people take substantial amount of housing loan etc.. In the unfortunate event, the family will not only loose the bread-winner but will also loose the house. In order to protect them, creditor protection products were introduced and this was attached with the housing loan. This product helped many families. LIC offered this product at affordable premium and hence the home loan borrowers were not feeling the pinch. By this process investment in housing was encouraged indirectly.
  - f. India does not have a well defined social security system. Many persons working in the private sector and self-employed and majority of rural population did not have proper social security protection. Even though, pension products were introduced by many private sector life insurance companies, they do not offer this product on competitive terms and this pension portfolio accounts for less than 5 per cent of the total. LIC started many pension schemes and premium collected towards pension scheme has increased from Rs. 1766 crore in 2004-05 to 2326 crore in 2011-12. In the subsequent years this has come down to Rs 857 crore in 2015-16. This decline is due to the introduction of 'Varishta Bima Yojana'. By providing these pension products LIC has ensured continued life style for retired people.
  - g. Health insurance is assuming more importance and medical inflation is very high. The cost of any ordinary medical treatment is becoming very costly and beyond the reach of the common man. Under this circumstances, LIC has introduced a couple of health insurance products and the premium collected is Rs. 59 crore in 2015-16. By this, LIC has started offering an affordable health insurance for the Indian public.
  - h. The major strength of LIC is her agent population. As at end March 2016, LIC has employed 10,18,039 effective agents. LIC has started exploring other distribution channel since 2011-12, like bancassurance etc. and a premium of Rs 32,838 crore was collected from these alternative channels during 2015-16. Going by the experience of other countries, there is a general perception that alternative channels are cost effective and lapses and surrenders are less in this segment compared to other channel.

- i. Financial inclusion is the buzz word of the financial sector. There is a perception that a major proportion of population is outside the banking network either for their income or for their credit facilities. Since 2012 a number of steps have been taken to give a major push to 'financial inclusion'. Under this objective LIC has introduced micro insurance products for the benefit of this important segment. LIC has introduced special policies known as 'Madhur Bima Gram' and has collected a premium of Rs 13 crore.
- j. In order to enhance the protection to the vulnerable section of the population, LIC is actively participating in a number of social security schemes, viz., Aam Admi Bima Yojana, Pradhan Mantri Jan Dhan Yojana and offer life cover. So far Rs 381 crore claims have been settled by LIC. As at end March 2016, 5 crore people were covered as compared with 1.41 crore by the end of March 2005.
- h. In addition, LIC is also offering a number of scholarship to the children of these families, so that the earning capacity of these members increase and there shall be a clear visible increase in the standard of living of these people.
- i. For the whole India, LIC served as a reservoir to supply technical people and this supply has helped the private sector and also the regulator to grow, when the sector was opened up since 2000. LIC's contribution in providing eminent actuaries is well known.

All the above clearly exhibit the contribution made by LIC in the economic development of India and also in improving the quality of life of vulnerable section of the population who have very limited access to the formal systems. It is important to recognize that the benefits of these activities goes beyond monetary one and has a number of positive qualitative aspects. In order to nurture these benefits and maintain prime position in the Indian economic scene, LIC may consider the following issues and take timely, adequate and comprehensive actions.

1. The annual premium collection of LIC has increased from Rs. 0.75 crore in 2004-05 to Rs. 2.66225 crore in 2015-16, exhibiting an annual compound growth rate of 12.2 per cent. If we consider the period 2001-16, we can see two distinct phases in the premium collection of LIC, viz., the first phase 2001-2011-12 where average

annual growth rate was 15.3 per cent, where as for the period 2012-13 to 2015-16, this annual compound growth was 7 per cent. Hence we clearly see a deceleration in the growth of premium income. It is very important to analyze the reasons for this deceleration.

If we consider the share of different types of products, first year individual products premium collection accounted for 14 per cent of the total premium income in 2004-05 and this has declined to 8 per cent in 2015-16. Renewal premium, which accounted for 66 per cent in 2004-05 has gone down to 60 per cent. The decline in individual business could be a reason for this decline. Group products, which accounted for 11 per cent in 2004-05 has significantly increased to 32 per cent. Pension products which has a share of 2.4 per cent gone down to 0.3 per cent. LIC introduced unit linked products in 2004-05 and this accounted for 6 per cent share in total premium income. But in 2015-16, this has gone down to less than 1 per cent. Hence growth in group products supported to maintain the growth in total premium income while all other categories witnessed a decline.

In order to understand the concentration of a few products, we worked out the Gini concentration index and mis index revealed that during 2005-11, this index has declined indicating fair degree of diversification of products, but in the later period 2011-16, this has increased indicating the dependency on a few products to achieve the premium target. For a few selected years, Gini concentration index, based on region-wise premium collection, also indicates the increase in concentration in recent years. Hence LIC shall spread her wings in a number of products and may not concentrate on a few products or a few regions in India for their premium growth.

2. The return on investment ( yield rate) was 8.11 per cent in 2015-16 as compared with 9.93 per cent in 2004-05. This yield rate is almost 150- 200 basis points lower than similarly placed bank's yield rate. If we look at the yield rate of NPS managed by LIC, this is in the range of 8.6 to 10.4 per cent: Even though the investment norms are somewhat different for NPS as compared with Life fund, this clearly indicates that there is a wide scope of improving the yield. The Life fund of LIC is Rs 20,57,625 crore at end March 2016. Additional 100 basis points means Rs 20,576 crore. With this additional money, LIC can easily embark on a number of schemes to the benefit for her own staff and Indian public.

3. Non-performing assets is slowly increasing. For the year 2015-16, a provisioning of Rs 4560 crore was made in the books. Although this is only 0.2 per cent, this

provisioning is increasing over time. Today 'non-performing asset issue' is a serious threat to the public sector banks. LIC must take prompt action and bring this down so that NPA shall not be an issue.

4. Closely related to the NPA issue, LIC invests in a number of infrastructure projects of Centre and State Governments. There is no clue as how these investments are performing and how the state governments maintain their repaying schedule. In the recent period, a number of State Governments experienced severe financial strain. In the light of this, LIC shall disclose the performance history of these investments. Please note that the investment of LIC is policyholders' money and the policyholders' have the right to know the performance of these investments. This will also help LIC in streamlining her investments in infrastructure.

5. The share capital of LIC was only 5 crore till 2011-12 and in this year this was increased to 100 crore. Compared with similarly placed financial institutions, for an organization of this size, the capital is very small and once LIC goes for rating, this low capital will affect her rating. The Government of India may consider increasing her capital to at least Rs. 1000 crore.

6. The claim settlement of LIC is extremely good and the families of policyholders benefit a lot by this timely process. But some amount of caution is needed here. If we consider the claim history of other private sector life insurance companies, a number of frauds were brought to light. Hence in order to avoid such situation, on a sample basis, LIC must examine the true nature of claims. This will help LIC to improve their claim processing procedure.

7. It is a welcome development that LIC has introduced other channel for distribution of her products. If we work out the premium collected by the agents force, premium per person has come down. This raises some crucial issues about the productivity of agents. Fortunately the cost of commission and salaries is only 11.3 per cent of the expenses at end March 2016. There is small variation to this percentage in the last 4/5 years. This ratio is much less than the ceiling prescribed by the IRDA. Hence there is room available for increasing the expenses so that their productivity is increased and at the time they are retained for a longer period. It is important to recognize that additional income is more pronounced than additional expenses.

8. In 2014, the RBI has appointed 'Naik Committee' to examine 'Governance of Boards of banks in India'. The Committee came out with a number of findings and also suggested solutions to address these issues. These

findings are very important and clearly exhibit the gap in the way in which these public sector banks are functioning as compared with private sector banks. I do admit that profitability is not the only criteria of public sector banks, but the modus operandi of the manner in which the Board and business are conducted in the public sector banks; there are a number of crucial issues, which need to be addressed quickly. Otherwise, once Basel HI is implemented this is going to have a strong toll on the capital of these banks. I strongly feel that these findings are equally applicable for public sector insurance companies in India, as these insurance companies share a number of commonalities with banks in their working culture including the way in which Board meetings take place. It is high time that these findings are examined with reference to public sector insurance companies and take appropriate actions. I would like to emphasize three aspects here, viz., corporate governance, payment of market related wages rather than Government decided salaries, and Bank Board Bureau. With reference to corporate governance, there are no doubts that LIC is having all sub-committees as envisaged under corporate governance of IRDA. But to what extent issues are discussed and their feeds backs are made available to the Board is not known. It is high time LIC shall mention these aspects in their Annual report. This will not only give credibility to these sub-committees but also enhances their role in an effective and useful functioning of the Board.

Secondly, public sector organization is somewhat handicapped by the pay structure as approved by the Government and like private sector life companies the incentive system is not effective. This ineffectiveness considerably affects the quality of decisions taken by the Board. Hence Board must have necessary powers to hire technical people and also incentives the existing staff so that they take best of them and this would also help in retaining the talent.

Thirdly, consequent to the Naik Committee report, the Government has appointed 'Bank Board Bureau'. This Bureau is responsible for selecting executives and other members of the Board of the banks. I request that this could be renamed as 'Financial sector Board Bureau', as the entire financial sector would benefit from this. It is important to note the Government is the owner of many financial institutions in various segment of the financial sector. This would benefit the financial institutions also as they could get best talents people in their boards.

9. In product development, the future lies in pension and health insurance products. Although LIC is a pioneer in pension products in India, in the last 2/3 years the premium collected is significantly low. It is a fact that no reinsurer is prepared to reinsure pension business because of uncertainty in mortality improvement and volatility of stock markets. International experience clearly says that 'variable annuity products' offer a clear and safe solution. In designing variable annuity products, there could be two components, one fixed and one variable. The fixed component will give a minimum pension and the variable component will give pension based on the last 3/6 month performance of stock markets. LIC is already having many superannuation products where minimum interest rates are guaranteed. Hence deciding the fixed component will be difficult. Let LIC be the pioneer in this field also.

Like pension, health insurance also is going to be in great demand as cost of medical treatments including medical tests are subject to huge price inflation. Many banks / financial institutions and many public sector undertakings are offering group medical benefits for their employees. This is an area where one need not lock the premium for a longer period, in fact on the basis of burning cost method' and by combining appropriate investment strategy, one can offer an affordable health insurance cover on group basis with many benefits. At the same time the insurance company does not take inappropriate risks. LIC is positively having enough expertise in this area. It needs to explore this.

10. In any financial institution risk management is central piece. LIC must use robust risk management practices and start preparing economic capital report. Economic capital is the capital required for various types of risks it has in its operations. This will clearly portray the advantages and any incipient risks it has. On this basis, LIC can also prepare 'consolidated risk index' (CRT). Whenever there is an increase in this index, this will clearly show the cost of this risk on capital and on

income. Down the line, the IRDA has to move towards 'risk based supervision'. The consolidated risk index is central to RBS. CRI would also help LIC in deciding the business strategy. This would give a clear view about risk-return profile.

11. Whether it is product design, or consumer preference for any particular product, investment strategy, risk mapping, etc., all the above are possible once LIC is having a strong in-house research department. It is very surprising to note that LIC is not have any research wing so far. **It is a high time LIC works towards this.** In addition to in-house research, LIC can also select various research / educational institutions and create dedicated chairs. These research chairs could be asked to work on any research issues which LIC want. By creating chairs in different parts of the country, it can pool the talents and use them for LIC's advantage. One of the strong base of RBI / SBI today is their research strength. This has put SBI / RBI in an enviable position as compared with other organization. In India insurance research is in nascent position. There is a wide scope for initiating this and there is no doubt LIC would reap very good benefits.

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