Insurance – Growth Nexus:
An Overview in context of SAARC Countries

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Preamble

Insurance is a form of risk management through which risk of an uncertain loss is hedged. It is considered a key pillar of financial services sector and a vital function of entrepreneurial activity that contributes towards the socio-economic development of any country. From a macro-economic perspective, insurance plays a diversified role in promoting trade and commerce, infrastructure development, mobilization of savings, capital formation leading to improvement in investment climate and quality of lives of people.

Research has proved that any country's level of development and economic growth has a positive correlation with the insurance coverage. This can be gauged from the fact that the industrialized nations with well developed financial sector, especially insurance services, is contributing over 85 percent in the global insurance market as compared to just 15 percent share of emerging or developing nations.

The Research and Publications Directorate of ICMA Pakistan, while undertaking literature review on the subject of correlation between financial sector development and economic growth, observed that majority of the research studies all around the world have been conducted on exploring the role of 'banking sector' and 'stock market' – *the two major components of financial market* – on the GDP growth. Very little theoretical and empirical research was found on exploring how the insurance services sector impact, positively or negatively, towards the growth and development of any economy.

Hence, it was thought prudent that a brief exploratory research be carried out to explore the nexus between insurance sector and GDP growth in the context of SAARC countries which would be useful for the policy makers and governments in these countries to frame policies accordingly to promote and strengthen this important component of financial market, which has recently showed remarkable growth, especially in the Asian region. This would also provide a base for further research on this subject. It is hoped that this paper would fill a gap in the current insurance-growth nexus literature.

Before we proceed further, let us first have a quick look at few insurance terminologies which would help understand how insurance plays a contributory role towards the economy and GDP growth.

Insurance Penetration

Insurance penetration rate is defined as the level of development of insurance sector in any country. It is measured as a ratio of gross premium underwritten in a specific year to Gross Domestic Product (GDP). Insurance penetration is also sometimes called 'insurance spending' representing relative importance of the insurance sector in the domestic economy. The level of insurance penetration depends on many factors such as level of economic development, savings in financial instruments and size and reach of insurance.

The insurance penetration rate can be classified into life insurance penetration and non-life insurance penetration. Life insurance penetration considers premiums from life insurance policies as percentage of GDP whereas Non-life insurance penetration considers premiums from other than life insurance policies such as health, fire, marine, auto insurance etc.

Table 1: Insurance Penetration in SAARC Countries (Ratio of Gross Premium to GDP)

Sr.	Country	Insurance Penetration (%)
1	Bangladesh	0.64
2	India	3.30
3	Nepal	1.53
4	Pakistan	0.80
5	Sri Lanka	1.20

Source: Websites of relevant Insurance Regulators

Insurance Density

Insurance Density is defined as per capita premium or premium per person in any country. It is measured in terms of US Dollars as an average value of the insurance premium paid by a person in a specific year.

Table 2: Insurance Density in SAARC Countries (Ratio of Insurance Premium to Population)

Sr.	Country	Insurance Density (USD)
1	Bangladesh	06
2	India	56
3	Nepal	11
4	Pakistan	09
5	Sri Lanka	40

Source: Websites of relevant Insurance Regulators

Cross-Border Expansion of Insurance Services

With the increasing globalization and liberalization of economies, the insurance services have also expanded across the border and multi-national insurance companies are making huge profits through economies of scales and by offering specialized insurance products. Many of these companies have expanded through mergers and acquisitions and managing multiple companies in several countries. They are also take full advantage of globalization, technological advancement and investment incentives offered by other countries. Let' have a look at the top ranking ten insurance companies who have achieved highest profit during the year 2015.

As can be seen from the above table 3, all the top 10 ranking companies are from advanced and emerging nations, with none of them representing the SAARC region. This indicates that due to low penetration rate within the domestic market and lack of capacity and potential for growth, the insurance companies in SAARC countries are not in a position to expand their services across the boundaries.

The SAARC Chamber of Commerce and Industry and insurance regulators in the SAARC countries should, therefore, devise policies and common strategies to form alliances of regional leading insurance companies to compete for the top ranking positions globally in terms of revenue.

Insurance Sector Profile of SAARC region

The countries in the SAARC region have huge potential and resources, encompassing around 3 percent of the world's total geographical area and 21 percent of total world population. The region makes up around 9.12 percent of the global economy with combined foreign exchange reserves at over US$ 400 billion as of 2015. The combined economy of SAARC countries is the third largest in the world in terms of GDP (PPP) after the US and China, and fifth largest in terms of nominal GDP. There is ample proof, supported by research and experts opinions of global economists, that the South Asian region is today one of the fastest growing regions in the world, contributing around 2% of world trade and 1.7% of world FDI.

As far as Insurance is concerned, we find that SAARC region is marked with low insurance penetration with a large portion of poor population not getting the insurance services, including life insurance. The region is also facing issues of climatic changes, droughts, famines and diseases which effect the general population in a big way. This necessitates expansion in insurance sector to mitigate the negative effects of such catastrophes. The insurance sector in SAARC has to play a more proactive role in this regard.

Table 3: Top Insurance Companies in the World by Revenue (2015)

Ranking	Insurance Company	Country	Total Revenue (In Billion USD)
1	Berkshire Hathaway	USA	194.7
2	AXA	France	161.2
3	Allianz	Germany	136.8
4	Japan Post Holdings	Japan	129.7
5	Assicurazioni Generali	Italy	118.9
6	Prudential plc	U.K	99.0
7	China Life Insurance	China	87.2
8	Ping An	China	86.0
9	Legal & General Group	U.K	84.8
10	Munich Reinsurance	Germany	81.7

Source: Websites of relevant Insurance Regulators

Table 4: Size of General and Life Insurance Companies in SAARC Countries

Sr.	Country	General (Non-life) Insurance	Life Insurance	Combined Life/ Non-Life Insurance	Total
1	Bangladesh	41	31	—	72
2	India	29	24	—	53
3	Nepal	17	08	02	27
4	Pakistan	38	07	—	45
5	Sri Lanka	15	12	03	30
		140	**82**	**05**	**227**

Source: R&P Directorate, ICMA Pakistan Research

ICMA Pakistan's research indicates that around 227 insurance companies both in non-life (general) and life insurance business are operating in SAARC countries, out of which 140 are in non-life and 82 in life insurance (Table-4). Bangladesh stands at top with 72 insurance companies, followed by India with 53 and Pakistan with 45 companies. Sri Lanka and Nepal ranks 4th and 5th with 30 and 27 insurance companies.

Bangladesh

The Insurance industry in Bangladesh was nationalized in 1972 and two state-owned organization viz. Sadharan Bima Corporation (SBC) and Jiban Bima Corporation (JBC) were established under the Insurance Corporation Act, 1973 to deal with non-life and life insurance business, respectively. Later, the private insurance companies were also given permission to operate under provisions of Insurance (Amendment) Ordinance, 1984. Initially, the Ministry of Commerce was the regulator of Insurance sector; however the supervisory role was subsequently shifted to the Ministry of Finance of Bangladesh. In 2010, two new laws namely the Insurance Act, 2010 and the Insurance Development Regulatory Authority Act, 2010 were passed by the Bangladeshi Parliament. These laws became effective from 18th March 2010. In 2013, the Asian Reinsurance Corporation Act has been implemented in accordance with Insurance Corporation Act 1973 for setting up the state-owned insurance institutions.

The Bangladesh market is saturated with dozens of insurance companies, highest in the SAARC region. It is ranked 76th in the world with just 0.02% share in the global insurance business. The Insurance penetration rate (premium as a % of GDP) is continuously declining since 2010 i.e. 1.02% in 2011; 0.95% in 2012; 0.85% in 2013; 0.70% in 2014 and 0.64% in 2015. Less than one percent of Bangladesh's population is insured, which shows huge potential for growth of insurance business.

India

The Insurance industry in India was nationalized in January 1973 with the passing of General Insurance Business (Nationalization) Act, 1972, which led to establishment of four state-owned insurance companies viz. National Insurance Co. Ltd.; New India Assurance Co. Ltd.; Oriental Insurance Co. Ltd.; and United India Insurance Co. Ltd. The General Insurance Corporation of India was incorporated as a company in 1971 and started business in January 1973. In 1999, the Insurance Regulatory and Development Authority (IRDA) was formed as an autonomous body to regulate and develop the insurance industry.

India stands as 15th largest insurance market in terms of volume of premium and accounting for less than 1.5% of global total insurance premiums and 2% of global life insurance premiums. Coupled with banking sector, insurance business contributes to the tune of 7 percent to India's GDP. The Insurance penetration rate in India is currently 3.30 percent which is below the world average of just over 6 percent.

The life insurance sector of India is one of the biggest in the world, with recorded premium income of US$ 20.54 billion during period from April 2015 to March 2016, showing growth rate of 22.5 percent. The General Insurance business recorded premium growth of 12 percent with US$ 1.55 billion in same period. The private insurance companies contribute around 50.2% in total non-life insurance revenue whereas the public companies have share of 49.8% by September 2015.

Sri Lanka

During 1961 to 1964, both general and life insurance in Sri Lanka were nationalized by amalgamating over 50 foreign based companies and 2 local companies. The Insurance Board of Sri Lanka (IBSL) is the regulatory body in Sri Lanka which is responsible for the development and supervision of the insurance industry. The Regulation of Insurance Industry Act, No. 43 of 2000 provides the legal framework for the regulation and supervision of insurance companies in Sri Lanka. This Act has been amended twice in 2007 and 2011.

The recent amendments in the Insurance laws requires all composite insurance companies to segregate their business into two separate companies on or before February 2015 and obtain a listing on the stock exchange before February 2016. The Board is also in process of introducing a 'Risk based Capital Rules' for insurance companies which would replace the current Solvency Margin Rules to be applicable from 2016.

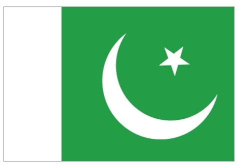
The insurance business in Sri Lanka has been expanding steadily with life and non-life insurance business showing growth of 20% and 15%, respectively in 2015. Insurance penetration in Sri Lanka is still at a lower level than many other countries in Asian region, which indicates untapped potential for insurers to expand their businesses by offering insurance products. In 2015, penetration ratios of long term (life) and general insurance businesses were recorded at 0.48% and 0.62% respectively.

Nepal

The insurance needs of Nepal during 1940s were mostly catered by the Indian insurance companies. In 1947, the Nepal Bank Ltd. formed the 'Nepal Insurance and Transport Company (now Nepal Insurance Co.) as its subsidiary company. From 1947 to 1991, two insurance companies, one life and the other non-life, were established in Nepal with 100% Indian investment. In 1992, the Insurance Act was promulgated and an Insurance Board was formed under which 20 new insurance companies were set up in Nepal. The life insurance business was started with the establishment of Rastriya Beema Sansthan in 1972. Beema Samiti is the Insurance Regulatory Authority of Nepal and operates under the Ministry of Finance. The Board regulates and supervises the insurance sector under the Insurance Act of 1992.

The share of insurance sector in overall financial system of Nepal is 3.5 percent. The insurance market in Nepal has been expanding at the rate of 15 percent annually. The Insurance premium collection by Nepal's life and non-life insurance companies has crossed over NRs 100 billion mark. Life insurance accounts for 87 percent of the gross insurance premiums. The insurance penetration is 1.53%, second highest after India, whereas the Insurance density is US$ 11.

Pakistan



In 1947, at independence, there were five domestic and 77 foreign companies operating in the insurance sector. In 1948, the government established an 'Insurance Department' within the domain of the Ministry of Commerce, headed by the Controller of Insurance, with the objective to supervise the insurance industry and to safeguard the interests of insured. In 1952, Pakistan Insurance Company (PIC) was established to promote new insurance companies and provide reinsurance facilities to the insurance industry. In 1955, a National Co-Insurance Scheme (NSC) was initiated by the government to promote insurance culture. In 1973, State Life Insurance Corporation (SLIC) was established as a public sector entity to promote the life insurance sector. Later, in 1976 National Insurance Company (NIC) was established to promote the non-life insurance business. Subsequently, in 1992, the government opened the life insurance sector to the private sector. At present, both life and non-life insurance companies are permitted to be incorporate with 100% foreign ownership. The business of insurance in Pakistan has been regulated under the Insurance Act, 1938.

There were major changes in insurance regulation in the year 2000. An Insurance Ordinance, 2000 was promulgated by the government and the responsibility of insurance regulation was shifted from the Ministry of Commerce to the Securities and Exchange Commission of Pakistan (SECP) since January 2001. The Insurance Division in SECP now regulates the insurance industry and is responsible for implementing the insurance law under powers vested in the Insurance Ordinance, 2000 and Companies Ordinance, 1984.

The Insurance penetration rate in Pakistan is one of the lowest in SAARC region i.e. 0.80% which is comparatively lower than India, Nepal and Sri Lanka. Similarly, the insurance density of USD is also the second lowest in the SAARC countries, with only Bangladesh at the last with USD 6.

Nexus between Insurance and Growth

It was way back in 1964 when during the first conference of UNCTAD it was realized that "a sound national insurance and reinsurance market is an essential characteristic of economic growth'. Similarly, in all the text books relating to insurance, majority of the authors indicated that insurance has an overall positive impact on the economy through risk transfer and indemnification and it also promotes financial intermediation. Many research studies conducted by authors have concluded that a better developed financial market or system leads to a stable and sustained economic growth through improvement in total factor productivity.

Research also establishes the fact that insurance market activity and economic growth has a casual relationship, with both life and non-life insurance having a positive and salutary effect on economic growth of any country. The benefits of non-life insurance are derived by both the developed and emerging countries, whereas benefits of life insurance are derived by only high-income countries. This is because life insurance is a smaller part of the total insurance market in low income countries.

The insurance sector has an integral association with the macro-economic components of any country and as such any development in this sector has a positive impact on overall economic growth. For instance, insurance is linked to commerce and infrastructure and as such it plays a key supporting role in all economic activities such as exports and imports, manufacturing, services, shipping, aviation, foreign exchange, privatization, savings and investments. Insurance lowers the overall risk faced by the economy.

How Insurance Stimulates Growth and Development?

Financial development is a key driver of economic growth and Insurance business is now being considered as an integral part of the financial development. Hence, insurance indirectly stimulates economic growth. Secondly, there is an established strong link between insurance sector and other sectors of the economy and therefore insurances leads to long term economic growth.

Evidence and statistics are pointing towards the fact that the share of insurance services in aggregate financial sector is persistently increasing in both developed and developing countries. Statistics also prove that economic growth is much higher in developed countries where the weightage of insurance in GDP is more than ten percent. Now let's see how insurance stimulates growth and development:

Role in Capital Formation and Investment

The scattered domestic savings in a country are collected and mobilized by insurance companies in shape of 'premiums' which are then invested as 'capital' on a long term basis in development projects, in addition to providing protection of such projects from various types of risks involved such as fire, natural calamities, disasters etc. Hence, Insurance provides an important source of funds for capital investment.

Role in Facilitating Commercial Transactions

Through indemnification and risk pooling as well as mitigating business losses by provision of credits, the insurance business facilitates commercial transactions. These unique attributes of insurance provides confidence to risk-averse entrepreneurs and individuals to undertake high risk and invest in commercial transactions, which eventually leads to higher productivity and growth in the economy.

Role in Improving Investment Climate

Insurance helps improve the domestic investment climate through provision of risk management instruments that attract long term funds and investment from foreign entrepreneurs. In fact, insurance not only attracts but also channelizes long term funds towards productive sectors of the economy. The growth in insurance premiums eventually translates into higher investments in other key sector of economy and promotes a more efficient mix of activities.

Role in Creating Employment Opportunities

Insurance business provides employment opportunities for a range of associated professionals such as insurance brokers, advisors, underwriters, claim managers and actuaries. Hence, insurance leads to creation of both direct and indirect employment in the economy. The expansion of insurance business has increased demand for highly skilled and semi-skilled human resource, especially in emerging economies.

Supplementary Roles of Insurance

Insurance business has other supplementary roles towards growth and development of economy such as:

1. It enhances financial stability of companies and individuals
2. It encourages market competitiveness
3. It facilitates trade and industry
4. It promotes financial intermediation
5. It facilitates in efficient capital allocations
6. It enhances internal cash flow though payment of premiums
7. It increases total productivity of factors of production
8. It complements or substitutes government security programs
9. It stimulates growth through investments in stock, bond and real estate markets
10. It increases social stability through improvement in quality of lives of people

Conclusion

There has been scarce empirical research to provide evidence on the positive impact of insurance on economic growth. The paper provides some theoretical justification for establishing a casual nexus and co-relation between insurance development and economic growth and vice versa. The insurance sector has an integral association with macro-economic scenario and lead to improvement in overall economic growth.

The SAARC countries have many things in common for which common strategies are required. Almost all the SAARC nations are faced with poverty, natural calamities in shape of floods and earthquakes, agrarian and service based economies. Similarly, all SAARC countries have low insurance penetration and density which indicates huge potential for expansion of insurance services to the poor segments of the society.

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