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Synergy Analysis and Risk Management of Unit Linked Insurance Plan in India

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Abstract – Insurance companies are in the business of taking risks of various kinds. All over the world, the insurance companies write the policies that deal with specific risks, and in many cases even underwrite exotic risks. As a direct corollary, therefore insurance companies should be good at managing their own risks. However the reality is little far from that. While these companies are good at assessing insurance risks for its policy holders, but not very good at setting up structures internally for managing their own operating and business risks. Over the past years Unit Linked Insurance Plans (ULIP) had emerged as a major player in savings mobilization. Investors had showed keen interest by subscribing to ULIP schemes anticipating higher returns. However with the global recessionary trend the performance of ULIP had been drastically affected. The BSE Sensex which had shot up to 21000 points came crashing down and stood at 8335 points on12th March 2009 and had greatly affected the Net Asset Value (NAV) across all the plans of various companies.

This research paper elaborates the concept and proceeds to explain risk identification, distinguishes risk management in life insurance Unit Linked insurance Plans and details the risk management process. It also explains the risk management system and structure within the organization as per the IRDA Guidelines. Finally it forays on the vital issues and strategies relevant to the insurer, the policy holder and the IRDA as regulatory authority.

Key Words: Risk Identification; Risk Assessment; Unit-linked Insurance Plan: IRDA

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INTRODUCTION

Insurance is a means of protection from financial loss. It is a form of risk management, primarily used to hedge against the risk of a contingent or uncertain loss. An entity which provides insurance is known as an insurer, insurance company, insurance carrier or underwriter.

Life is a roller coaster ride and is full of twists and turns. You cannot take anything for granted in life. Insurance policies are a safeguard against the uncertainties of life. Insurance is system by which the losses suffered by a few are spread over many, exposed to similar risks. Insurance is a protection against financial loss arising on the happening of an unexpected event. Insurance policy helps in not only mitigating risks but also provides a financial cushion against adv erse financial burdens suffered. Insurance policies cover the risk of life as well as other assets and valuables such as home, automobiles, jewelry etc. On the basis of the risk they cover, insurance policies can be classified into two categories.

- Life Insurance
- General Insurance

1.1 Life Insurance

Life insurance is a written contract between the insured and the insurer, which provides for the payment of the insured sum on the date of the maturity of the contract or on the unfortunate death of the insured, whichever occurs earlier.

Types of Insurance policies

- Endowment Policy
- Whole Life Policy
- Term Life Policy

Money-back Policy

- Joint Life Policy

- Group Insurance Policy
- Loan Cover Term Assurance Policy
- Pension Plan or Annuities
- Unit Linked Insurance Plan

Unit Linked Insurance Plan (ULIP) is one single solution for insurance as well as for investment. It is considered to be a hybrid instrument comprising the features of a life insurance policy and a mutual fund. A unit linked insurance plan (ULIP) is a type of life insurance where the cash value of a policy varies. The cash value depends on the current net asset value (nav) of the underlying investment assets.

It allows protection and flexibility in investment, which are not present in other types of life insurance such as whole life policies. ULIP came into picture around 1960s and became very popular in the world due to its lucrative features. In 1971 the Unit Trust of India offered the first ULIP policy in which a small part of premium was utilized for providing life cover and balance was invested in units. With new developments in the insurance policy, finally the plans which provided the dual benefit of „sum assured" plus the „fund value", in the event of an unforeseen occurrence became popular. The Unit Linked Insurance Plans involves risks of investors" money because the investments are channelized in capital market and that is why the return is not guaranteed. As we are aware that insurance is a way to manage risk whereas ULIP are not risk free investments, so a dilemma arises whether to avoid risk or to accept risk. In this perspective, the study compares the Traditional policies with U-lip policies catered by the Life Insurance Companies in India in this era of globalization.

NEED OF STUDY

The last few years have been a watershed for assured return plans. As the insurance sector has developed, there's been a growing acceptance by most policyholders that the assured return era is a thing of the past. The private insurance companies are focusing on the Market Linked Plans. This study undertaken for Life Insurance Companies dealing with Unit-Linked Insurance Plans with the objects to analyze the risk which involved in Market linked insurance plan and to analyze the performance of their funds. This study would help in explaining Market risk and returns which create awareness about the Market linked product among the investors through which the company gets more investment. All this would help in giving suggestions to Life Insurance Companies offering unit linked insurance policies in strengthening their marketing efforts, in tapping private insurance companies" schemes and expand their business.

LITERATURE REVIEW

Stefan Engelander and Joachim Kolschbach (2006) felt that especially in life insurance, but also in the case of some traditionally styled mutual companies, risks (as well as chances) remaining after use of the pool approach (especially risks of long-term changes of circumstances which cumulatively affect all risks in the pool) are re-transferred to policyholders by a refund of premiums not required. Such performance-linked features have a significant role in insurance business. In many jurisdictions, insurance contracts grant insurers a significant discretion in determining policyholders' benefits, especially in the case of surrender or participation benefits, while in others, any contractual benefit is subject to strict contractual provisions. The complexity of the benefit trigger, the insured event, often means that there is a significant lapse of time between occurrence of the insured event and the actual settlement of the claim. The knowledge of the specific situation of the individual contract, lost after outset of the contract, is after the coverage period regained step by step during the settlement process. Insurers might have some influence with regard to the speed of the settlement process, reducing liquidity risks. Traditionally, the relationship between policyholders and insurers is significantly shaped by a reciprocal trust, where policyholders' economic existence often relies on the claims payment ability of the insurer in the long run, while insurers depend on the honesty of policyholders, and a long-term relationship, to underpin the pool.

Nair, K.K. (2009), conducted a study on Unit Linked insurance plans (ULIP) based on secondary data available on its emergence, concepts, parameters, benefit, current position and future outlook. The study suggested that India has a plethora of opportunities for insurance companies because three-fourth of the population was uninsured also majority of the investing population were small and medium investors and majority of the investors lacked the expertise to directly enter the stock market and earn good returns. The Study emphasized the about facts to be the reasons for increased importance of ULIP. The study observed that ULIP will continue to be a good investment option for the investors as it combines the multi aspects of insurance, investment and tax benefit.

Akula, R. and Kanchu, T.,(2011), conducted a study on growth of ULIP Policies in life insurance sector of India by comparing traditional (Life Fund + Pension & General Annuity + Group Fund) and ULIP Policies. The objective of the study was to observe the evolution of ULIPs in India, the growth of ULIPs over traditional Policies, risk factors involved in ULIPs over traditional policies and to suggest various measures to develop and stabilize the growth of ULIPs. The period from 2007 to 2009 was covered in the study. The study considered 5 companies to compare growth, namely, LICI, HDFC Standard Life, ICICI Prudential Life, SBI Life and Bazaz Allianz Life. It was revealed from the study that there was remarkable growth in ULIP compared to traditional policies as the new private entrants targeted ULIPs for market penetration.

Venugopalan, K., V.(2011), conducted a study on global financial crisis and Life insurance sector in India by undertaking a comparative study of LIC with Private Sector. The impact of the Global Financial Crisis of 2007 to the Indian Life Insurance Sector is measured by using the following variables insurance penetration, insurance density, number of insurance policies issued, number of insurance premiums collected, total premium collected, profit obtained. The period covered in the study was from 2004-05 to 2010-11. The study suggested insurance sector to be an emerging and untapped sector in our country.

Udayan Samajpati (2012) enhanced the performance evaluation of ULIPs is carried out through Risk-Return Analysis, Treynor's Ratio, Sharpe's Ratio and Jensen's Measures. The schemes selected for study were ICICI Life Stage RP-Maxi miser (Growth) Fund, Bajaj Allianz New Family Gain-Equity Index Fund II and ING High Life Plus-Growth Fund. The results of performance measures suggested that all the three ULIPs schemes have outperformed the market. Among the three schemes ING Vysya ULIP was best performer.

OBJECTIVES OF STUDY:

The main objective of the study is to examine the marketing of ULIP policies and the growth in the Unit Linked Insurance Plans over traditional policies. For this, the study is aimed at achieving the following objectives.

1. To study the evolution of ULIPs in India.

2. To study the growth of ULIPs over Traditional Policies.

3. To study the risk factors involved in the ULIPs over Traditional Policies.

4. To suggest various measures for considerations to develop and stabilize the growth of growth of ULIP policies to achieve the long term success to the organizations.

RESEARCH METHODOLOGY

The present study has been conducted on the basis of secondary data and is descriptive in its nature. The required secondary data for the study was collected through different websites, annual reports, magazines and company reports. The researcher selected five leading Life insurance companies (ICICI Prudential Life Limited, Reliance Life Limited, SBI Life Limited, Met life Limited and Bajaj Allianz Life Limited) for the study.

DATA ANALYSIS AND INTERPRETATION

1. Evolution of Unit Linked Insurance Plans

Unit linked insurance plan (ULIP) is life insurance solution that provides for the benefits of risk

Protection and flexibility in investment. The investment is denoted as units and is represented by the value that it has attained called as Net Asset Value (NAV). The policy value at any time varies according to the value of the underlying assets at the time.

The returns in a ULIP depend upon the performance of the fund in the capital market. ULIP investors have the option of investing across various schemes, i.e., diversified equity funds, balanced funds, debt funds etc. It is important to remember that in a ULIP, the investment risk is generally borne by the investor

2. Fund wise growth of investments of ULIPs over Traditional Policies

The entry of private sector made the life insurance sector a competitive one. To overcome the competition, the private life insurance companies mainly targeted with ULIP policies over traditional policies. The growth of ULIP funds increased at a great speed especially during the period between 2016- to 2018.

3. Benefits and Return Approach

Life insurance policies are valuable assets to mitigate the financial risk o untimely death. A buyer has to choose a policy which best suits to his needs. These include:

- Need protection for entire life or for a specified period
- Adequacy of insurance protection
- Specific sums of money for meeting planed expenses
- Premium Price.

Nowadays, many companies are merging traditional policies with ULIPs which provides both the benefits of life insurance and greater margin on investments which are paid. As such, every individual facing such a financial risk who can afford to pay for such a protection must seriously consider purchasing some life insurance. The differences in policies occur due to:

- Inherent complexity due to uncertainty and long time horizons.
- The need to compare a plethora of different types of products from competing insurance companies.
- Most insurance policies bundle pure insurance with savings to offer composite products.

4. Risk factor in ULIP:

The investment risk is related to the stock market. The NAVs of the units go up and down depending on the fund's performance and the factors affecting the Capital market. The ULIP are subject to following charges:

a. Premium allocation charge

b. Mortality Charges

c. Fund Management Charges

d. Policy Administration Charges

e. Surrender Charges

f. Fund Switching Charges

Unit Linked insurance plan provides the combination of insurance with investments. It has the double benefit of providing a RISK cover & investing in stock markets.

FINDINGS OF RESEARCH

Performance of ULIP Products over three years

1. The SBI Life Smart has improved over 2 years period from its inception as the market conditions and economy have improved over these years globally. The rate of return on the investment is 3.71% much lower than the fixed deposits a safest investment option.

2. Since the inception in the year 2011 ICICI life insurance product has shown an overall improvement with very poor returns in the initial year of its inception. The rate of return on the product is 6.48% which is much lower than the return on the fixed deposits.

3. The Bajaj alliance wealth insurance has shown good performance in 2013 in January month but it has decreased its performance in February 2013. The rate of return on the investment is 1.13% which is much lower than the fixed deposits a safest investment option.

4. The PNB Met Smart has improved over 2 years period from its inception as the market conditions and economy have improved over these years globally. The rate of return on the investment is 25.30% much higher than the fixed deposits a safest investment options.

5. The reliance wealth plus health basic plan has improved over 2 years period from its inception as the market conditions and economy has improved over these years globally. The rate of return on the investment is 19.16% much higher than the fixed deposits a safest investment options.

6. The MetLife provides good returns to investors compared to other products. Reliance life insurance is ranked second. The reasons for good returns may be because of the better portfolio of investment opted by MetLife and Reliance, which needs to be further analyzed.

SUGGESTIONS

The following suggestions will help the companies to increase the growth of the ULIP policies further in the current scenario.

1. The IRDA must carefully study the performance of each ULIP policy of the life insurance companies in order to provide fair justice to the policyholders.

2. The companies must provide guaranteed benefit through ULIP to increase its present sales.

3. The companies while allocating the fund in the market must carefully study the fluctuations and projections before investing the amount. Such practices will benefit the ultimate receivers, i.e., policyholders

4. The performance of ULIP policies for the current period is very gloomy. Due to the recession, there will be vulnerability in growth rate. Hence, the companies must re assess the performance of ULIP policies and must introduce the ULIP policies that are to be tailor made to the needs of the customers.

5. Integration of ULIP and Traditional plan is a latest strategy adopted by the present life insurance companies. But, the companies must assure that actual performance should not be deviated with expectations. The companies must also monitor the performance of policies and must ensure

its marketers are making fair justice to the policy holders. Because, any mismatch of expectation or forceful selling of ULIP policy or traditional policy will lead to lapsation, which harms the company, marketers and ultimately policyholders also.

CONCLUSIONS

The introduction of Unit Linked Insurance Plan (ULIP) is a historic achievement in the life insurance services. The ULIP policy right from its introduction in the market achieved staggering growth in a limited period of time. Many life insurance companies' especially private life insurance companies are showing huge growth in the ULIP policies over traditional plans. From the period 2007 all the companies including LIC achieved maximum growth in the ULIP policies over traditional policies. ULIP policies are different to traditional policies as the investment of policyholders fund is not done in the traditional policies where as in ULIPs the investments are done by allocating a certain limit of percentage of policyholders fund in the market. Comparing to traditional policies, the ULIP policies have risk factors. The policyholders can expect good returns from the ULIP over traditional policies but the market performance is highly influencing the ULIP performance. Policyholders prefer ULIP policy for long term returns.

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