Insurance Protection Gap in India:
A Need for Public-Private Partnership

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Introduction

In the last couple of years, India's insurance penetration and density has increased due to Government's commitment & efforts to include the vulnerable sections under the protection plans. However, the real problem is that the protection gap (the gap between economic loss and insured loss) is significant. For instance, during 1991-2021 around 8% of the total losses are covered through any type of insurance, so there is around 92% protection gap in India. So, an early intervention is needed to close the protection gap, which are in all lines (life & non-life) of insurance. With the rise in economic losses due to disasters, India should go for a public-private solution, say a Disaster Pool, for natural disaster risk involving the insurance sector could offer many benefits over government crisis loans and grants.

Background of the Insurance Protection Issue

The understanding of risk has undergone significant evolution since the global financial crisis 2008. Previously, risk meant management's focus was on deviation from expected values or outcomes, while tail events were considered as anomalies. However, in the last two decades, tail events that were expected to happen once in 1000 years or so, are now occurring with increased frequency / amazing alacrity with each such event setting new records of economic stress. These events in statistical parlance are commonly called fat-tail events and India is no exception to the alarming phenomenon. India, in fact, is one of the most disaster-prone countries in the world. The locational and geographical features render it vulnerable to several natural hazards.

Though, the insurance penetration (premiums to GDP) in India has increased from 2.71% in FY01 to 4.20% in FY21. However, the real problem is that the protection gap (the gap between economic loss and insured loss) in India is significant. Further, it seems that the lack of awareness about the ideal adequate life insurance cover for an individual increases the mortality protection gap. In the rest of the article, we will be discussed about the protection gap and ways to meet the uncertain risk arises mainly due to the natural disasters in India.

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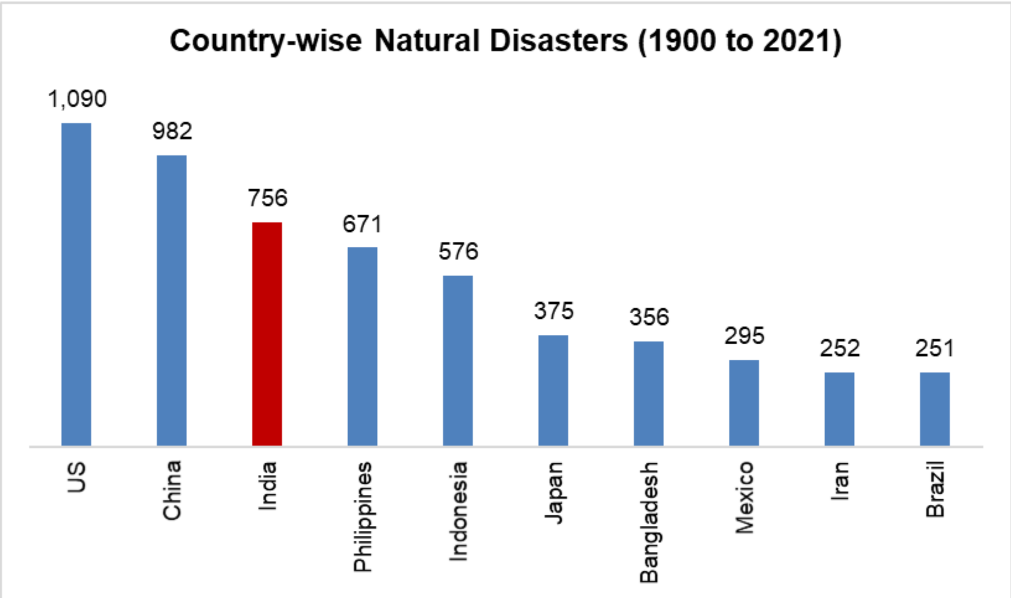
Growing Disaster Risks: A Major Strain on Government Budgets

A natural disaster is an event of nature that causes sudden disruption to the normal life of a society and causes damage to property and lives, to such an extent that normal social and economic mechanisms available to the society are inadequate to restore normalcy. Viewed in this manner, a host of natural phenomena constitute disasters to a society, whether they are related to an occurrence in microenvironment or not. In macro terms, the disasters, which cause widespread damage and disruption in India, are drought, flood, cyclone, and earthquakes. India is one of the most disaster-prone countries in the world. The locational and geographical features render it vulnerable to several natural hazards.

Graph 1



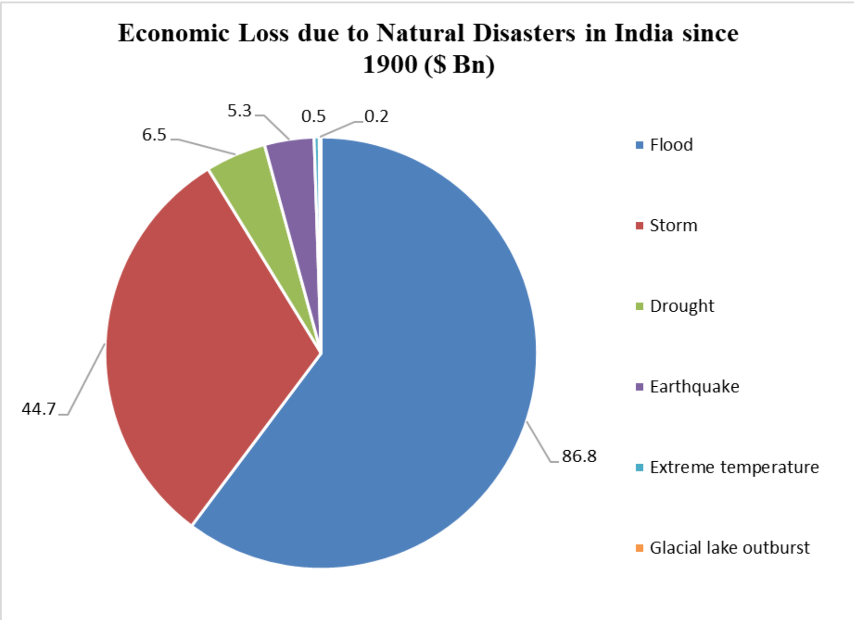
Source: EM-DAT Database

India has been ranked at 3rd position, after US and China (Graph 1) in recording the highest number of natural disasters since 1900. India recorded 756 instances of natural disasters (Landslide, Storm, Earthquake, Flood, Drought, etc.) since 1900 with 402 events occurring during 1900-2000 and 354 during 2001-2021, indicating the preponderance of tail events at an alarming frequency and each such events setting new records of economic stress. These events in statistical parlance are commonly called fat-tail events. Since 2001, a total of 1 billion people has been impacted and almost 83,000 people died due to these disasters since 2001 (Refer Table 1).

Table 1: Natural Disasters in India			
Year	Occurrences	Deaths	Total Number of People Affected (in Mn)
1900-2000	**402**	**90,50,599**	**1474**
2001	22	21045	27
2005	31	4997	29
2010	18	1344	04
2015	22	3400	347
2020	11	2316	20
2021	17	1860	4
2001-2021	**354**	**82747**	**1006**
Total (1900-2021)	**756**	**91,33,346**	**2480**
Source: EM-DAT; SBI Research			

By disaster type, India is marred mostly with floods. Almost 41% of disasters occurred in the form of floods followed by storms. Apart from human losses, there is huge economic loss due to these disasters. Since 1900, India has suffered an economic loss of $144 billion (where the loss is reported) with largest loss from floods ($86.8 billion) followed by storms ($44.7 billion) (Refer Graph 2). If these losses are adjusted with current prices the losses come out to be around $187 billion. Still there is huge gap in reporting of losses (loss data of only 193 events available out of 756 for India) and there are problems in existing estimation methodologies also.

Graph 2



Source: EM-DAT Database

Reducing Protection Gap in the Hinterland

The occurrence of catastrophic events, largely floods, in the last few years has seen huge losses to property, in particular, to dwellings and small business. The protection gap stands out, both in terms of property not being insured and those not being adequately insured. Further, the 2020 and 2021 will be remembered for the global health and economic crisis triggered by COVID-19. The global catastrophe protection gap (difference between economic and insured losses) is USD 113 billion in 2020. In otherwards, it is the financial loss generated by catastrophes not covered by insurance. In 2020, the global protection gap was around USD 113 billion, up from 87 in 2019, but down from the previous 10-year average of USD 143 billion (Refer Table 2).

Table 2: Global Catastrophe Protection Gap (in USD Bn)				
		2020	2019	10 Year Average
Economic Losses	A	202	150	222
% of Global GDP		0.24	-	0.26
Insured Losses	B	89	63	79
Global Protection Gap	C=A-B	113	87	143
Source: SBI Research, Swiss Re				

In several countries (in table 3), insurance programmes or pools have been established, usually with the support of the public sector/Government, to provide insurance coverage for certain risks and/or for certain segments of the population. In many cases, these programmes have been established to provide affordable insurance coverage for risks that have been deemed uninsurable through private insurance markets – although in others, the programmes have been established to promote solidarity in terms of loss-sharing across regions. Among all the countries, France has had a nationwide insurance scheme since 1989. From 2016, insured losses have exceeded EUR 550 million each year, with the average annual loss standing at EUR 810 million, compared with an average annual loss of EUR 310 million in 2000–2015.

Table 3: Catastrophe Risk Insurance Programmes: Cross Country				
Country	**Programme**	**Risks covered**	**Type of insurance**	**Public sector involvement**
Australia	Australian Reinsurance Pool Corporation	Terrorism	Reinsurance	ARPC is a government enterprise Backstop for losses above ARPC capacity and up to AUD 10 billion

	(ARPC)			
Belgium	Terrorism Reinsurance and Insurance Pool	Terrorism	Co-insurance/ Reinsurance	Backstop for losses above TRIP capacity and up to EUR 300 million
France	Caisse centrale de réassurance (CCR)	Flood, earthquake, tsunami, landslide, mudslide, avlanche, subsience and cyclonic winds; terrorism	Reinsurance	CCR is a government entity backed by an unlimited government guarantee
Germany	Extremus	Terrorism	Direct insurance	Backstop for losses above Extremus capacity and up to EUR 6.48 billion
Japan	Japan Earthquake Reinsurance (JER)	Earthquake, volcanic eruptions, tsunami	Reinsurance	Losses above a certain threshold are shared by the government and industry
New Zealand	Earthquake Commission (EQC)	Earthquake, volcanic eruptions, tsunami, landslides, storm/flood (for land only)	Direct insurance	EQC is a government entity backed by an unlimited government guarantee
Spain	Consorcio de Compensación de Seguros	Flood, earthquake, tsunami, volcanic eruption, windstorm, terrorism	Direct insurance	CCS is a government entity backed by an unlimited government guarantee (although self-financed with its own capital and reserves)
Netherlands	Nederlandse Herverzekeringsmaatschappij voor Terrorismeschaden (NHT)	Terrorism	Reinsurance	Backstop for losses above NHT capacity and up to EUR 50 million
UK	Flood Re	Flood	Reinsurance	Established by legislation
United States	National Flood Insurance Program (NFIP)	Flood	Direct insurance and risk management program	NFIP is administered by the Federal Emergency Management Agency (a government agency). The NFIP collects premiums and has the authority to borrow from the US Treasury. NFIP has transferred part of its risk to private reinsurance companies and capital market investors
	Terrorism Risk Insurance Program	Terrorism	Co-insurance	Federal government backstop through co-insurance for losses above industry loss of USD 200 million with cap on overall losses of USD 100 billion annual

China	China Residential Earthquake Insurance Pool (CREIP)	Earthquake	Direct insurance (co-insurance pool)	The co-insurance pool is reinsured by a state-owned reinsurer
India	Indian Market Terrorism Risk Insurance Pool	Terrorism	Co-insurance/ Reinsurance	The co-insurance pool is reinsured by a state-owned reinsurer
Russia	Russian Anti-Terrorism Insurance Pool	Terrorism (and SRCC)	Co-insurance/ Reinsurance	None
Source: RESPONDING TO THE COVID-19 AND PANDEMIC PROTECTION GAP IN INSURANCE @OECD 2021				

Conclusion & Way Forward

As India's overall Protection Gap in all the segments (both life & non-life) is about 80% to 90%. In other words, only 10% to 20% is being availed any type of insurance. Another issue is the lack of awareness around what is an adequate life insurance cover for an individual, which has increased the mortality protection gap. For instance, during 1991-2021 around 8% of the total losses are covered through any type of insurance, so there is around 92% protection gap in India. So, there is a huge potential, and the insurers need to exploit the situation to garner more business. To plug the gap quickly, in line with Jan Suraksha, Government of India should come out with some standardised products for various sectors so that the protection gap in each segment can be reduced significantly.

Further, to meet the economic losses due to disasters, India should go for a public-private solution, say *a Disaster Pool*, for natural disaster risk involving the insurance sector could offer many benefits over government crisis loans and grants. By considering 2020 floods in India, the total economic loss was of $7.5 billion but insurance of only 11%. If Government would have insured it, then the premium for the sum assurance of Rs 8 billion crore would have only in the range of $1.7-18.8 billion.

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