Insurance industry can risk-proof India

Mr Hemant Shah, Co-Founder and CEO, RMS, lights the lamp at the In:Site India Conference organised by RMS in partnership with GIC Re in Mumbai recently. Also seen in the picture are Mrs Alice G Vaidyan, Chairman-cum-Managing Director, GIC Re; Mr. Randeep Chikara, SVP & Managing Director - India Operations, RMS and Professor Haresh Shah, Co-Founder and Senior Advisor, RMS (extreme right).

Geographic and climatic conditions of India make it highly prone to natural catastrophes. Insurance culture is yet to take root and its penetration is low. This, coupled with growing urbanisation and unplanned expansion, invariably leads to a big gap between economic and insured losses in catastrophic events. The insurance industry needs to work on a strategy to help build a better protected and more resilient Indian society.

By Anoop Khanna

India's geographical area is 329 million hectares and just about 40 million hectares, barely 12%, is flood prone. However, during the period 1913-2013, 51% of natural disasters in the country were due to floods. Also, flood losses have been enormous historically. Available data shows that direct losses due to floods during the period 1965-2001 amounted to over US$30 billion.

Flood disasters

The city of Chennai experienced two major flood disasters in 2015 and 2016. In December 2015, rains broke a 100-year old record with one-day's rainfall covering a month's average precipitation in the city. In December 2016, Chennai's resilience was again put to test by a severe cyclonic storm, Vardah.

Floods in December 2015, caused economic damage to the tune of $2.2 billion and insured losses were around $757 million. Loss of lives was put at 350. Cyclonic storm Vardah in December 2016, according to initial estimates, has caused economic losses of around $1 billion. 18 people lost their lives due to the cyclonic storm.

Development leads to exposure and aggregation of risks

India is also a demographically young nation with growing aspirations. Development is happening with emphasis on 'Make in India'. Investment in infrastructure and other projects is going up. Developmental activity is happening at a rapid pace. All this translates into increase in construction and growth of assets and hence, increase in exposure and aggregation of risks.

These activities exert pressure on the already limited availability of land. Development, especially in big cities and other urban areas is uncontrolled and pressure is to build on flood plains or areas that are highly flood prone.

This rapid and unplanned expansion tends to make future hydrological events more catastrophic and losses can only be expected to rise. When coupled with low insurance penetration, these catastrophic events, make the protection gap between economic and insured losses even larger! The protection gap between economic losses and insured losses in India has always been quite high at almost 80% to 90%.

Protection gap needs to be narrowed

If the pace of growth and development of Indian economy has to be sustained, this huge protection gap needs to be narrowed by increasing insurance penetration. However, it is easier said than done. To focus on these aspects of catastrophe risk management and explore challenges and opportunities provided by low insurance penetration, RMS, a leading global catastrophe risk modelling company, in partnership with GIC Re organised a 1-day In:Site India Conference in Mumbai recently.

Inaugurating the Conference Mrs Alice G Vaidyan, Chairman-cum-Managing Director, GIC Re, said: "The best way to predict the future is to create it. We cannot prevent natural catastrophes but can certainly be well-prepared to address the challenges they pose in their aftermath".

Risk modelling

Risk modelling for floods and other natural catastrophes has yet to take off in a big way in India. Geographical regions in India are unique in their own way. Risk exposures are diverse and different. Moreover, the required historical data for risk modelling is either not available or its quality is suspect. Above all, India is still an evolving insurance industry and the market is yet to mature.

The challenge is to increase awareness about insurance as a means of risk-transfer and to ensure that the insuring public insure their risks right. This is important as often, the insureds are usually underinsured.

Predictive weather risk modelling

Predictive weather risk modelling helps the insurance industry to anticipate and act 'ahead of the weather' and predict risks better. This ensures that insurers adopt more prudent pricing of risks. Adoption of pricing, based on risk modelling could be a difficult proposition to begin with, but in the long run, it would only improve the quality of underwriting and the financial health of insurance industry.

New flood risk model for India

Mr Hemant Shah, Co-Founder and Chief Executive Officer, RMS, introduced a new Flood model for India at the Conference. He explained the range of catastrophe risks – both natural and man-made – and how models provide valuable insights to Indian businesses. The new India flood solution model consists of a full probabilistic flood model as well as a consistent set of flood hazard maps. It is designed to support all cases from underwriting to portfolio management.

Mr Shah said: "In view of climate change and growing global catastrophe risks, catastrophe risk models are much more needed in the decision-making and planning process today than ever before."

Disasters spur insurance

Insurance can help cities like Chennai understand their exposure to flood risk. People are slowly becoming aware of the value and utility of insurance, especially in the aftermath of such catastrophes.

Post 2015 floods, there was a 40-50% increase in the sale of general insurance policies in Chennai. It could be due to a fear psychosis or knee-jerk reaction of people. This spurt, however, does give a feel-good feeling.

Raising prices is not the solution

Insurers are contemplating raising premium rates for various assets located in areas that have experienced increasing frequency of natural catastrophic events in the recent past.

While commercial considerations would justify this response, it may wean away some neo-insurance customers.

Climate change is only likely to increase the probability of catastrophic events happening. There is a lot more, therefore, that the insurance industry needs to do on the ground, beyond raising the premium rates, to ensure that the protection gap is narrowed down. This can only be achieved by close collaboration between the insurance industry and the Government.

At times, political, social and economic compulsions allow development in flood-prone areas. This affects the insurability of the area and the properties being developed there. A lot of public resources are taken away for relief and rehabilitation measures post catastrophic events and not much is left for prevention and risk awareness tasks. Risk management measures such as modelling also need to be complemented by risk reduction, mitigation and adaptation measures.

If risks can be reduced by adaptation measures and losses reduced by risk mitigation, pricing of risks would be more affordable and thus more numbers can be brought under the umbrella of insurance. This would enable insurance penetration to increase and the gap would automatically be reduced.

Highlights

- Risk modelling for floods and other natural catastrophes has yet to take off in a big way in India;
- Development, especially in big cities and other urban areas is uncontrolled and pressure is to build on flood plains or areas that are highly flood prone; and
- RMS introduces a new India Flood Model which consists of a full probabilistic flood model as well as a consistent set of flood hazard maps.

Indian insurance is growing

The Indian insurance industry is on an expansion mode. There are 29 general insurance companies, two Indian reinsurers and five branches of overseas reinsurers operating on-shore. Many more overseas reinsurers including Lloyd's are just steps away from commencing operations in India.

To ensure that they discover the El Dorado, they would need to work on a concerted strategy to prepare the ground that could spawn enough opportunities to keep all of them healthy.

The insurance community should therefore work on a 4-step strategy:-

1. Create better understanding and awareness about risks that India is exposed to.
2. Ensure that insurance as a risk-transfer mechanism gets wider acceptance in India.
3. Strengthen social resilience so that preventing losses becomes the watch-word.
4. Create an infrastructure that manages risks better.

Insurers need to take a greater social and economic role in helping the society and government to create a risk-proof India.