

# Impact Of Joint Venture Companies On Innovation And Growth In Indian Insurance Industry

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*Innovation represents the adoption of new idea, process, product or services, either developed internally or acquired from external environment. Joint venture is viewed as a mode for growth and expansion in target market by applying "Resolve or Involve" ideology. This is necessary for value creation and enhancing learning curve. The improved performance of Indian economy has been reflected in incremental growth of insurance industry and vice-versa. While looking from endogenous factors, the kind of growth that we are currently seeing in Indian insurance industry is largely attributed to innovative techniques introduced and applied by Indian and Foreign joint ventures entrants. The paper will try to explain and examine the impact of product and process innovation emanating out of joint venture (JV) operations and its impact on the growth of this industry. JV provides firms with an efficient means for acquiring and exchanging complimentary knowledge thereby leading to greater level of innovation and growth as its consequence.*

Field of Research : Insurance

## 1. Introduction

The dynamics of inter firm collaboration and joint ventures are increasingly capturing the interest of researchers in strategy and international management. This collaboration provides an avenue to study and analyze their impact on innovation, growth, and value creation in various industries. Insurance industry is an important financial sector contributing in development of a nation's economy. Not only does it helps in adequate risk management of various economic and commercial activities but also helps to regulate the financial industry in an effective way.

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In the past 8 years, Indian insurance industry has witnessed an unprecedented level of innovation and growth, but little research addressed or examined this phenomena. This growth is largely due to innovative products and processes introduced by formation of joint ventures (JV) between foreign and Indian companies post liberalization of insurance market in early 2000. The services sector constitutes approx. 55% of India's GDP (exhibit 1) and it has maintained a higher growth of 10.3%. The opening up of insurance sector has contributed favorably to insurance growth in the country. GDP from insurance sector which constituted 12% of GDP in 2000-01 increased to 19.3% in 2004-05 (exhibit 2). Essentially being a financial service industry, insurance remains an industry with a greater appetite for innovation, be it product or process innovation. This intangible character of the product and service(s) makes it more inclined to adopt innovative ideas to develop and maintain growth. *Integration of tangible or intangible resources from participating firms provides a joint venture or alliance with strategic rents that are achieved not necessarily because it has better or more resources, but rather because the venture's distinctive competence involves making better use of joint resources (Penrose, 1959).* Due to entry of JV companies, consumer awareness has improved; stiff competition has brought more products and better customer servicing. It is having a positive impact on the economy in terms of income generation and employment growth. Not only did the liberalization brought these joint venture companies but also ushered in an era of innovative ideas and practices through them, virtually unseen or adhered to before in the industry.

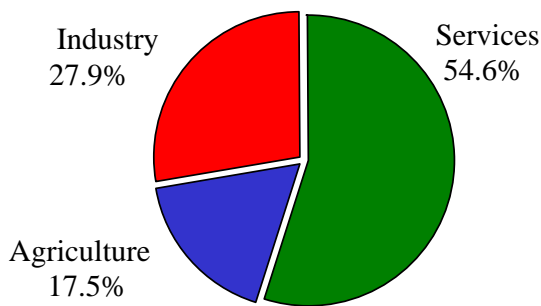


Exhibit 1 (Source : World Bank)

**Share of Service Sector in India's GDP - 2005**

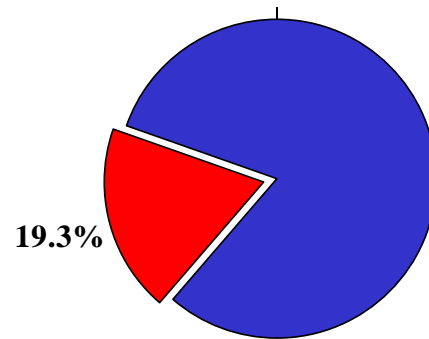
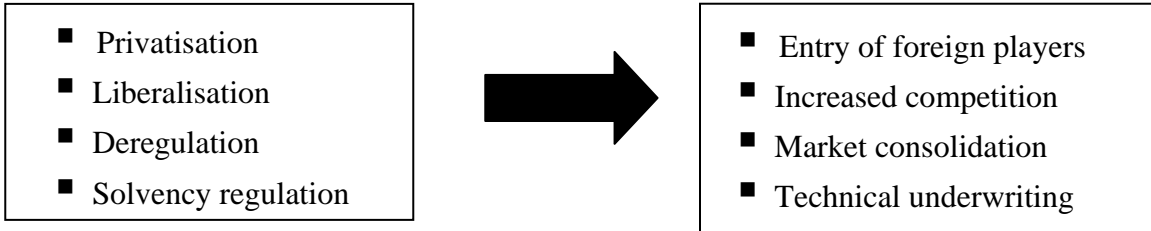


Exhibit 2 (Source : IRDA)

**Insurance Sector as % of GDP - 2005**

Trends in Insurance industry - Insurance regulation has an important impact on structure and development of emerging markets. Currently many countries in Asia (including India & China), Africa and Middle East are going through the path of privatization, liberalization and deregulation (exhibit 3). This will entail the entry of foreign players, increased level of competition and innovation, besides facilitating market consolidation.

**(Exhibit-3) Regulatory changes affecting market structure in emerging markets**



Source : Swiss Re Economic Research & Consulting

Indian Insurance industry - Although India is home to 16% of humanity, but the insurance market has not grown to its full potential and it accounts for only 0.59% of global insurance market (2003). But the scenario is changing and prospects are bright as Industry has witnessed accelerated growth post liberalization period, with studies suggesting that Indian insurance industry can grow by over 125% in the next 10 years. Life Insurance is expected to grow from 33 billion USD<sup>(2)</sup> in FY 2007 to 72 billion USD by 2010 (exhibit-4) with CAGR<sup>(3)</sup> of 35%, while non-life insurance market will grow from current 6 billion USD in FY 2006 to around 12-13 billion USD by FY 2010, clocking a CAGR of 35% (as shown in exhibit-5 & 6).

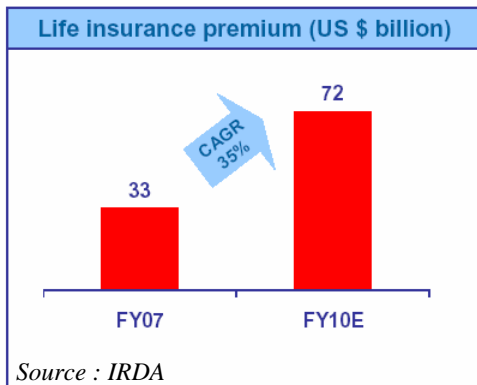


Exhibit - 4

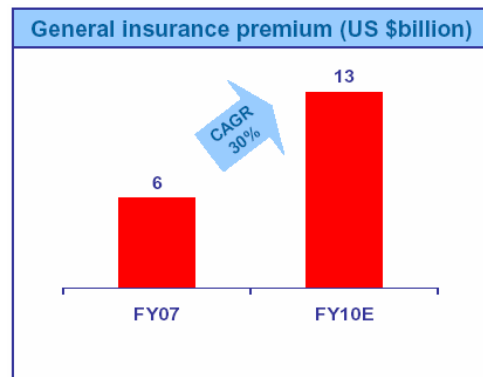


Exhibit - 5

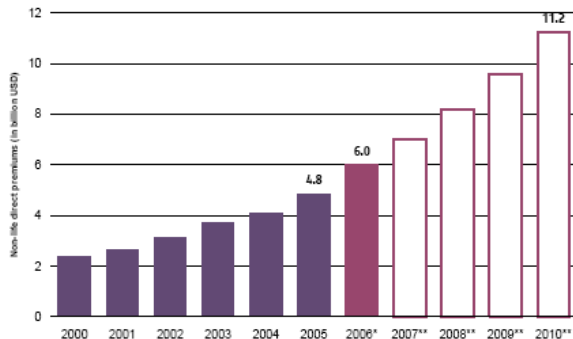
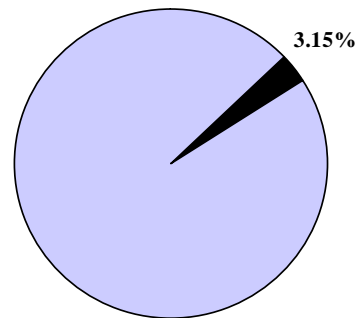
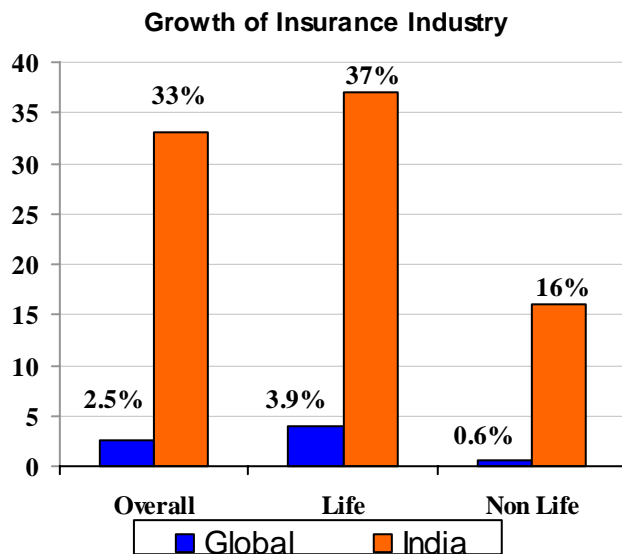


Exhibit-6 **General Insurance Growth**  
Source : India 2010 A Lloyd's View (2007)



**Insurance Premium % of GDP (2005)**  
Exhibit-7

In fact India has been identified as among the fastest growing insurance markets in the world. With a large population and vast untapped market, insurance happens to be the next big area of opportunity in India. Insurance penetration in terms of premium volume as share of India's GDP for the year 2004-05 stood at 3.15% (2.53% for life and 0.62% for non-life insurance) as shown in exhibit 7 above. This is considerably low in comparison to developed markets average of 6-10% of GDP. The insurance sector in India, which was opened to private participation in the early 2000, has completed eight years in liberalized environment. With an average annual growth of 37% in the first year premium in the life segment and 16% growth in the non-life segment (as of 2006), this is exceedingly above the average global growth rate of 2.5% (Exhibit-8). Saturation of markets in developed economies has made the Indian market attractive for global insurance companies, this has resulted in presence of fair number of insurers in both life & non-life segment (exhibit - 9). Together with the largest number of life insurance policies in force in the world, the potential of the Indian insurance industry is enormous.



**NUMBER OF REGISTERED INSURERS IN INDIA**

Type of business	Public Sector	Private Sector	Total
Life Insurance	1	15*	16
General Insurance	6	9	15
Re-insurance	1	0	01
<b>Total</b>	<b>8</b>	<b>24</b>	<b>32</b>

\*One has commenced operations in 2006-07  
Source : IRDA annual report 2005-06

**Exhibit – 9**

Source : Indian Insurance Industry (2005) Exhibit – 8

Furthermore, liberalisation has allowed foreign participation in the markets while former controls on competition and business practices are gradually giving way to a regulatory regime based on prudential supervision of insurance solvency. Foreign companies have since been flocking to participate to not only have the piece of the cake but also to enlarge the size of the cake altogether

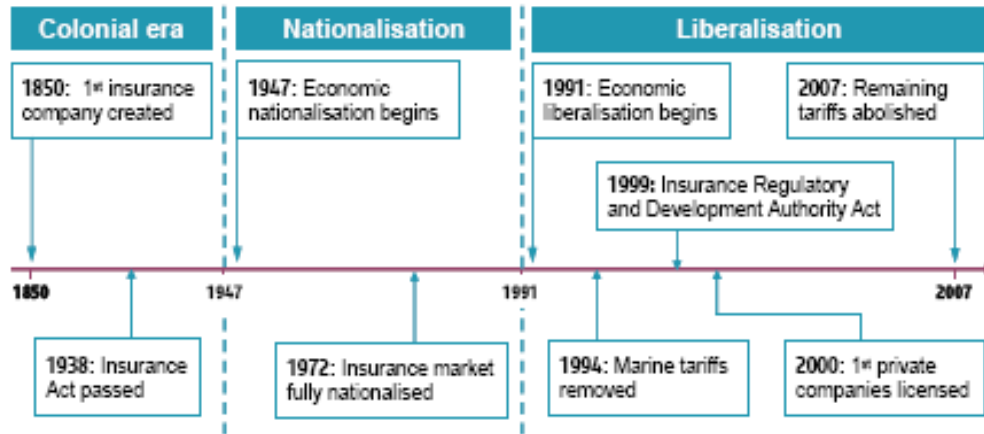
## 2. Literature Review

Innovation represents the adoption of new idea, process, product or service, developed internally or acquired from external environment. (*David Mulford, 2005*). The adoption of innovation follows from and is contingent upon an organization's repertoire of technical, strategic and administrative skills (Nelson and Winter, 1982). The phenomenon of joint ventures is currently much talked about topic in the field of strategy and international management. Ironically this interest partly stems from the fact that while JV continues to proliferate the corporate landscape, they have also been known to exhibit termination rates of 50% or above in various samples (Harrigan, 1988; Kogut, 1989; Park and Russo, 1996; Porter 1987). This phenomena is also been talked upon in Indian insurance industry, once the IRDA act extends or completely abolishes the FDI cap limit. Firms use JVs for a variety or reasons, e.g. access to new technologies and know how, enter new markets, gain competitive advantages, etc. (Contractor & Lorange, 1988; Kale et al., 2000; Casson, 1987). A crucial determinant for a successful JV is the ability to internalize the tacit knowledge of the partner ("absorptive capacity"). Cohen & Levinthal (1990: 128) define the absorptive capacity as the "ability to recognize the value of new, external information, assimilate it and apply it to commercial ends". Gravier et al. (2006) also claim that implementing the external knowledge is more important than just sharing it.

The opening of insurance industry also witnessed major changes in the insurance *products being offered by insurance companies* and *insurance covers opted for by the customers*. For example we see a greater shift from traditional life insurance product (tax saving schemes) to unit linked insurance policies which further justify the changing mindset of the customer in wake of operation of these joint venture companies which are targeting the '*psychic needs*' of the customer rather than just their financial considerations. The operations of joint ventures in Indian insurance industry remains relatively new phenomena, since many of them began their operations post 2002. Therefore not much literature is present on this; other than govt. publications, specific articles, besides some published annual reports and consultancy papers. At this stage its important to analyze the importance of IRDA act.

**Insurance Regulatory and Development Authority (IRDA) Act, 1999** - Upon the recommendations of the Malhotra committee, Indian government passed the insurance bill in Indian parliament, thereby opening the insurance sector for private insurance companies with the enactment of IRDA Act, 1999. Hence, the insurance industry saw a complete circle of events from liberalization to nationalization and back again to liberalization in early 2000 (*India 2010 - A Lloyd's report 2007*), with the partial de-regulation of insurance sector and allowing entry of private and foreign companies into the insurance market. Further, foreign investment was also allowed and capped at 26% holding in the Indian insurance companies. (*IRDA Act, 1999*). Noteable events in Indian insurance industry are shown below.

### Exhibit – 10 : History of Indian Insurance market (1850-2007)



Source : India 2010 A Lloyd's View (2007)

In *Sigma research (2004)* report published by “Swiss Re” comments: “Impressive growth prospects for emerging markets, are putting them at the frontier of insurance. India is arguably the most challenging and promising emerging insurance markets. In tandem with robust economic development, the insurance markets have grown spectacularly (*Clarence Wong, Head of Economic Research and Consulting-Asia.*). While the public sector insurance companies made enormous contribution in the spread of awareness about insurance, and expanded the market, it was recognized that their reach was still limited, the range of products offered restricted and the service to the consumer inadequate (C.S Rao - *Chairman- IRDA*; ‘Indian insurance industry conference ‘*New Avenues for Growth*’ - 2004). It was also felt that the rapid economic growth witnessed in the 90s cannot be sustained without a thriving insurance sector. Till year 2002, the only mode of distribution of insurance products was through agents. Today, alternate channels like bancassurance, brokers, corporate agents and direct marketing through internet are in action.

JV insurance companies are also using innovative techniques to market and expand the outreach of their product and service through intermediaries such as banks, microfinance institutions and cooperative societies to increase their market share and compete with well-entrenched state-owned insurance companies. While no doubt the Joint venture insurance companies have ushered a new wave of innovation into the industry, but additional controversy arises over the question of who does innovation? Whether it is large (public sector) insurers or relatively small (JV) insurers within an industry are more likely to innovate. The conventional view is that small firms are the major innovators as they are more in need of new product or methods to gain a greater share of the market (*Michael L. Murray*). A significant challenge to this view was offered by *J. Schumpeter* when he asserted that innovations are carried out by large firms. However this view is not much in-line today especially in insurance industry which continues to detract away from oligopolistic tendencies thanks to greater deregulations and enhanced use of information technology to overcome the costs of innovating. It will also not be

incorrect to say that for foreign players entered into JV because it was the only means to enter the Indian market as prescribed by the IRDA act. The literature also indicates that joint ventures (especially international JV) are transitional structures, which terminates once they have achieved their initial objectives (Williamson, 1996). Particularly when the cost of cooperation exceeds its benefits the joint venture becomes unsustainable.

### **3. Methodology**

The purpose is to find a positive correlation as to how JV in Indian insurance industry has initiated product and process innovation, which was almost negligible before their inception of operation(s). Here, my aim will be look at the innovation factor from 2 broad perspective applicable to insurance industry :

I.) Product Innovation – Number and types of products introduced, some examples are mentioned as under :

- Life / Health / Accidental/ Rural insurance
- Fire / Professional indemnity / liability insurance
- Underwriting / Premium collection / Renewals / Endorsements
- Claim processing and settlement practices

II.) Process Innovation - some examples are mentioned as under :

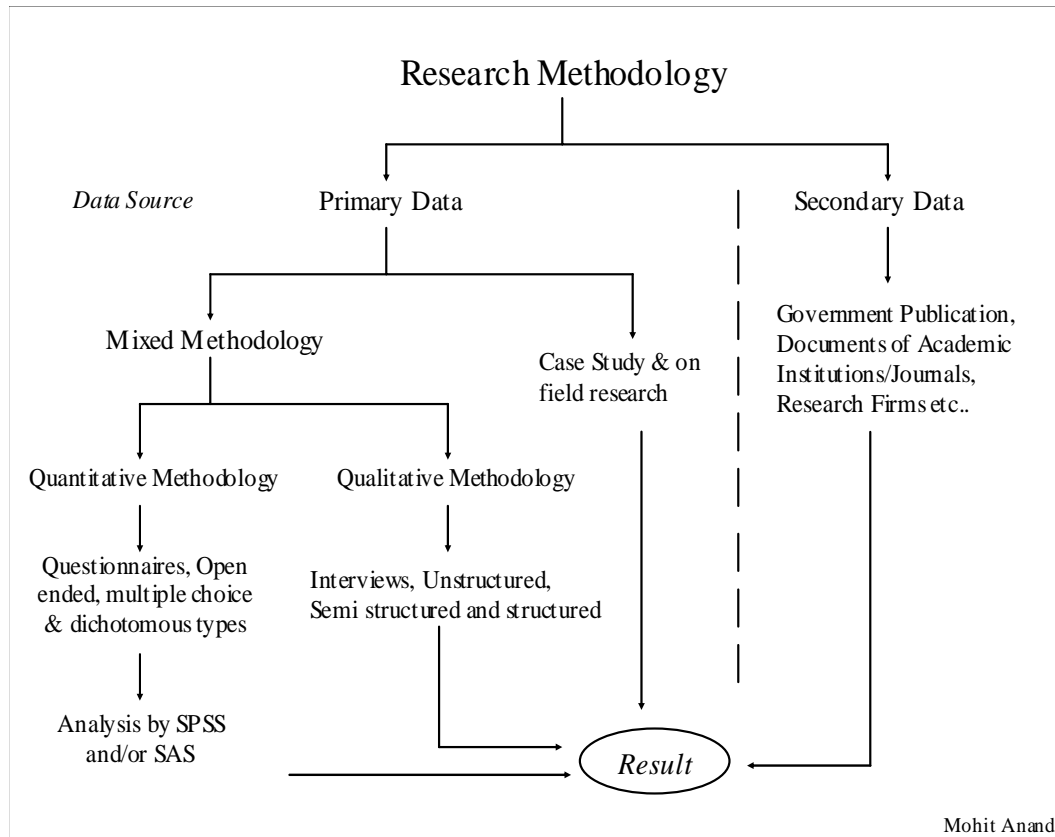
- Distribution channels/ Sales offices / Agents (Individual/Corporate)
- Intermediaries - Bancassurance / Consultants / Risk Managers / Brokers
- Marketing strategy / Advertising / E-insurance / (CRM)
- Role of Information communication technology (ICT)

Growth factors :

- Penetration - Increase in number of insurance policies issued
- Premium (aggregate collection of renewal, first year and new premium)

The data collected will be a cross sectional time series data. The idea is to compare the period when JV companies are operating with a scenario (in terms of innovation and growth) to the period in absence of JV insurers. Hence time series for number of insurance companies' pre and post IRDA act (1999). Since IRDA act allowed JV to operate in India, hence IRDA act and JV operations years are approximately the same and hence it can be used interchangeably as reference year for statistical purpose.

Exhibit – 11 : Flowchart of approach to research question



F.Y. 1993-2000 – pre Joint venture time series  
 F.Y. 2001-2008 – post Joint venture time series

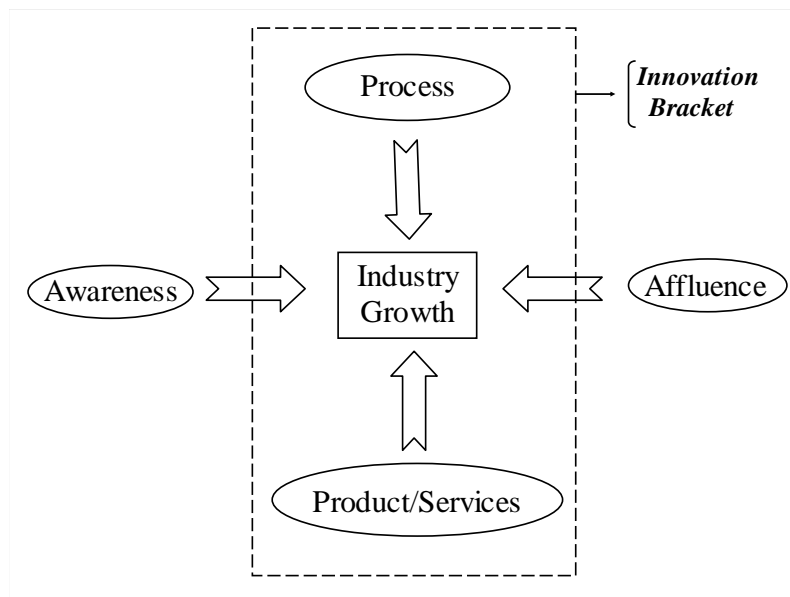
Sample Size: is 31 companies (as of 2007) – This includes total population. Collection of data on insurance companies in operation, identifying number of companies which are :

1. Joint venture companies; &
2. Non JV companies

#### 4. Discussions

The prime objective of the JV companies to enter Indian market is to reap benefits from the booming economy. India is world's second fastest growing economy recording an impressive growth rate of 8% and above. With this accelerated economic activity, comes the rising income and affluence which has been complimented by greater consumer awareness in regard to insurance. As a result major insurance players began their operations in India, but with this developing industry, insurance companies face a range of common challenges. They need to develop innovative bundles of products and services, cross-sell more effectively and

strengthen their relationship with sales intermediaries in order to drive top-line growth (Global Insurance Outlook 2007 - Deloitte Research). Common practice is to divide innovation into two categories – product and process innovation (c.f. Shepherd, William G). The fact that insurance is still in a nascent stage (owing to low insurance penetration rate) is a pertinent point that is leading to adaptation of innovative ideas to reach, lure and cater to untapped customer base in this vast and demographically diverse nation. Hence this generates a large pool of uninsured urban, semi urban and rural middle class population, which is: both in need of insurance; and have the extra disposable income to buy, is therefore the target market for these JV companies. Therefore rising affluence and awareness on one hand and application of innovative ideas on the other are prime contributing factors in growth and development of insurance industry in India (exhibit-12).



(Exhibit -12) Key drivers to growth in Insurance Industry

Most of the joint ventures formed have similar structure as prescribed under the act, but what makes every JV distinct from each other is the source of attractiveness/willingness to enter into such an alliance with their joint partner. With the foray of new JV companies into Indian market, not only they provided more choices to consumers, but also ushered in a new and a much needed wave of innovative products and services. The formed JV works as a 'good fit'; since the Indian partner brings :

- In-depth knowledge of market (demographics of Indian consumer and environment)
- Extensive customer base and strong existing distribution channels
- Greater acceptability and reliability of the product

While, foreign partner provides :

- Insurance expertise and effective risk management practices
- Sound understanding of risks and knowledge of products
- Brand Image and International recognition to JV

## 5. Conclusion

An evolving insurance sector is of vital importance for economic growth. With the entrance of foreign JV firms into the market this invites an analysis of how innovation (product and process) will have considerable impact in both 'approach and reach' to enhance consumer base, is thereby lending further support to the development of insurance industry in India. The contours of insurance business have been changing across the globe and the rippling effects of the same can be observed in domestic markets also. It's been 8 years since the Indian insurance industry was reformed, but relatively not much research has been dedicated to analyze the impact of JV insurers upon growth and innovation in the industry; It is this gap I want to fill. Besides innovative ideas applied in product, Insurers face rising pressure to retain clients. Hence innovation in information systems, customer service and imaginative marketing approach are more so necessary. Many of the JV insurers bank upon product innovation and an increased acceptance of its global products to survive in this highly competitive insurance market which is even today dominated by public sector insurers. Hence for JV firms, innovation is a necessity but also the key to competitively survive and grow in long haul prospects of this market.

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**Appendix :**

- 1.) General Insurance is interchangeably referred to as Non-life Insurance
- 2.) Values in INR & USD indicated are applicable for the referred year
- 3.) CAGR : Compound Annual Growth Rate