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# Impact And Influence of Insurance on Economic Trustworthiness of A Financial System to Achieve Financial Inclusion

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**ABSTRACT**

The insurance industry is critical to the financial stability of a financial system. This is because its liabilities are long-term in nature, whereas its assets have a short term average maturity. Insurance is an important part of the financial system. Financial services constitute an important component of the financial system. Financial services through the network of financial institutions, financial markets and financial instruments, serve the needs of individuals, institutions and corporates. The Financial System includes securities, banking, insurance, mutual funds, pension funds, and provident funds. The growth of the insurance industry is inextricably linked to economic growth. It is intertwined and responsible for the expansion of the economy. Innovation in product which invited many unit linked policies was the centre of attraction for all. Linking insurance with allied finance products like housing loan, mutual funds investment in companies, bank credit cards etc. are the new channels for insurance.

Stable economic development, increasing population, urbanization, commodity prices, the middle class, and increased knowledge of risk in an individual's life are all key parameters that contribute to the growth of insurance. India is a developing economy, hence, all of these factors are critical. The financial system in India underwent a change after 1990 with the adoption of new economic policy, which is one of liberalization. Vast changes have been witnessed in financial markets and services due to the far reaching economic and financial reforms introduced. Insurance industry has introduced a lot of micro insurance schemes, which even the poor folk can afford. This paper focuses on creating awareness among the people, and the role insurance plays in enhancing economic trustworthiness of financial system to achieve financial inclusion in India.

**Keywords:** *Financial system, Financial services, Insurance, Economic Trustworthiness and Financial Inclusion*

## INTRODUCTION

Indian financial system consists of financial markets, financial instruments, financial services and financial intermediaries. The financial system is concerned about money, credit and finance. The economic development of the Indian nation is reflected by the progress of the three economic units called corporate sector, Government sector and household sector. While executing their functions and activities these units will be placed in a surplus or deficit or balanced budgetary situations. The main function of Indian financial system is the flow of funds through the financial services from the suppliers of funds mainly from the household sector to the seekers of funds mainly to the business firm and government sector. Hence, the trading in money and monetary assets constitute the activity in the Indian financial markets and are referred here as the financial system. Stable economic development, increasing population, urbanization, commodity prices, the middle class, and increased knowledge of risk in an individual's life are all key parameters that contribute to the growth of insurance. India is a developing economy, hence, all of these factors are critical.

Financial system aims at establishing a regular, smooth, efficient and cost effective link between savers and investors. Thus, it helps encouraging both saving and investment. Financial system facilitates expansion of financial markets and over space and time and promotes efficient allocation of financial resources for socially desirable and economically productive purposes. Various constituents of financial system are financial institutions, financial markets, financial instruments and financial services. These constituents are closely inter-mixed and operate in conjunction with each other. The centrality of finance in an economy and its importance for economic growth naturally raises the importance of financial innovation and its diffusion. With the advancement of technology, online trading has gained importance. One can have access to the capital market from any nook and corner of the world.

## FINANCIAL SERVICES

Financial services are the process by which funds are mobilized from a large number of savers, and make them available to all those who are in need of it. Financial organizations facilitate the financial transactions of both individuals and corporate customers. When the borrower approaches the financial markets to raise the funds, proper channel within the financial system should be ensured through various financial instruments. Hence financial services came into existence. These services are offered by the banks and other financial institutions. Financial institutions provide a variety of services such as, financial and performance guarantees, deposit insurance and other insurance, underwriting, discounting and rediscounting, leasing, factoring etc. Financial institutions are business organizations dealing in financial resources to collect resources. To serve the financial services to the needy ones, the financial intermediaries are functioning in the organized sector under the control of the Reserve bank of India.

Finance plays a part in every economic transaction in which there is a present or future payment of money. It is one of the foundations of all kinds of economic activities. A firm's success, and in fact, its very survival depends upon how efficiently it is able to generate funds. Financial services need to be tailored to meet the needs of the poor, and marginalized. Extending access to finance in rural areas is helping farmers and small businesses thrive. Thanks to the micro financial services aimed at expanding financial inclusion in India. It is true that the first- time users may need customized products and accompanying financial literacy services that explain how to use financial products. Without financial access, these small entrepreneurs would be telling a different story.

Financial services include not only banking products but also other financial services such as insurance and equity products. Access to affordable basic financial services (having a bank account, credit, deposit and insurance etc.) is one of the key challenges facing the rural and semi-urban population in India. Insurance occupies an important place in the complex modern world since risk, which can be insured, has increased enormously in every walk of life. This has led to growth in the insurance business and evolution of various types of insurance covers.

## Insurance

Liberalization has created an acute competition in the insurance market because more and more players join in the greater Indian insurance. It is necessary to promote more awareness about insurance among the public because there is a lot of untapped market in the country. Customer behavior will be influenced by environmental factors as well as intrinsic personal aspirations. The environmental factors are socio-economic and demographic factors, inputs of insurance advisors, the company's efforts to manage customer satisfaction and experience. There are quality insurance advisors in the field due to the passing of IRDA bill. Distribution is a key determinant of success for insurance companies. Because at more number of distribution channels the insurers have a large database of their disposal. Linking insurance with allied finance products like housing loans, mutual fund investment in companies bank credit cards etc. are the new channels for insurance. It is definite that the new channels will help the insurance companies to reach out farther, wider and deeper.

**Objectives**

This research paper has two main objectives and they are:

1. To study about the significance of insurance in the Indian financial system.
2. To evaluate the relationship between Insurance and economic trustworthiness of financial system and create awareness about its benefits among the rural population.

**FINANCIAL INCLUSION**

Financial inclusion is a process of ensuring access to financial services and timely and adequate credit to vulnerable groups such as weaker sections and low income groups at an affordable cost. It is a much cherished policy objective for India: the Indian economic policy has always been driven by an intent of a sustainable and inclusive growth. The policy makers in India, i.e., Government and the RBI, had an early realization about the implications of poverty for financial stability and have endeavored to ensure that poverty is tackled in all its manifestations and that the benefits of economic growth reaches to the poor and excluded sections of the society. Recent initiatives by the government, regulators the private sector and global developmental community to improve financial inclusion are yielding impressive results. Let us take a close look at what policy makers and central bankers are doing to fine tune enabling environment.

The main objective of financial inclusion is to bring the bottom of the pyramid of financial landscape under the ambit of formal banking and financial system. For example, the financially excluded ones, the poor and the illiterate, instead of availing a bank loan or availing micro credit facility from a bank or financial institution, they approach the money lenders in dire need and these money lenders exploit the poor by charging them a high rate of interest. Also take advantage of their vulnerability. This is because of the complexity of the procedure of availing a bank loan. If they are given easy access to micro financial services, they will be in a position to meet/build their financial requirements and safety. Such people can even save some money for their own future needs, children's education, famers for their agricultural needs, sick business units can be brought to the healthy zone, medical needs etc.

RBI's financial inclusion effort can be traced back to the 1960's when focus was on channelizing of credit to the neglected sectors of the economy and the weaker sections of the society. Since 2006, RBI has adopted a planned and structured approach to address the issue of financial inclusion. There is a growing concern in Indian system, as liberalization improves financial services and products for the few. RBI's approach has been to focus on the demand as well as the supply side, and has been possible due to the gradual adoption of technology within the banking processes interwoven with other players in financial system.

Financial inclusion refers to a state in which all sections of the society, including those currently excluded by the financial system, have effective access to financial services such as credits, savings, payments, insurance etc., offered by formal institutions. Being included in the formal financial system helps people –

- To make day-to-day transactions such as sending and receiving money.
- Finance small business or micro expenses.
- Manage expenses related to unexpected events and improve their overall welfare.
- To safeguard savings which can help households manage cash flow spikes smooth

consumption and build working capital.

Thus the financial inclusion is linked to the economy and social development of a country and plays a role in reducing extreme poverty.

## LITERATURE REVIEW

Sourajit Aiyer (2017), in his article concludes that financial inclusion is a cycle and there must be adequate capacity to feed that cycle sustainably. That supply is a push towards economic progress. Moreover, as the local financial industry develops, it gives a push to local talent. As India's GDP rises, it will open up further opportunities for financial services through banks and capital markets.

Jawed Akhtar and Md. Masoor Alam (March 2017) state in their article that microfinance has emerged as a vital approach to meet the heterogeneous needs of the poor in India. Micro finance, in the formal sector has assumed the form of SHG-bank linkage programme. In India, this SHG-bank linkage programme is rapidly expanding its outreach under the pioneering initiative of NABARD, the monitoring supervision of RBI and the promotional policies of the government of India.

Dr. Paresh Shah (2018), was of the opinion that financial inclusion is a much cherished policy objective for India. According to him, the government of India and the RBI had an early realization about the implications of poverty for financial stability and have endeavored to ensure that poverty is tackled in all its manifestation and that the benefits of economic growth reaches to the poor and excluded sections of the society.

Dr. Alamelu (September 2017), found that there is a significant gender gap exists in the form of the quality of access to a bank or a mobile money account and ownership of that account. He further states that there is a clear need to enable more women to participate in the global economy. The World Bank Group, in its new gender strategy, puts women's economic empowerment and the financial services necessary to achieve it, high on the agenda. For this, the WBG is developing policy frameworks promoting conditions for women entrepreneurship, reducing skill gaps etc.

J. Thiravia Mary Gloria and P Santhi (March 2016), were of the opinion that participation in financial inclusion plans would inculcate financial discipline among subjects. Enhancement of knowledge and judgment skills with respect to financial decision making would be the outcome of better understanding of the features of various financial products such as risk/return aspects. It is also expected to develop a regular savings and stable accumulation of wealth, appropriately purchasing insurance and borrowing when necessary.

## Frequency Distribution with respect to Financial Behavior

In this our endeavor we have tried to examine the financial behavior of 120 respondents from Medchal district of Telangana State. Rural respondents were given awareness about the financial services and the advantages of the various financial products like Insurance, micro credits, Debt, Financial Emergency, Risk and Return by the Financial Literacy Centers appointed by Central Government of India.

**Table – 1- Frequency Distribution with respect to "Financial Behavior"**

| **Financial Behavior** | | Strongly Agree | Agree | Neutral | Disagree | Strongly Disagree | Total |
|---|---|---|---|---|---|---|---|
| I feel capable of using my future income to achieve financial goals | Frequency | 27 | 29 | 23 | 18 | 23 | 120 |
| | percent | 22.4 | 24.2 | 19.2 | 15 | 19.2 | 100 |
| I enjoy talking to my peers about money related issues (i.e. Taxes) | Frequency | 20 | 27 | 20 | 24 | 29 | 120 |
| | percent | 16.7 | 22.5 | 16.7 | 20 | 24.1 | 100 |
| Dealing with money is stressful | Frequency | 24 | 26 | 23 | 22 | 25 | 120 |
| | percent | 20.1 | 21.6 | 19.2 | 18.3 | 20.8 | 100 |
| I have the ability to understand financial language | Frequency | 21 | 29 | 22 | 26 | 22 | 120 |
| | percent | 17.3 | 24.2 | 18.3 | 21.9 | 18.3 | 100 |
| Having thought about long term financial plans for the future and retirement | Frequency | 22 | 25 | 24 | 25 | 24 | 120 |
| | percent | 17.6 | 21.1 | 20.1 | 21.1 | 20.1 | 100 |

*Source: Field data*

The study shows there are 22.4% and 24.2% responses obtained for strongly agree and agree, respectively out of 120 responses for 'I feel capable of using my future income to achieve financial goals'. This means that the financial literacy rate of these respondents are high and they are well aware of the financial schemes and financial instruments available in the financial markets. The result was found to be 16.9% for strongly agree and 22.7% for agree results out of 120. This shows that opinions are confident in taking advice with their peers in financial issues. The third point in table shows that there are 20.1% and 21.6% responses obtained for strongly agree and agree, respectively. After the awareness Program on understanding Financial Language, the study shows there are 17.3% and 24.2% responses obtained for strongly agree and agree, respectively. For the last point there are 17.6% and 21.1% responses obtained for strongly agree and agree, respectively. Finally we can say that respondents are able to manage their financial needs in a just manner.

The table below shows the insurance penetration and density over the past ten years.

Table 2 - Year wise Insurance Penetration and Insurance Density

| Year | 2010 2011 | 2011 2012 | 2012 2013 | 2013 2014 | 2014 2015 | 2015 2016 | 2016 2017 | 2017 2018 | 2018 2019 | 2019 2020 |
|---|---|---|---|---|---|---|---|---|---|---|
| Insurance Penetration in (%) | 4.4 | 3.4 | 3.17 | 3.1 | 2.6 | 2.72 | 2.72 | 2.76 | 2.74 | 2.82 |
| Insurance Density (USD) | 55.7 | 49 | 42.7 | 41 | 44 | 43.2 | 46.5 | 55 | 55 | 58 |

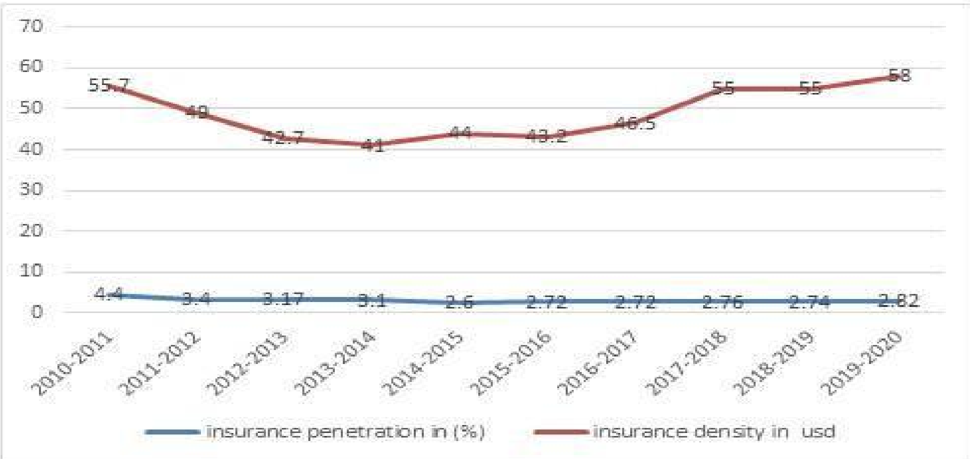


*Figure – 1- Year wise Insurance Penetration and Insurance Density*

In the above diagram we can see that over the years insurance has made its market expanding and the penetration level increasing. And it is pointing to a positive feeling that insurance can influence the economic trustworthiness of a financial system in achieving financial inclusion. Insurance plays a major role in achieving financial inclusion. In India, liberalization of the economy has created new opportunities for insurance to reach the vast majority of the poor. As India is a vast country with a large population living below the national poverty lines and is extremely poor, financial inclusion has become an urgent need of the hour. Emerging country like India getting access to the various financial services through the central government's social security schemes like Pradhan Mantri Jan Dhan Yojana (PMJDY), Pradhan Mantri Jeevan Jyothi Bheema Yojana (PMJJBY), Sukanya Samriddhi Yojana (SSY) etc., which are acting as powerful tools to enhance the financial inclusion is noteworthy. A wide range of social security schemes were launched for the purpose of financial inclusion and they have proved to have a competitive advantage in remote areas and deprived community, less educated and those in the unorganized economy. Although there are various means to achieve financial inclusion, insurance plays a vital role in bringing about the desired financial inclusion.

Financial services need to be tailored to the needs of the poor and marginalized. Extending access to finance in rural areas is helping farmers and small businesses thrive. Thanks to micro financial services aimed at expanding financial inclusion in India. In India, in the past, successive Indian governments have taken efforts to use insurance as one of the tools to promote socio-economic development in rural areas. When we think of innovations in insurance products and services what comes to our mind are innovations in banking, micro credit and micro finance. Micro insurance in rural India was encouraged by financing institutions primarily to hedge their own risks while lending to the poor under the requirements of direct lending issued by the government. Over the years, micro insurance as a financial service innovation is fast emerging as an important method of bettering the lot of the poor and the downtrodden.

## CONCLUSION

The Indian financial system has experienced comprehensive changes in the last few decades. Its market infrastructure has advanced while the corporate governance has progressed faster than in any other emerging market economies. Insurance occupies an important place in the complex modern world since risk, which can be insured, has increased enormously in every walk of life. This has led to growth in the insurance business and evolution of various types of insurance covers. It can play a significant role in the economic development of a country, while economic development itself can facilitate the growth of the insurance sector. Insurance is an important financial service available in today's world as it provides safety and security against the loss on particular event.

The most powerful steps adopted to advance financial inclusion as identified from such policies of various countries can be adopted and integrated into national financial inclusion strategies with the ultimate goal of eliminating persistent gender gap in financial inclusion. The main objective of financial inclusion is to bring the bottom of the pyramid of financial landscape under the ambit of formal banking and financial system. Since 2006, RBI has adopted a planned and structured approach to address the issue of financial inclusion. In contrast to several developed countries, Indian financial system is still shallow, which implies that further reforms are needed to make India a world class financial Centre.

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