

Conceptual Analysis of Risk management Pertaining to Insurance Industry

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Abstract: *Over the years, general insurance firms have made significant efforts to manage risk in order to safeguard investors and their interests. The general insurance industry today places the greatest emphasis on two factors: the potential of the Indian general insurance market and the participants' consequent focus on achieving company expansion. The continual process of calibrated de-tariffing is the second factor. De-tariffing has increased the number of market options for players and may open up even more in the future, but it has also placed the onus of fair pricing on the players themselves. Players are now more prepared, emphasising risk factor detection and product pricing in accordance with risks as a result. As an early response to the pressure of a free market environment, the participants have reduced the rates even in previously unsuccessful businesses. The general insurance market places a great deal of emphasis on an efficient risk assessment and management due to the emergence of private players, associated legislative changes, the existing reality of unprofitable books, and capital degrading as a result of unsustainable claim ratios.*

Keywords: risk assessment, risk mitigation, general insurance, and asset liability management.

I. INTRODUCTION

Any industry that is growing must contend with a number of internal and external risks. In contrast, the majority of risks in industries that have been there for a while are caused by the internal actions of the different participants. An industry that is changing often confronts larger risks from the competitive and regulatory environments than from internal operations. One must focus on sales while scaling operations swiftly by adding channels and extending their geographic reach in order to grow in a competitive market. There are several risks for achieving financial success when sales and corporate expansion are prioritised more. A company's performance or even survival may suffer as a result of these risks. Because of the nature of their line of work, general insurance companies are both an insurer and an insured. The performance of the company depends on its ability to comprehend both internal and external risks associated with the general insurance business industry, as well as the methods insurers and insured utilise to effectively manage their risks.

II. LITERATURE REVIEW

Because they are in the business of assuming the risks of other corporate and social organisations, the general insurance players are vulnerable to operational and financial risks affecting both themselves and the insured. The key to success for successful risk management of structural functions is in the accurate identification of structural functions, their insurability, sufficiency, and economic viability. In the event of an underwritten threat, the risk may also be decreased by risk sharing via microinsurance pooling, appropriate quantification, and accurate result estimation. It is impossible to overstate the importance of understanding risk transfer in the risk management process for successful risk mitigation and adaptation by core business. Certification will offer the instruments even more depth by embracing innovation. Encouragement of public-private partnerships and a strong financial, legal, and political framework will be essential to further increase the penetration of general insurance and decrease the constantly increasing claim ratio. The Asian Rice Insurance Mechanism (ARIM) is an idea presented by Mendoza and Ronald (2009) for a regional risk-sharing framework that may be used by the region as a long-term solution to the issue of food security. It proposes that ARIM might serve as a regional public good by enabling countries in the region more efficiently in managing the risks associated with variable rice production and trade, as a result of new structural elements such the rising and shifting

food demand. In their examination of environmental risk, risk management, and uncertainty, Lubken et al. (2011) also addressed the influence of environmental risk on social, scientific, economic, and cultural processes. They propagated the fallacy that natural disasters are brought on by previous patterns of vulnerability and resiliency. As well as the challenges insurers and reinsurers face in addressing the implications of climate change on their risk management strategies, Kunreuther et al.'s 2007 research looked at the insurance industry's role in minimising the effects of global warming. The study has examined the issues of attribution and insurability by focusing on natural disaster insurance. Phelan et al. (2011) studied the efficacy of insurance responses to climate risk and provided new criticisms of the insurance system's responses to climate change and the related political economics perspective on the subject. According to a complex adaptive system analysis, ecologically suitable mitigation is the only viable option to manage medium- and long-term climate risk, both for the insurance system as a whole and for human civilizations as a whole. Another essential component of commercial viability has been studied by Akter et al. (2009). The study's conclusions show that Bangladesh's crop insurance market structure is not uniform. It emphasises how thoroughly examining the socioeconomic characteristics of rural farming communities as well as the types of disaster risks that farm households face when developing such an insurance plan is necessary. Mauelshangen & Franz (2011) looked at the characteristics of adaptation and decision-making in the insurance industry. They have drawn parallels between the historical analysis, the present-day concerns about global warming, and potential changes to insurance to cover associated losses. In France, Erdlenbruch et al. (2009) looked at the impact of the French Flood Prevention Action Programme on risk distribution. The results of the survey indicated that the proposed reforms might not be financially feasible. Then, a number of risk-sharing alternatives that are more practical are taken into account, including insurance policies, governmental intervention, and regional institutions. Spatial pooling in the microinsurance programme could reduce these capital requirements. Spatial pooling may be a desirable alternative for micro-insurers when creating index-insurance schemes, according to a 2009 study by Meze-Hausken et al. This warrants a comprehensive case-by-case assessment. Botzen et al. (2009) also examined how insurances can reduce the uncertainty surrounding individual losses brought on by climate change. The estimation results indicate that a successful flood insurance industry may be feasible, and that climate change may potentially increase the profitability of flood insurance sales. Rohland & Eleonora (2011) have investigated risk management and risk quantification in the wake of fire in the Swedish and international reinsurance businesses. The report argues that classifying fire as a man-made hazard misrepresents its overall risk by disregarding its natural causes and associated concerns.

III. RISKS TO THE INSURANCE SECTOR

Participants in the general insurance industry are likely to be exposed to a variety of financial and non-financial risks due to the nature of their industry and the socioeconomic environment in which they operate, including capital risk, enterprise risk, asset liability management risk, insurance risk, operating risk, and credit risk.

3.1 Financial risk

A variety of financial risks, including those relating to capital structure, capital (in)adequacy, exchange rates, interest rates, investments, underwriting, catastrophic risk, reserve risk, pricing, claims management, reinsurance, policy holders and brokers, claims recovery, and other debtors, are present in the insurance industry because it is fundamentally a financial one. The insurance sector employs a variety of strategies to manage financial risk by using techniques like interest rate hedging and reserving that are based on financial modelling but come with an inherent "model risk" because such financial models may not be able to accurately predict the actual results within an acceptable margin of error.

3.2 Other types of risk

The industry's growing reliance on sophisticated financial technology, which occasionally runs the risk of failing, (ii) an increase in operational losses, (iii) the rate at which the deregulated insurance system is changing, and (iv) the process of globalisation, which has opened the door for the entry of foreign players have all contributed to the importance of non-financial risk management in recent years. The "volatility" element, which affects the general insurance business's future cash inflows and, as a result, its value, is the additional non-financial risk that the insurance industry faces in

addition to these. Studies have indicated that the operations of the company, rather than financial risks, are a key source of volatility, so "the value of an insurance company is the present value of its future net cash inflows adjusted for the risks it undertakes." Therefore, the operating risk may result from either inadequate or ineffective internal procedures like employment practises, workplace safety, and internal fraud, or from deficient or ineffective external events like external fraud and damage to physical assets from natural disasters or other uncontrolled events.

IV. PROCEDURES FOR RISK MANAGEMENT AT GENERAL INSURANCE

In the general insurance sector, the insured's approach to risk management commonly takes the form of "enterprise risk management," whereas the insurer's approach frequently entails "risk based capital management" and "reserving."

Any organisation must use every available means to minimise the risk of loss brought on by unforeseen events like earthquakes, floods, fires, theft, etc. To ensure that a system for risk minimization and mitigation is in place, the insured must engage in an effective risk management drive. The phrase for the approach the insured can take to handle such risks is enterprise risk management.

4.1 Management of Organisational Risk -

The process of planning, organising, and controlling an organization's operations in order to lessen the impact of risk on its assets and income is known as enterprise risk management (ERM). As markets and regulators throughout the world rate businesses on how well they manage risk, ERM is increasingly spreading among business practises.

4.2 Risk monitoring and reporting

Another crucial element of ERM is monitoring risks over time to evaluate how well they are being managed and to deal with new trends. Comparing them is less important than creating a baseline that can be followed across reporting periods. The insured must continually remind them that a risk should not be dismissed or excluded from the ERM strategy just because it cannot be precisely evaluated or compared to other risks. Although it can be difficult to estimate a risk's financial impact, its incidence can nonetheless be tracked. When the relative gravity and likelihood of various risks are assessed, a mitigation strategy is developed. In some circumstances, a risk-mitigation strategy may actually increase the likelihood or severity of another risk, in which case the trade-off must be carefully addressed.

Even though it may raise a company's reserve or liability coverage requirements, ERM's goal is to provide the best protection against unfavourable situations. By minimising the double counting of risks by prior risk management measures, an ERM framework may in some cases result in cost savings. In any case, under ERM, a greater variety of threats is likely to be considered.

4.3 The insurer's risk mitigation techniques

The two fundamental categories into which the risk management strategy employed by the insurer in the general insurance sector can be broken down are "risk-based capital management" and "reserving." The management role, capital and solvency margins, and risk-based capital are all included in the "risk based capital management technique" category, whereas the "reserve" category of risk management techniques includes unearned premium reserves, unexpired risk reserves, outstanding claim reserves, incurred but unreported reserves, catastrophe reserves, and claims equalisation reserves. Perhaps it is not out of place to mention this distinction once more.

V. CONCLUSION

The goal of the study is to identify the risks that the insured and the insurer face, particularly in India, as well as the strategies for managing these risks. According to the survey, both the insured and the insurer in India often have to deal with risks, both financial and otherwise. Financial hazards for both of them fall under the categories of capital risk, asset/liability management risk, insurance risk, and credit risk. Their non-financial hazards are under the categories of enterprise risk and operational risk. Capital (in)sufficiency risk and capital structure risk are both components of capital risk. The asset liability management risk includes exchange risk, interest rate risk, and investment risk. Similar to how insurance risk includes underwriting risk, catastrophe risk, reserve risk, and claims management risk, credit risk also includes reinsurance risk, policyholder and broker risk, claims recovery risk, and other debtor's risk. The enterprise risk also includes reputation risk, parent risk, and competitors risk, much as operational risk consists of regulatory risk, business continuity risk, IT obsolescence risk, process risk, regulatory compliance risk, and outsourcing risk.

A typical risk management tactic employed in the general insurance industry for the insured is enterprise risk management, which entails planning, risk tracking and reporting, implementation, tools, and risk management. While it takes the form of managing risk-based capital and reserves for the insurer, the former including management role, capital and solvency margins, and risk-based capital, and the latter including unearned premium reserves, unexpired risk reserves, outstanding claim reserves, incurred but not reported reserves, catastrophe reserves, and claims equalisation reserve.

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