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An Empirical Study on Consumer Behavior of Life Insurance Purchasing Decision

Prof. Ashish Kumar Srivastava

Department of Commerce,
DDU Gorakhpur University, Gorakhpur

Abdul Jadid

(Research Scholar)
Department of Business Administration
DDU Gorakhpur University

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Abstract

The Indian economy is one of the fastest growing economies in the world with GDP per capita growing at a rate of 7.1% per annum¹. The country is also experiencing a demographic shift towards a younger population with about 35% of the population being between 15 and 34 years of age² in 2017. In the next few decades, unprecedented numbers of young people are expected to enter the workforce, earn and save part of their earnings. India's household financial savings were estimated to be about 8.1% of the Gross National Disposable Income (GNDI), or about \$26 trillion in the financial year 2016-17. About a fourth of these savings are invested in insurance³. Thus, the insurance sector is large and will grow further in the coming years. Understanding consumer behavior and what influences purchase decisions is important for different players in this industry including regulators and insurance companies.

Despite recent growth, the life insurance market in India has low penetration rates compared to many other countries. Financial inclusion is one of the primary concerns of policy makers across the world. Now the author has described several aspects about consumer behavior about Life Insurance at the event on purchasing.

Keywords- Behavioral theories of Insurance Economics, Socioeconomic and Demographic Factors which effects life Insurance Demands, and Consumer Behavior in Life Insurance

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Introduction

The Indian economy is one of the fastest emergent economies in the world with GDP per capita growing at a rate of 7.1% per annum¹. The country is also experiencing a demographic change towards a younger population with about 35% of the population being between 15 and 34 years of age² in 2017-18. In the next few decades, unprecedented numbers of young people are expected to enter the workforce, earn and save part of their earnings. India's household financial savings were estimated to be about 8.1% of the Gross National Disposable Income (GNDI), or about \$26 trillion in the financial year 2016-17. About a fourth of these savings are invested in insurance³. Thus, the insurance sector is large and will grow further in the coming years. Understanding consumer behavior and what influences purchase decisions is important for different players in this industry including regulators and insurance companies.

Life insurance allows individuals to secure the financial future of their families in the event of their own premature death. It also serves the savings and investment needs of individuals who may be unaware of or wary about investing in mutual funds or the stock market. Unlike countries in the developed world, social security or government pension schemes are accessible to only a small part of the population in India. Most people use bank savings, fixed deposits, post office savings and public provident fund (PPF) as instruments for savings and investment. Due to the lack of access to formal financial markets and lack of information and financial literacy, life insurance assumes a critical role in the financial wellbeing of a large part of the society. It is especially important for rural and poorer sections of the society.

Evolution of Life Insurance sector in India

The insurance sector in India was under public ownership until late 1990s. With the liberalization of the insurance sector, the Insurance Regulatory and Development Authority Act (IRDA) were passed in the year 1999 to regulate and promote the insurance industry in India. Insurance Regulatory and Development Authority of India (IRDAI) was set up as a statutory body to regulate Indian insurance and re-insurance market and to protect the interest of its stakeholders. The Indian insurance sector was further liberalized in the year 2015 with Insurance Law (Amendment) Bill 2015 and Foreign Direct Investment (FDI) limit was increased from 26% to 49%. Today, the life insurance market in India is one of largest in the 5 world both in terms of total premium expenditure as well as number of policies sold. In insurance business India is ranked 10th among 88 countries.

The Indian life insurance market has been a monopoly with the Life Insurance Corporation of India (LIC) being the only provider of insurance till the year 2000. After 2000, the market was

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liberalized and private player were allowed to enter the market. At present there are 24 life insurance companies registered in India. Among these, Life Insurance Corporation of India (LIC) is the only public-sector company. Even though there are larger number of private players in the market, Life Insurance Corporation of India (LIC) is the single largest insurance provider with about 71.8% of the market share. LIC operates through a large network of sales agents. By the end of the year 2016-17 LIC had 1.13 million agents, the corresponding number for private sector insurers was 0.96 million. LIC has a unique position in Indian market as it is considered as the most trustworthy life insurance provider in the country. As per the IRDA, the insurance market in India was about Rs. 328,000 crores (or about \$48 billion) in terms of the premiums collected. ICICI Prudential, SBI Life Insurance and HDFC Standard Life are the largest private sector players catering to about 15% of the market together.

Socio economic Prospects of Life Insurance

Life insurance has low penetration among Indian households, with insurance premiums accounting for about 2.72 % of GDP. Due to lack of access to formal financial markets and low levels of financial literacy many Indian households do not effectively plan their financial future. With an increasing emphasis by the government towards greater financial inclusion of all sections of the society, it is important to understand how socio-economic and demographic aspects of rural and urban households affect their decisions to acquire or discontinue life insurance coverage.

Though life insurance is primarily a means of mitigating financial risks associated with premature death, it is mostly used as a tool for savings and investment through endowment policies in India. Social security or government pension schemes are accessible only to a small part of the population. Indian households often depend on informal social support networks for risk mitigation rather than the formal life insurance sector. This social support may not be available equally to all sections of the society. Hence, life insurance assumes an important role in ensuring the financial well-being of a large section of the population.

One of the interesting aspects of life insurance industry in India is the prevalence of a wide network of insurance agents, many of them employed by the largest life insurance company (Life Insurance Corporation of India, LIC)⁸. These agents are often drawn from within the local population and serve a large population of financially unsophisticated customers in pursuing their financial goals. Most life insurance policies sold in India are not term-life policies but rather investment-linked policies, usually with modest returns. Since life insurance is used for risk cover as well as a means of

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savings and investment, its demand depends on the changing financial resources and needs of a family.

While there is significant mis-selling of life insurance, investment-linked life insurance policies do serve a useful role in Indian society by providing access to investments with a reliable institution, protection of these investment plans and premiums from the exigencies of daily life as well as demands from extended family members.

Empirical studies in the research literature of insurance demand in households have typically used cross-sectional data. There are few studies that have looked at the temporal changes in life insurance demand within the same household. Models based on data that track changes in insured status within the same household might avoid the problem of omitted variable bias and provide an insight into the dynamic determinants of insurance demand.

With that aim, in this study, we attempt to study the *changes* in demand for life insurance within the same household over time. We use a short panel dataset from the Indian Household Development Survey which includes 1503 villages and 971 urban neighborhoods across the country, surveyed in 2004-05 and 2011-12. We are interested in both the acquisition as well as the discontinuation of life insurance coverage. We build logistic regression models to estimate the probability of uninsured households acquiring life insurance, and of insured households dropping life insurance coverage.

We also build models to understand the factors that affect the total expenditure on insurance by a household. While we did not have access to the policies bought and the coverage under these policies, we did have data for total expenditure on insurance premiums. This gives us an idea of the differing demand for insurance in different households. 10

Socio-economic factors such as the socio-economic status of the household, changes in financial conditions, financial inclusion (such as getting a bank account or taking a bank loan); as well as demographic factors such as gender of the household head, education levels of the head and increase in family size are found to be correlated with the probability of acquiring or discontinuing life insurance. Urban households tend to have a larger probability of acquiring life insurance than rural households. However, the effect of financial status on insured status is stronger in rural households than in urban households.

Objectives of the Study

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The primary focus of this research was to understand decisions to purchase insurance from a consumer behavioral perspective. Four studies have been conducted to understand the life insurance purchase behaviors among Indians. These four studies are based on the following four themes:

- (i) Understanding the effect of several socio-economic and demographic factors on life insurance demand,
- (ii) Understanding the process of life insurance purchase decision using the theory of planned behavior,
- (iii) The effect of different purchase motives on choice of different kinds of life insurance products and
- (iv) The effect of purchase motives on life insurance policy lapse.

Review of Literature

Consumer choice in the life insurance sector has been studied extensively in the last five decades. Studies have examined various factors, including socioeconomic, demographic and psychographic factors that might affect life insurance demand. In this section, we discuss some of the more recent empirical papers that have looked at socio-economic and demographic determinants of insured status.

Several studies look at macroeconomic variables that may affect the demand of life insurance. These studies give an insight into the aggregate demand for insurance in entire economies. However, they do not provide an insight into factors affecting decision making by individuals or households. A review of 13 such macro-econometric studies is given by Schlag (2003). We do not include these studies in the following literature survey because while they provide an aggregate view of the market, they do not shed light on the large variations among different sections of the society within a given country.

Zietz (2003) presented a comprehensive and detailed survey of the empirical literature over five decades. Among the papers that she reviewed, age, income, education, marital status, family size and occupation were among the most significant determinants of life insurance demand. Higher levels of income and education as well as family size were mostly found to be positively related, while the life insurance premiums and having other avenues of social security were negatively related to life insurance demand. Zietz also pointed out that some of the studies found conflicting and contradictory results for certain determinants of life insurance demand such as age and family size.

For Germany, Hecht et al. (2010) found that marital status, number of children, financial literacy and number of dependents all have a positive impact on life insurance demand. *Ulbinaitet al.*

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(2013) showed that demographic characteristics and socioeconomic factors have a significant impact on life insurance purchase decisions in Lithuania. They found that families without children take into account a wide range of factors for choosing a life insurance policy and families with children consider only a few factors.

In Malaysia, Annamalah (2013) found that income and education are positively related to life insurance demand while age, number of children, occupation and working spouse were found to be insignificant.

Arunet al. (2012) found that participation in micro life insurance is positively correlated with the number of children or dependents in the household indicating a possible bequest motive. They also found that financially better off households participate more in micro-life insurance than their poorer counterparts.

In the Indian context, individual characteristics of life insurance policy holders and choice of life insurance products have been the main focus of the research on life insurance purchase.

Bodla and Verma (2007) found that middle-aged individuals dominate the rural life insurance market; insurance sales agents are important sources of information and influencers for taking life insurance; and a money-back policy is the most preferred policy in rural areas, followed by endowment policies.

Kakar and Shukla (2010) used NSHIE9 and IFPS10 data for 2004-05 and built logistic models for a cross-section of Indian households to understand factors affecting life insurance demand. This study used both directly measurable variables (from NSHIE data) as well as latent traits such as attitudes towards future financial security and propensity to save etc. (from IFPS data). They report that insured households tend to be well off economically, have higher levels of education, have a chief earner who is salaried, and tend to be more optimistic about their financial future. Our work differs from Kakar and Shukla (2010) in that we do not use latent traits, and in that our data is for two different points of time, i.e., we are able to follow and model changes in insured status of individual households.

Several studies have used a static framework to understand variances in demand for life insurance across individuals and households. Few studies have looked at changes in life insurance demand by the same individual or within the same household. We cite two such studies below.

Liebenberg et al. (2012) used panel data from the Survey of Consumer Finances (SCF) with data over the period of 1983-89. They found a significant relationship between life events and life insurance demand. In particular they found that events such as marriage, birth of a child, starting a

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new job and income growth are positively related with acquiring a life insurance policy or increasing coverage on previously purchased policy. Death of spouse, separation and becoming unemployed contribute toward terminating life coverage.

Heoet al. (2013) used data from the 2004, 2006 and 2008 National Longitudinal Survey of Youth (NLSY) 1979 cohort in the USA and found that an increase in net worth was associated with increases in life insurance consumption. They also found that women and black individuals increased their life insurance consumption over the period of the study. Finally, they concluded that life insurance acts as a complement to rather than a substitute for wealth.

Socioeconomic and Demographic Factors which effects life Insurance Demands

Life insurance has low penetration among Indian households, with insurance premiums accounting for about 2.72 % of GDP⁷. Due to lack of access to formal financial markets and low levels of financial literacy many Indian households do not effectively plan their financial future. With an increasing emphasis by the government towards greater financial inclusion of all sections of the society, it is important to understand how socio-economic and demographic aspects of rural and urban households affect their decisions to acquire or discontinue life insurance coverage.

Though life insurance is primarily a means of mitigating financial risks associated with premature death, it is mostly used as a tool for savings and investment through endowment policies in India. Social security or government pension schemes are accessible only to a small part of the population. Indian households often depend on informal social support networks for risk mitigation rather than the formal life insurance sector. This social support may not be available equally to all sections of the society. Hence, life insurance assumes an important role in ensuring the financial well-being of a large section of the population.

One of the interesting aspects of life insurance industry in India is the prevalence of a wide network of insurance agents, many of them employed by the largest life insurance company (Life Insurance Corporation of India, LIC)⁸. These agents are often drawn from within the local population and serve a large population of financially unsophisticated customers in pursuing their financial goals. Most life insurance policies sold in India are not term-life policies but rather investment-linked policies, usually with modest returns. Since life insurance is used for risk cover as well as a means of savings and investment, its demand depends on the changing financial resources and needs of a family.

While there is significant mis-selling of life insurance (see Halanet al. (2014)), investment-linked life insurance policies do serve a useful role in Indian society by providing access to

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investments with a reliable institution, protection of these investment plans and premiums from the exigencies of daily life as well as demands from extended family members.

Empirical studies in the research literature of insurance demand in households have typically used cross-sectional data. There are few studies that have looked at the temporal changes in life insurance demand within the same household. Models based on data that track changes in insured status within the same household might avoid the problem of omitted variable bias and provide an insight into the dynamic determinants of insurance demand.

Socio-economic factors such as the socio-economic status of the household, changes in financial conditions, financial inclusion (such as getting a bank account or taking a bank loan); as well as demographic factors such as gender of the household head, education levels of the head and increase in family size are found to be correlated with the probability of acquiring or discontinuing life insurance. Urban households tend to have a larger probability of acquiring life insurance than rural households. However, the effect of financial status on insured status is stronger in rural households than in urban households.

Research Hypothesis

H1: Household head's age has a positive impact on life insurance acquisition

H2: Household head's age has a negative influence on life insurance discontinuation

H3: Education of the household head has a positive impact on life insurance acquisition.

H4: Households with a male head are more likely to buy life insurance than households with a female head.

H5: Urban households are more likely to purchase insurance as compare to rural households.

H6: Households in higher SEC have higher probability of buying life insurance and low probability of discontinuation.

The objective of this study is to understand how individuals form an intention to purchase life insurance in India. Purchase intention (or actual behavior) is a function of individual's attitude (extent to which life insurance purchase is evaluated either positively or negatively) toward life insurance, perception of the social norms on purchase decision and individual's control over the purchase decisions. We also hypothesize that individual attitude, subjective norms and perceived behavioral control is influenced by individual's belief (evaluation of consequences of buying or not buying life insurance) towards life insurance policy. Based on the prior literature on Theory of Planned Behavior (Ajzen, 1985) and its application in insurance decisions (Fletcher and Hastings, 1983, 1984; Omar and Frimpong, 2007 and Kurland, 2009) we formulate the following hypotheses:

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H1: Beliefs towards life insurance significantly influence attitude towards life insurance.

H2: Beliefs towards life insurance significantly influence subjective norms about life insurance purchase.

H3: Beliefs towards life insurance significantly influence individual's perceived behavioral control over the life insurance purchase.

H4: Individual's attitude towards life insurance has a significant impact on life insurance purchase intention.

H5: Subjective norms significantly affect life insurance purchase intentions.

H6: Perceived behavioral control has a significant impact on life insurance purchase intention.

Research Methodology

Data

The data used in this research was collected by the National Council of Applied Economic Research (NCAER) through the Indian Human Development Survey (IHDS). As per the description of the data that is available from the IHDS website, the data represents a multi-topic survey of 1503 village and 971 urban neighborhoods across India. The first round of survey was conducted in 2004-05 and included 41,554 households. In the second round of the survey 16 most of these households were re-interviewed in 2011-12. However, with the addition of some new households the second round includes 42,152 households.

The survey gathered information on a wide range of socio-economic topics including family structure, poverty, employment, income, consumption expenditure, ownership pattern, and fertility data and so on. The rural sample was drawn using stratified random sampling and the urban sample was a stratified sample of towns and cities within states selected by probability proportional to population (PPP).

Structural Equation Modeling of the Behavioral Intention Model

(Empirical Analysis uses AMOS model 21)

We use Structural Equation Modeling (SEM) for testing our structural model and hypothesized relationships among model constructs. We use IBM AMOS 21 for the analysis. Structural equation modeling (SEM) is a multivariate modeling technique that allows estimation of a series of multiple regression equations estimated simultaneously (Hair *et al.* 2013).

It consists of two basic components:

- (i) The structural (path) model and

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- (ii) The measurement model. The measurement model allows the researcher to measure a latent construct using several indicator variables. The path model specifies a set of regression equations which indicate the direction of causality where the latent constructs are the independent variables that may lead to a certain dependent variable.

We use the Theory of Planned Behavior to depict the direction of causality in the structural model set up. Several different models were specified to understand the covariance structure in the data. The SEM model was estimated using maximum likelihood estimation (MLE). After several trials, we arrived at the following model that fit the data best. Describe in given

Figure 1.1.

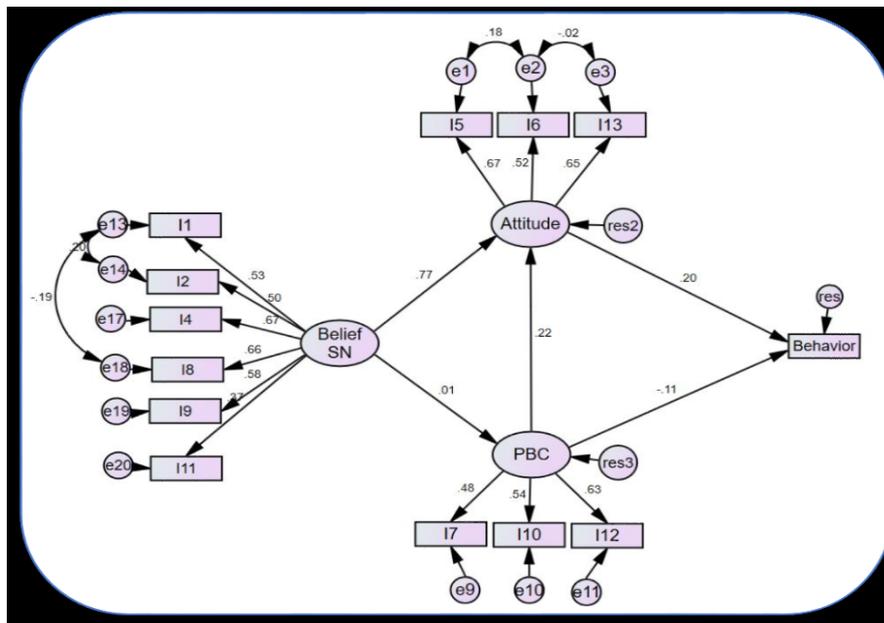


Fig 1.1-Structural Equation Model for Life Insurance Purchase Behavior

The regression Estimates of our Structural Equation Model (SEM) are given in Table 1.2. As we can see from this table, belief and subjective norms have a high positive effect on attitude towards life insurance. Perceived behavioral control affects attitude towards life insurance positively. Belief and subjective norms have positive effect on perceived behavioral control and perceived behavioral control has a negative effect on life insurance purchase behavior. But we find that these two relationships are not statistically significant. Attitude toward life insurance has a highly significant positive effect on life insurance purchase behavior.

Table 1.3 shows the direct and indirect effects of model constructs on life insurance purchase behavior. We find that belief and subjective norms have a positive indirect effect on life insurance

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purchase behavior. Perceived behavioral control has a positive indirect effect on life insurance behavior. The overall effect of perceived behavioral control on life insurance purchase behavior is negative. Attitude toward life insurance acts as a mediator between belief and subjective norms and behavior; and between perceived behavioral control and behavior.

Table 1.2

Constructs	Direction	Constructs	Estimates	Std. Estimate	p value
PBC**	Belief and Subjective Norms	0.012	0.011	0.882	
Attitude	Belief and Subjective Norms	0.906	0.767	0.000	
Attitude	PBC	0.248	0.217	0.007	
Behavior	Attitude	0.081	0.195	0.003	
Behavior	PBC	-0.05	-0.105	0.134	

PBC.- Perceived Behavioral Control**

Table 1.3 Direct, Indirect and Total Effects

Table 1.3 Direct, Indirect and Total Effects Constructs			Belief and Subjective Norms			Perceived Behavioral Control			Attitude		
Direct Effect	Indirect Effect	Total Effect	Direct Effect	Indirect Effect	Total Effect	Direct Effect	Indirect Effect	Total Effect	Direct Effect	Indirect Effect	Total Effect
PBC		0.011	0		0.011	0		0	0		
Attitude		0.767		0.002		0.769		0.217		0.217	
Behavior	0	0.149	0.149	-0.105	0.042	-0.063	0.195	0	0.195		

Proposed Hypotheses – Acceptance or rejection

The hypotheses proposed are reiterated below with the results from our model to support or reject the hypotheses.

H1: Beliefs towards life insurance significantly influence attitude towards life insurance. We

find support for this hypothesis and conclude that beliefs do affect attitudes.

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H2: Beliefs towards life insurance significantly influence subjective norms about life insurance purchase. Beliefs and Subjective norms are in fact identified as one factor. Hence, they are highly correlated to each other.

H3: Beliefs towards life insurance significantly influence individual's perceived behavioral control over the life insurance purchase. We fail reject null hypothesis since the effect of beliefs on PBS is statistically not significant.

H4: Individual's attitude towards life insurance has a significant impact on life insurance purchase intention. We find that attitude does have a statistically significant effect on behavior.

H5: Subjective norms significantly affect life insurance purchase intentions. Subjective norms do affect behavior; however, this effect is indirect, through attitude.

H6: Perceived behavioral control has a significant impact on life insurance purchase intention. We fail to reject the null hypothesis since the effect is statistically not significant.

Goodness of fit of the SEM model

Several fit indices are used to measure the goodness of fit of the SEM model. There is some debate about having single threshold values that determine the goodness of fit of a certain model (see Barret, 2007). Hu and Bentler (1999) recommend some a cutoff value of 0.95 for TLI, IFI, RNI and CFI and a value close to 0.06 for RMSEA and SRMR <0.06. Since our sample size is greater than 250, we expect fewer Type II errors. The goodness of fit values for the estimated model is listed in Table1.4. As we can see the RMSEA value for the model is really low with acceptable values for other fit indices (greater than 0.9). Thus, we conclude that our model has acceptable fit.

		Results from SEM Model	Recommended Threshold Values
NFI	Normed Fit Index (NFI)	0.855	>0.9
RFI		0.801	
IFI	Incremental Fit Index	0.909	
TLI	Trucker Lewis Index	0.872	>0.8
CFI	Comparative Fit Index	0.907	>0.9
SRMR		0.052	<0.05 - 0.08
GFI	Goodness fit Index	0.95	>0.9

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AGFI	Adjust Goodness of Fit Index	0.92	>0.9
PGFI		0.595	
RMSEA	Root Mean Square of error Approximation	0.061	0.05-0.1

Table 1.4 Model Fit Summary

Discussion

The main objective of this study was to build a model to understand how consumers formed the intention to purchase life insurance. We used the Theory of Planned Behavior as the underlying theoretical model to test how beliefs about insurance, subjective norms, attitudes and perceived behavioral control affected the behavioral intention and finally the behavior of purchasing insurance. We collected primary data from 386 respondents using a questionnaire which had several questions which tried to measure these latent constructs. Exploratory factor analysis indicated that the questions for beliefs and subjective norms loaded on the same factor. That is in the Indian context, beliefs about insurance were completely correlated with subjective norms. A structural equation model was built that indicated that beliefs and subjective norms together had a large effect on attitudes, while perceived behavioral control had a smaller effect on attitude. Attitude had some effect on behavioral intention - but the effect size was not large. Our results show that belief and subjective norms have statistically significant and positive effects on attitude and perceived behavioral control. This indicates that social influences and perception of important referents are very important in life insurance purchase decisions among Indians. Social influences and opinions of the important referents affect the individual attitude towards life insurance products as well as perceived behavioral control which in turn affect the overall decision to buy or not to buy life insurance policies. Our findings suggest that Life insurance decisions in India are more of collectivistic decisions rather than individual decisions. Greater awareness regarding the use, benefits and kind of life insurance policies might affect the level of social influence. This would help in increasing Life insurance penetration among Indian consumers especially, among marginalized and poor ones.

Limitation of the Study: We have used theory of planned behavior to understand life insurance decision making in India which takes into account intention as a proxy for actual behavior. In actual situation individual behavior may differ from intended behavior due to financial and other constraints. This is a limitation of the study which can be addressed in future research.

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Conclusion

We have studied several aspects of life insurance demand in India. We were interested primarily in understanding the consumer behavior associated with life insurance purchase decisions in the Indian context. We studied how individuals made a decision about purchasing insurance, how they made choices about the kind of insurance policy they choose and also the reasons behind why some of the insurance owners let their policies lapse.

First, in order to get an understanding of the dynamics of insurance demand in India, we were interested in seeing which socioeconomic and demographic factors affect changes in life insurance demand within a household. While there have been several studies that have looked at cross-sectional data to analyze household demand for life insurance – i.e. static models, there have been few studies that have looked at changes in insurance consumption. We used a large household level dataset of 34,885 households based on the Indian Human Development Survey which was conducted in two waves in 2004 and 2011. We were interested in the factors that affect the probability of acquisition of insurance or discontinuation of insurance. For the independent variables, we built a derived variable called SEC class which indicated the socioeconomic class that the household belonged to, based on the level of education of the head of the household and the assets owned. We also built a derived variable that indicated whether a household was poor based on a threshold level of consumption. Separate logistic regression models were built for rural and urban households. Results from these models indicated that variables related to the financial condition of the household (socioeconomic status, the poverty indicator and changes in reported income) were the most important predictors that indicated whether the household would acquire insurance or discontinue coverage. Among the demographic variables we found that family size, the gender and education of the household head affected the probability of acquiring, insurance. In terms of financial inclusion, households that had bank accounts or had taken bank loans were more likely to be insured. Models for insurance expenditure yielded similar insights.

In the second study, we were interested in investigating the factors that affect the attitudinal factors that affect consumer behavior with regard to purchase of insurance. For this part of the study, we used the Theory of Planned Behavior which proposes that beliefs, attitudes, subjective norms and perceived behavioral control affect behavioral intention which affects the actual behavior which in this case is the purchase of insurance.

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