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## Underinsurance in life insurance industry: A global perspective

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**Abstract**

Underinsurance is a challenge the life insurance industry faces worldwide. It has great implications for financial security and economic resilience. This article discusses the concept of underinsurance in multiple dimensions, exploring its global prevalence and incidence in India. It identifies some critical reasons for underinsurance such as lack of awareness, and economic constraints and it also outlines the consequences of underinsurance. Key strategies are suggested to reduce underinsurance which include collaborative awareness campaigns, leveraging social media, and the introduction of tools to assess life insurance adequacy. Periodic reviews of life cover, insights from measures adopted in other countries, and innovative solutions like customized term plans with health insurance coverage and digital transformation using AI to make the buying process simpler have been emphasized. This article concludes with a note that underinsurance reduction is a shared responsibility of stakeholders and a means to encourage the culture of adequate life insurance coverage.

**Keywords:** Underinsurance, mortality protection gap, inclusive insurance, technology integration

**1. Introduction**

The financial well-being of households is most important for societies as well as countries in the world. Life insurance as a risk management tool, absorbs financial shocks and helps households maintain their living standards. The mortality protection gap is measured as the difference between the incomes required to maintain the living standard and resources readily available to a household, in case of any unfortunate event like premature death of the breadwinner. Life Insurance as a financial planning tool, should provide adequate financial support to maintain the living standard of households, but the question here is: Are we adequately covered?



**Source:** Swiss Re Asia Pacific 2015-Mortality Protection Gap Report

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**1.1 Concept of Underinsurance**

The mortality protection gap arises due to both uninsured and underinsured. Underinsurance is the inadequate insurance coverage of the financial needs of the policyholder's family. The individuals who have not taken the insurance know that they are not insured against any potential adverse event, but many individuals who have taken the life insurance don't know whether their insurance coverage is sufficient or insufficient for the family to handle any financial shock. As an earning member of the family, most of the individuals are not aware of the amount of life cover for which they have to be insured.

There are various approaches used by the life insurance industry to calculate the life cover such as: Multiplier approach, Human Life Value approach (HLV), Need-Based approach, Income Replacement approach, and Capital Retention approach. The general public is not aware of these approaches and most of the time they end up with an insufficient life cover. Underinsurance has been identified as a common problem across countries and can have serious consequences. For example, Bernheim *et al.*, (2003) <sup>[2]</sup> showed that under-provision of life insurance is one of the most common causes of poverty amongst widows in the USA, while MetLife (2009) <sup>[11]</sup> indicates that most widows whose deceased spouses were underinsured had had to make significant lifestyle adjustments. One Path (2010) <sup>[12]</sup> demonstrated the devastating effect of inadequate life cover on the surviving spouse and children.

In this conceptual study, we discussed about the underinsurance in the life insurance industry in the global and national level, the reasons for the underinsurance and possible solutions to reduce underinsurance.

## 2. Materials and Methods

### 2.1 Underinsurance in Global level

According to the Swiss Re sigma No. 5/2019 report, globally only 45% of the funds needed to maintain household living standards in the event of the death of the primary breadwinner are protected by either life insurance, social security survivor benefits or household savings. The remaining 55% is the global mortality protection gap. The estimated mortality protection gap of the Asia-Pacific region was about USD 83 trillion in 2019 and this gap is widening year on year. As per Swiss Re, the US has a \$25 trillion mortality protection gap, three in ten households had no life cover. According to the Fin Health Spend Survey 2023, nearly 40% of Americans lack any life insurance coverage as of 2022. In Africa, the life insurance penetration rate is at an average of 3 percent of the GDP. In Nigeria, Africa's most populous country only less than 1 percent of the population have life insurance. In Europe, the level of inadequacy in Eastern European countries like Romania, and Bulgaria is high when compared to Western European countries like the UK, Germany, France and Netherlands.

**Table 1:** Mortality Protection Gap

SL. No	Countries	Total Mortality Protection Gap 2019 (USD Trillion)	Gap as a share of total protection need	Closing the gap: Additional life premium opportunity 2020-2030 (USD billion)
1.	China	40.6	70%	160.4
2.	India	16.5	83%	78.2
3.	Japan	8.4	61%	17.2
4.	South Korea	3.9	55%	9.7
5.	Australia	2.8	54%	9.1
6.	Indonesia	2.0	76%	8.5
7.	Thailand	0.9	71%	2.9
8.	Malaysia	0.7	74%	3.1
9.	Singapore	0.6	55%	1.5
10.	Hong Kong	0.4	41%	1.6

**Source:** Swiss Re - Closing Asia's mortality protection gap, July 2020

The Table 1 shows the mortality protection gap as a percentage of protection needs, the percentage is the highest (83%) in India followed by China (70%) and Indonesia (76%) and it is lowest in Hong Kong (41%). The table also illustrated the additional premium opportunities of insurance providers for about 160.4 billion USD in China and 78.2 billion USD in India.

### 2.2 Underinsurance in national level

According to the Swiss Re Institute Sigma No.4/2022 report, households in India are exposed to a larger protection gap of 83% of the total protection needed, which is at USD 17 trillion in 2019. India has the highest protection gap because the growth in savings and life insurance coverage is lagging behind economic and wage growth. According to IRDA reports, the average Indian is insured for only 8% of what is required for the protection of the family in case of any unfortunate demise of the breadwinner.

### 2.3 Reasons for Underinsurance

- **Lack of awareness:** The awareness among the public is very low, concerning the reason for purchasing life insurance and the amount of life cover they should avail. Most of the people in India are considering insurance as an investment, which makes them take up a life insurance product with inadequate life cover.

- **The nonavailability of tools to measure underinsurance:** LIMRA 2022 Insurance Barometer study states that one of the important reasons for the mortality protection gap is that people are not sure how much life cover they need. If an individual wants to know the right life cover for which he/she should be insured, they may ask the agent/distributors of insurance providers or search online. These agents or online portals will give a number for which they have to be insured, but is there any source to check whether this number is correct? The answer is no. Many personal finance-related online portals and websites of life insurance providers have life cover calculators and unfortunately, these life cover calculators are using different methodologies and are giving different life cover for an individual. The difference in the life cover provided by these portals ranges from several lakh to crore. This is misleading the potential life insurance policyholders and resulting in underinsurance.
- **The complexity of the products:** The complexity of the life insurance policies and the jargon used in the contracts discourage potential buyers from understanding the products. This not only leads to the purchase of inappropriate life insurance products but also leads to the delay or avoid purchasing life insurance.

- **Economic Constraints:** In many developing countries in the world, people's low income and high living expenses limit their ability to purchase life insurance products with appropriate life cover. Many people in India are opting for plans with both protection and investment features such as endowment plans and Unit-linked plans, which are leading to reasonably high premiums and low life cover.
- **Not adapting to changing circumstances:** The life cover requirement of an individual changes from time to time. As the earnings and responsibilities of the individual change, the life cover has to be updated accordingly. Most of the people after purchasing the life insurance plan, are not reviewing the life cover periodically to know whether the life cover would be sufficient for the family to manage any unfortunate event.

## 2.4 Consequences of Underinsurance

- **Insufficient Compensation:** Due to inadequate life coverage, the family of the deceased person may have to undergo financial hardships like paying off the debts, replacing the lost income etc.,
- **False sense of security:** Underinsurance may give a false sense of security to the policyholders, which can be even worse than not having any protection. Only after the occurrence of any unfortunate event, the family will realize that the life cover is not sufficient to them for their children's education, household expenses etc.,
- **Emotional Stress:** The lack of financial security amplifies emotional distress among dependents during already challenging times.
- **Societal Impact:** A widespread lack of adequate life insurance at the global level can lead to broader economic instability as families struggle with unexpected financial burdens.

## 3. Results and Discussions

### 3.1 Measures to reduce underinsurance

- **Enhancing financial literacy:** Many individuals do not fully understand the purpose of life insurance and the importance of adequate coverage. Governments, insurers, and educational institutions can make collaborative efforts to promote financial education and awareness about the importance of life insurance.
- **Providing appropriate tools to calculate life cover**  
The Australian government has a website [moneysmart.gov.au](http://moneysmart.gov.au) which helps citizens with various personal finance-related needs like managing money, reducing debt, financial planning for the future, growing wealth etc., In this portal, they provided a life cover calculator which enabled the Australians to calculate the appropriate life cover. Likewise, governments of various countries can provide such financial planning websites for their citizens to reduce the level of underinsurance. In India, IRDAI can provide such a life cover calculator in their portal, so that the people can know about the right life cover for which they have to be insured.
- **Product customization:** The National Insurance Academy Report 2023 offered the following suggestions to reduce underinsurance in the Indian life

insurance sector. The lower income protection gap can be addressed by micro-insurance schemes and PM

- **Jeevan Jyoti Bima Yojana (PMJJY) scheme.** The middle-income protection gap can be reduced through savings and investment products coupled with term insurance. The higher income group with higher education and better awareness can be offered high-value term insurance bundled with annuity and wellness insurance plans. People working in unorganized sectors and business owners have lower awareness, customized products under group insurance schemes can be offered to these segments.
- **Promotion of Term Insurance:** Term insurance products are a pure risk-covering tool, which can offer high life cover with a reasonably low premium. Hence, the promotion of term insurance products can reduce underinsurance to a great extent. With this objective, IRDAI issued a circular in 2020 for all insurance providers to offer a pure-term plan known as Saral Jeevan Bima Yojana. This plan can have a maximum sum assured of 25 lakh rupees and can be accessed by all segments of the community. Promotion of such products by insurance providers can reduce underinsurance.
- **Technology integration:** Digital platforms and mobile technology can enhance the accessibility of life insurance products in remote areas. Three major categories of digitization changes in the insurance sector were proposed by Eling and Lehmann (2018): new technologies such as chatbots, robo-advisers, and social media can alter the way insurers and customers interact. Business processes like online sales and digital claim settlement can be made more efficient and effective by automating, standardizing, and utilizing new technologies. The development of new products like cyber insurance and the modification of current ones like on-demand insurance are made possible by new technologies. The efficient use of digital technology can bring more young people into life insurance, which in turn would reduce underinsurance.
- **Inclusive Insurance:** This term encompasses different approaches to reach under-served, unserved, vulnerable and low-income populations with appropriate and affordable insurance products. The strategies to serve this market would be through simplifying the products, leveraging the digital channels and using InsurTech innovations. The new initiatives of IRDAI such as Bima Vahak will identify and develop local resources, especially women, as trusted intermediaries, who understand and cater to the unique needs of their communities. Such intermediaries would be instrumental in the distribution and servicing of insurance products and hence, promote financial inclusion and empowerment of the rural population.
- **Hyper-personalization:** Of the product offerings as well as journeys can be delivered through automation, AI as well as analytics. AI and behavioral analytics are enabling the carriers to provide hyper-personalized interactions for the customers besides providing solutions tailored to their particular needs. These have included every possible convenience such as the preferred mode of call during a preferred period, mode of payment, etc., all these serve to increase response and customer stickiness with the insurance providers.

#### 4. Conclusion

Underinsurance in the life insurance industry is a pressing global challenge that demands immediate attention. Addressing this issue requires collaboration among stakeholders, including governments, insurers, and civil society. By fostering financial inclusion, enhancing awareness, leveraging innovation, simplifying and personalizing product offerings, promoting term insurance, integrating technology and ensuring that agents prioritize client welfare over commissions, the global life insurance industry can move closer to ensuring that every individual and family has the protection they need to face life's uncertainties with confidence. By narrowing the coverage gap, the industry can not only improve financial security for families but also fulfill its social responsibility to provide adequate protection against life's uncertainties.

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