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Case Report
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GoDigit: Risk Management Analysis

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Abstract

The case provides the risk management process and framework of an insurTech company - GoDigit. The company incorporated in the year 2016, based in Bengaluru, is an online platform based organisation that provides non-life insurance. The company earned a revenue of INR 93.83 crore for the financial year 2017-18. The company majorly faces four kind of risks which are Assets/Liability Management (ALM), Liquidity risk, Reinsurance risk and Operational risk. The company has a risk framework monitored by the risk management committee which formulates and regulates the risk management of the company comprising of 2 non-executive directors and the CEO & Principal officer of the company. The case studies the detailed analysis of various kinds of risks and how severe they can prove to the company.

Keywords: InsurTech; Risk framework; Risk management; GoDigit; Liquidity risk

Introduction

The company is a digital platform based venture that initiated its operations with a paid up capital of INR 350 crore on 12th October 2017. The company provides advance cash in case of any accidental damage by providing information on the online platform of GoDigit by the claimer and uploading documents and pictures of the damaged car part or area. The company also has an insurance policy for airline customers where it provides insurance to the customers whose flight gets delayed by 75 minutes. The company has operations only in one country i.e. India.

The company encounters risks of various categories that are Financial, Non-Financial and Technical.

Types of risks

The start-up faces the following risks:

- Financial Risk: Assets/Liability Management Risk; Reinsurance Risk; Liquidity Risk,
- Non-Financial Risk: Operational Risk; Geographical Risk

Risk management process

Risk identification: The insurance companies use various tools to identify the risk. The companies prepare models such as Asset Liability Management Strategies. The functional heads and the Chief Risk Officer are responsible for supervising the risk and the risks are brought to the picture of the Risk Committee.

Planning: After identifying the risk, the companies plan on how to mitigate, avoid, reduce and retain the risk. The risk management committee comprising of the top officials of the organisation manages the risk of the company.

Derive safeguards: The company has to find the solution to the problems it identifies. The company has appointed an Internal Auditor that is responsible for the auditing the key operational activities. To mitigate the various operational risks, the Boards has also approved Whistle Blower mechanism and an Anti-Fraud Policy. The Risk Committee comes up with the solution of mitigating the risks. The investment portfolio has been set up according to the IRDAI Regulations.

Monitor: The risk committee keeps on accessing the benefits and the costs which are related to the risk exposure. The internal Auditor of the company carries audits on the investment functions of the company which is reported to the Audit Committee every quarter.

Risk management framework

The risk management framework is clearly to identify, measure and mitigate the risks that the company is or might get exposed to he risk management committee forms. The company has formed an internal risk management committee comprising of three people 2 independent directors and the principal officer/CEO. The CFO and the CRO are the invitees to the meeting of the committee. The committee responsibilities are to manage and plan policies to identify, plan, deriving safeguards and monitoring risk management and takes steps in order to avoid, reduce, transfer and retain the risks.

The company being a general insurer is exposed to different kinds of risks which are:

Assets/Liquidity management (ALM): ALM can be defined as the risk which occurs due to the imbalance between assets and liabilities that can be due to the change in the liabilities or liquidity of the assets. It occurs when the company's assets are not enough to meet claim obligations arising from customer claims [1].

Reinsurance risk (Credit Risk): This risk occurs when the Reinsurer defaults i.e. when the primary insurer or the ceding company is unable to get the amount from the reinsurer at the correct time and at the appropriate cost [2].

Operational risk: This risk is related to operational procedures of a company. This also includes human error related risk, legal risk, process risk, outsourcing risk, fraud risk. A company assumes these risks in business. It is a human tendency to make mistakes which lead to financial losses. This risk also includes the chance of filing wrong information and errors in paper work [3].

Geographical risk is a risk that arises when the policies issued by an insurance company are concentrated in a geographical area, the risks will be a hurricane or earthquake [4].

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Risk analysis of GoDigit

Asset Liability Management is the process that shows that the company's funds are sufficient enough to meet its current liabilities and the other assets are feasible enough to meet other liabilities those which are bound to rise or become due. With Go Digit having its founding year as 2016 and a background of being an insurTech Company makes it a company prone to ALM Risk. The most important word to be associated with ALM Risk is "uncertainty".

The main reason Go Digit has to face ALM Risk is because the Cash Flows Generated as compared to the liabilities around the Reserves of unexpired Risks and the Current Liabilities are less. The Analytical Ratios, Cash and Bank Balances, Statement of Liabilities and Revenue Accounts, provide the insight for the ALM Risk.

Balance sheet for the year ending 2018

The main reason to identity the same is the projected Liquid Asset and Liabilities Ratio which is 54.38% (as opposed to the strength of the Liquid Assets in the Year 2017 which amounted the ratio to nearly 340%) that shows there are not enough Liquid Assets to pay up for the Liabilities the company is generating. Also, the Available Solvency Margin to the Required Solvency Margin Ratio is 5.48 that again shows a gap between the two, which will affect liquidation of the company as a whole (Table 1) [5].

The timing of the cash flows is everything in order to understand the effect of ALM Risk. There has been a Cash Flow of INR 327,118,000 as opposed to the Current Liabilities of the Year 2018 which was INR 623,213,000. There is a huge gap between the two and thus shows the rising risk of ALM in Go Digit. The fundamental goal of asset liability management is to make sure the assets at least match the liability. This slightly deviated for Go Digit in the Quarter ended as on 31st March 2018. The Financial Quarter ended as on 31st December 2017 projected a fruitful picture for the company [6].

Solution: The proposed methods of mitigating the risk are through Cash Flow Matching, asset liability modelling to evaluate alternative asset allocations, new investment strategies as opposed to the ones used previously, and alternative funding policies in order to get sufficient cash flows to attend to the liabilities arising out of coverage and assurance provided to clients [7].

Reinsurance Risk Concentration

Reinsurance risk

The risk here is Reinsurance. It is the practice of insurers transferring portions to other parties by a form of agreement to reduce the chance of paying a large obligation resulting from an insurance claim (Table 2) [8].

There are two parties involved, one diversifies its insurance portfolio is known as the ceding party and the party that accepts a portion of their potential obligation in exchange for a share of the insurance premium is called insurer.

Solution: The company is transferring their risks to good graded companies as the risk of reinsurance is transferred to AA and A graded companies [9].

Geographic risk

Geographical risk is a risk that arises when the policies issued by an insurance company are concentrated in a geographical area, the risks will be a hurricane or earthquake (Table 3 and Figure 1).

Gross direct premium written for the quarter ended 30th June 2018. The company gets its business from 13 states and union territories. The company carries geographical risk. In case of a large natural calamity in one of their main business deriving regions will lead to a large number of claims and in turn hurt their balance sheet and profitability.

Solution: The company can mitigate this risk by underwriting policies in other states and union territories for which they need to ramp up operations in other states as well. The same could be seen in the company's statement of branches. The company currently has 15 offices at the start of the year. The company also opened 3 new offices during the year which makes it a total of 18 offices. The company has approval for 12 new offices which are yet not opened. These new offices will lead to a growth in business and spread of geographical risk over a larger region.

Particulars	Schedule	2018	2017
Sources of Funds			
	NL 8 NL	35,00,000	90,000
1. Share Capital			
2. Reserves and Surplus	10	-	-
3. Fair Value Account Change		290	245
4. Borrowings		-	-
5. Deferred tax liability	NL11	2,302	141
Application of Funds			
1. Investments Shareholders Policyholders	NL 12 NL	33,04,912	26,784
2. Loans	12A NL	29,514	-
3. Fixed Assets Current Assets	13 NL 14	-	-
4. Cash and Bank Balances		50,890	1,903
5. Advances and Other Assets	NL 17 NL	3,41,542	14,424
Sub Total (A)	18	3,23,387	5,697
6. Current Liabilities		6,64,929	20,121
7. Provisions		6,23,213	20,572
Sub Total (B)		6,87,971	100
8. Net Current Assets (A)-(B)		13,11,184	20,672
9. Miscellaneous expenditure to the extent not written off		(6,46,255)	(551)
10. Debit Balance in Profit and Loss Account		-	-
		7,63,532	62,250
Total		**35,02,593**	**90,386**

Table 1: Digit, Go Digit General Insurance Limited.

S.no	State	No.of reinsurers	Premium ceded to reinsurers Non-Proportional	Premium ceded to reinsurers/Total reinsurance premium ceded (%)
1	No.of Reinsurers with rating of AAA and above	0	-	-
2	No.of Reinsurers with rating AAA but less than AAA	2	10	19.73%
3	No.of Reinsurers with rating A but less than AA	9	35	90.23%
4	No.of Reinsurers with rating BBB but less than A	0	-	-
5	No.of Reinsurers with rating less than BBB	0	-	-
	Total	**11**	**45**	**100%**

Table 2: Digit, Go Digit General Insurance Limited.

S.no	Name of Product	Class of Business	Category	Date of approval from IRDAI
1	Digit Two-Wheeler Package Policy	Motor	Retail	31-01-2018
2	Digit Two-Wheeler Package Policy Consumable Cover	Motor	Retail	08-02-2018
3	Digit Two-Wheeler Package Policy Parts Depreciation Product	Motor	Retail	08-02-2018
4	Digit Two-Wheeler Package Policy Engine & Gearbox Protect	Motor	Retail	08-02-2018
5	Digit Two-Wheeler Package Policy Return to Invoice	Motor	Retail	08-02-2018
6	Digit Asset Care	Miscellaneous	Retail	14-03-2018
7	Digit on the Move Policy	Health/Travel	Retail	19-12-2017
8	Digit Two-Wheeler Package Policy - Breakdown Assistance	Motor	Retail	08-02-2018
9	Digit Two-Wheeler Liability only policy	Motor	Retail	18-10-2017

Table 3: Digit, Public Disclosure, 2018.

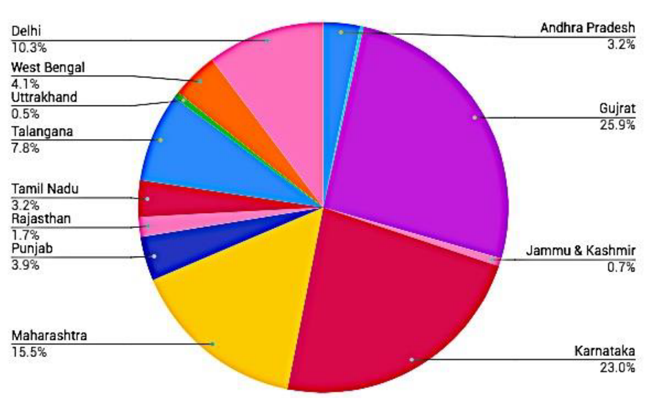

Figure 1: Digit - Geographical Distibution of Business.

Conclusion

The company's Risk Management Framework defines, identifies, derives safeguards and monitor the risks. The Risk Management System in GoDigit consists of the Board of Directors, Risk Management Committee, Chief Risk Officer, Auditors (Internal and External). InsurTech companies face Financial and Non-Financial risks, which needs to be monitored regularly and the company is doing so by regularly auditing and supervising the risks by the Auditors and the Chief Risk Officer, reported to the Risk Committee. The firm can thus be able to mitigate its Financial Risks by monitoring their cash flows with respect to their stated liabilities around reserves due to unexpired risks. The company strictly follows the norms for documentation set by IRDAI. GoDigit deals in 09 products majorly the Motor Vehicles. The company transfers the concentrated risks for now and in the future, it is expected to mitigate the diversified risks as it will open new branches across the country. The company has transferred its credit risk to the reinsurers having good credit ratings.

Suggestions

- Asset Liability Management - Change in Investment Policies and Alternative Asset Allocation with Monitoring of Operational Profit.
- Reinsurance Risk Management - The reinsurance chosen should have high credit rating in order to avoid the credit risk.

Geographic Risk Management - The company should expand the operations into different geographical location to avoid the risk of geographical concentration.

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