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JIN, Feng

Datum: 5.11.2008

Beijing Life Insurance Industry - An economic and social development perspective

Evaluation, issues and prospects

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Preface

This master thesis was submitted for obtaining the degree of master of management at the University of Hasselt in Belgium.

This thesis is a combination of my theoretical studies in Hasselt, a large amount of literature review and more than three years work experience in the life insurance industry in Beijing, China. Because of the limitation in time and financial support, it has been done mainly rely on empirical method and secondary data.

The readers of my thesis might find at some point that its content mainly focuses on secondary data rather than on my own analysis of facts and data. I want to express my apologies for this eventual weakness and hope readers can understand that the main reason for this is the difficulty of accessing and creating reliable primary data in China being most of the time in Belgium as a student. As a native Chinese with nearly four years working experience in this field, however, I certainly can give an analysis from my point of view. This has been complemented by interviews with a limited number of experts in the month of February 2008. However, future academic research and thesis in this field should be based more on in-depth data and larger surveys rather than on more general knowledge and limited expert opinion. In this sense, my thesis lays the groundwork for further exploration. For all the analysis I made, all be supposed by trustworthy data, statistic model and cautious inspection rather than simple estimation.

Moreover, the readers can find that it is so difficult for me to find, choose, extract, and condense the rudimentary and crowded information, then deduce the conclusion. Sometimes statistic model was being applied to test results and forecast the future development potential on a subject that the data is scarce.

Although I am indeed the sole author of this thesis, I am by no means the sole contributor! So many people have contributed to my thesis, without their timely help, I can not finish this difficult task.

First and foremost, I would like to express my appreciation to my thesis supervisor, Professor Wouter Faes, who has given me constructive supervision and valuable comments during this work. He devoted and sacrificed his personal time to improve my thesis, even in holiday; I never forget the feeling when I saw he replied my letter at the 6 o'clock in the morning. I am deeply grateful for his guidance, advice, encouragement, kindly help and his responsibility. To thank him in perpetuity for all that he had done for me, it is my great pleasure to have chance become his student.

I would like to give my special thanks to my previous colleagues, they provided lots of data and information for me, without them this thesis and my researches would not be possible.

And last but not least, we owe most of our thanks to our families, who have supported us with their love and passion.

Thank you very much!

Pleasant reading!

Jin Feng

Summary

Due to its large potential market and rapid growth rate, Chinese insurance industry has already become one of the most dynamic sectors in current economic structure and its healthy development has a close relationship with the economy and society. Obviously, after 27 years development, the Chinese insurance industry now enters a new phase of growth. At this moment, a thorough investigation of the development of Chinese insurance industry, through the perspective of economic and social development, is of great theoretical and practical importance.

Because China is so large and differences between regions are enormous, I have to focus on only a part of it, situated in a densely populated urban area. I thus focused our research scope on the capital, Beijing. As the capital and the center of economics and politics, Beijing is indeed representative for the life insurance market in China. Results can be used as guidance for other cities in China. The thesis focuses on the whole life insurance industry in Beijing, so it does mention the details for every insurance company separately.

This thesis is a combination of an historic overview, current analysis and future forecasting of the life insurance market in the Beijing area. The main objective of the thesis is to explore the available information and data, evaluate the current development status of the Beijing life insurance industry, find out its function and problems, evaluate its effectiveness and efficiency, discover the causes of observed problems and deduce potential opportunities. Finally I want to integrate these elements to conduct a quantitative study of future development of this market and make a qualitative assessment of the measures to be taken by both managers and government to keep the momentum going.

Finally, we can fairly accurately state that the Beijing life insurance market is growing fast but only plays a limited role on macro-economic development level. It improves economic welfare, the financial system of China and the social security system to a limited extent due to a number of limiting internal and external factors. At the same time, it has a rather low

efficiency and shows a weak profit margin. To summarize the research results, a SWOT-analysis also be used to represent current status.

In view of this analysis, it is high time for the participants on the Beijing life insurance market to finally respond to the threats and to correct some of the weaknesses in order to take advantage of the enormous potential the market presents. Basically this signifies that the direction future should take should be guided more by efficiency than by scale. The objective of a more modern life insurance industry in Beijing should indeed be the realizing of a healthier interaction between the developments of the industry on the one hand and the development of economy as well as society on the other hand. Further opening up of the market and stimulation of competition, next to the fully exploitation of the industry's function in complementing social security, optimizing economic development and enhancing social harmony, are the cornerstones of this strategy.

This represents a huge turnaround which will take years to implement. Among the major steps to be taken, some following recommendations for both insurance companies and regulator are mentioned in the end.

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Chapter 1 Introduction

In order to provide a general framework for readers, this first chapter introduces the research background and research area of this thesis. It further delimits the research and specifies the main research problems. Furthermore, the purpose of the thesis will be clearly stated.

1.1 Background and research area

Since the implementation of reform and opening policies in 1978, China has achieved a real average annual growth rate of 9.8 %, (*see table 1-1*) which makes it one of the fastest growing economies in the world. From National Bureau of Statistics of China, GDP in 2007 was equal to 24,661.9 billion Yuan and grew 11.4% versus the previous year, constituting the fastest annual growth since 1994¹.

Table 1-1 China's average annual real GDP growth

Time Period	Average Annual Growth (%)
1960-1978 (pre-reform)	5.3
1979-2007 (post-reform)	9.8
1990	3.8
1991	9.3
1992	14.2
1993	14.0
1994	13.1
1995	10.9
1996	10.0
1997	9.3
1998	7.8
1999	7.6
2000	8.4
2001	8.3
2002	9.1
2003	10.0
2004	10.1
2005	9.9
2006	11.1
2007	11.4

Source: National Bureau of Statistics of China

As one of the stabilizers of economic and social development and also one of the most important components of economic and financial system, the Chinese insurance industry has

¹ National Bureau of Statistics of China, <http://www.stats.gov.cn>

achieved tremendous development since 1980. Meantime, it has made a great positive contribution to reform, opening up and helping the modernization of China.

Actually, the “modern” insurance industry in China began in the middle of last century. The first Chinese insurance company, the People’s Insurance Company of China (PICC) was founded in 1949. However, due to Chinese special historical and political reasons, the Chinese government closed it in 1958. The Chinese insurance industry stopped its development until 1980. PICC resumed its operations only in 1980, taking advantage of its monopoly status and name recognition acquired in the beginning period. Since then, two another domestic insurance companies were established: *Ping An* and *China Pacific*, founded in 1988 and 1991 respectively. The Chinese insurance industry has since entered a period of rapid development.

Due to the rapid Chinese economic development, more open policies and its huge population, China is providing the most attractive insurance market for domestic enterprises and foreign investors in the world. All participants express a strong ambition to take a share of this “big insurance cake” in China. By the end of last year, there were 39 property insurance companies and 47 life insurance companies in mainland China.² (*See table 1-2*)

Since the American insurance association Co. Ltd. (AIA) entered China in 1992, more and more international insurance companies have entered China, especially since China entered WTO in the end of 2001. Chinese authorities have gradually loosened the restrictions for foreign investment in the insurance industry. Furthermore, in 2004 all governmental limitations were canceled, thus encouraging rapid growth of foreign investment in the insurance industry. Currently, fourteen of the 39 property insurance companies and twenty-five of 47 life insurance companies in China are domestic. The number of the foreign life insurance players on the market is thus already larger than the number of domestic insurance companies.³ Moreover, there are hundreds of foreign insurance companies waiting for a license to operate in China.

² National Bureau of Statistics of China, <http://www.stats.gov.cn>

³ National Insurance Regulatory Committee (CIRC), <http://www.circ.gov.cn>

Table 1-2. The major insurance companies in China

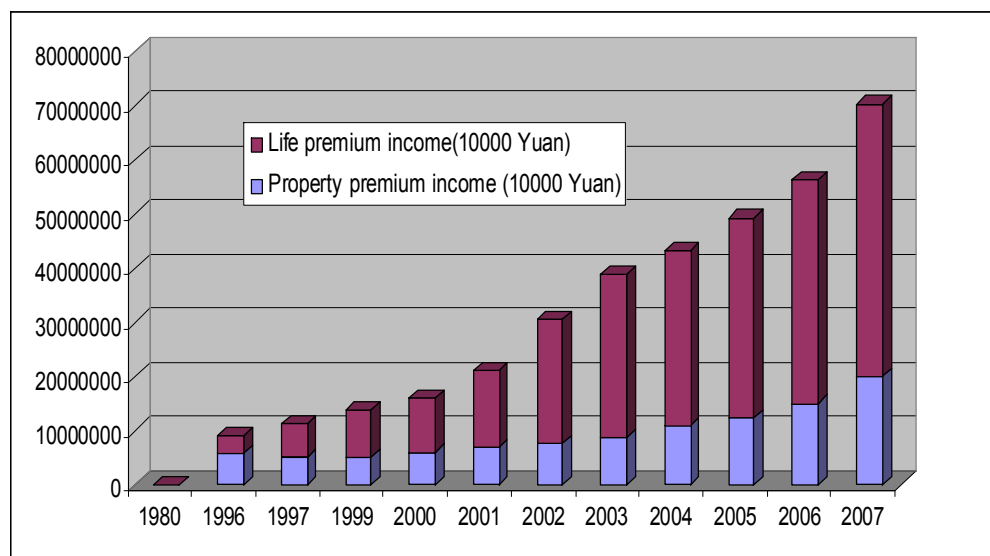
DOMESTIC	Number of Branches Nationwide	Outside Owners
China Life Insurance Limited	35	Public Investors
China Pacific	32	Currently none
Minsheng Life	Beijing, Hangzhou, Nanjing, Shijiazhaung	Currently none
NCL	29	Meiji Life, Zurich Financial
Ping An	35	Dai-ichi Life, Goldman Sachs, HSBC, Morgan Stanley
Sino Life	Shanghai Planned: Beijing, Nanjing, Hangzhou	Milea Group
Taikang Life	23	Winterthur
Taiping Life	15	Fortis
FOREIGN (Joint Venture)	Operating Currently	Operation Planned
AIG (wholly owned)	Beijing, Guangzhou, Shanghai, Shenzhen, Suzhou Sub-branches: Foshan, Dongguan, Jiangmen	
Aegon-CNOOC	Shanghai	
Allianz Dazhong	Shanghai	Beijing, Guangzhou
AVIVA-COFCO	Guangzhou	Beijing, Chengdu
AXA-Minmetals	Guangzhou, Shanghai	
China Life CMG	Shanghai	
CIGNA & CMC	Shenzhen	
CITIC Prudential	Beijing, Guangzhou	
Citi (Travelers)	Shanghai	
CNP	None yet	
Generali China	Beijing, Guangzhou	
Haker New York Life	Shanghai	
Heng An Standard	Tianjin	
ING Capital	Dalian	
John Hancock Tianan	Shanghai	
Manulife-Sinochem	Beijing, Guangzhou, Shanghai	
Nissay-SVA	Shanghai	
Pacific-Aetna (ING)	Beijing, Shanghai	
Sino-US Metlife	Beijing	
Skandia-BSAM	Beijing	
Sun Life Everbright	Beijing, Tianjin	

Source: China's insurance market- The giant awakens

With the rapid increase of insurance companies, insurance premiums have experienced a rapid development since 1990 as well. Moreover, the growth became much faster since 2000.

In 2007, the national premium income had reached 703.58 billion Yuan, up 25% over the amount in 2006, and nearly 4 times of the amount in 2000⁴. (See figure 1-1)

Figure1-1 Insurance premium income in China

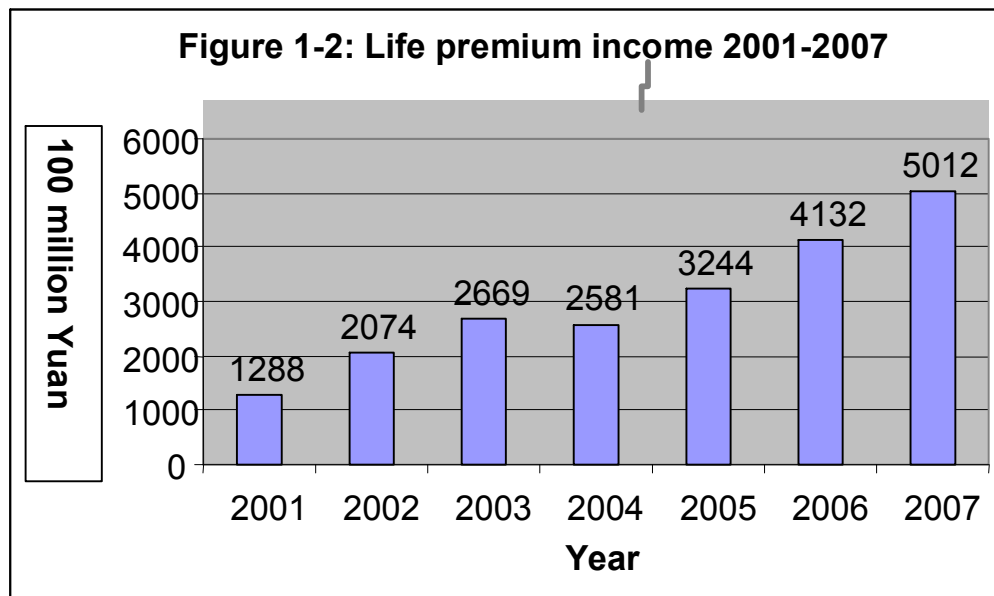


Source: National Insurance Regulatory Committee, <http://www.circ.gov.cn>

Property insurance premium increased from 68.8 billion Yuan to RMB 199.7 billion Yuan during 2001-2007, an annual growth rate of 19.7 %; Comparing to property insurance, life insurance is growing faster. Life insurance premium increased from 128.8 billion Yuan to RMB 501.2 billion Yuan during 2001-2007, an annual growth rate of 24.5 %⁵. (See figure 1-2)

⁴ National Insurance Regulatory Committee (CIRC) , <http://www.circ.gov.cn>

⁵ National Insurance Regulatory Committee (CIRC) , <http://www.circ.gov.cn>



Source: National Insurance Regulatory Committee, <http://www.circ.gov.cn>

Due to its large potential market and rapid growth rate, Chinese insurance industry has already become one of the most dynamic sectors in current economic structure and its healthy development has a close relationship with the economy and society. Obviously, after 27 years development, the Chinese insurance industry now enters a new phase of growth. At this moment, a thorough investigation of the development of Chinese insurance industry, through the perspective of economic and social development, is of great theoretical and practical importance.⁶

1. 2. Delimitation

This thesis only focuses on the Chinese life insurance industry, not only because life insurance industry has a larger market potential and faster growth rate than the property insurance market, but also because of the fact that if we want to give an in-depth overview of both main components of the Chinese insurance market, this research would become too complex in terms of time and length. Thus we opted for in-depth research of one market element only rather than staying with a general introduction of both components.

⁶ China insurance industry development research

Because China is so large and differences between regions are enormous, we also have to focus on only a part of it, situated in a densely populated urban area. We thus focused our research scope on the capital, Beijing. As the capital and the center of economics and politics, Beijing is indeed representative for the life insurance market in China. Results can be used as guidance for other cities in China.

The thesis focuses on the whole life insurance industry in Beijing, so it does mention the details for every insurance company separately.

1.5 Objective of this thesis

This thesis is a combination of an historic overview, current analysis and future forecasting of the life insurance market in the Beijing area. The main objective of the thesis is to explore the available information and data, evaluate the current development status of the Beijing life insurance industry, find out its function and problems, evaluate its effectiveness and efficiency, discover the causes of observed problems and deduce potential opportunities. Finally I want to integrate these elements to conduct a quantitative study of future development of this market and make a qualitative assessment of the measures to be taken by both managers and government to keep the momentum going.

1.6 Research problem definition

To achieve the objectives mentioned above, this thesis tries answering the following research questions:

1. *What is the current status of the life insurance market in Beijing?*
2. *How does the life insurance industry influence economic development and maintain social stability?*
3. *What are the obstacles for the development of life insurance market in Beijing?*
4. *What are the opportunities and threats for further development?*
5. *What is the growth potential of Beijing life insurance industry ?*
6. *To which extent can it be achieved in the future?*
7. *Which preconditions have to be met to achieve this development?*

In order to answer questions 1 and 2, I will give a comprehensive introduction into the Beijing life insurance industry, and then implement a more systematic assessment to find out the relationship between life insurance industry development and social and economic development. In this evaluation process, descriptive empirical analysis, theoretic analysis, and statistical analysis will be used.

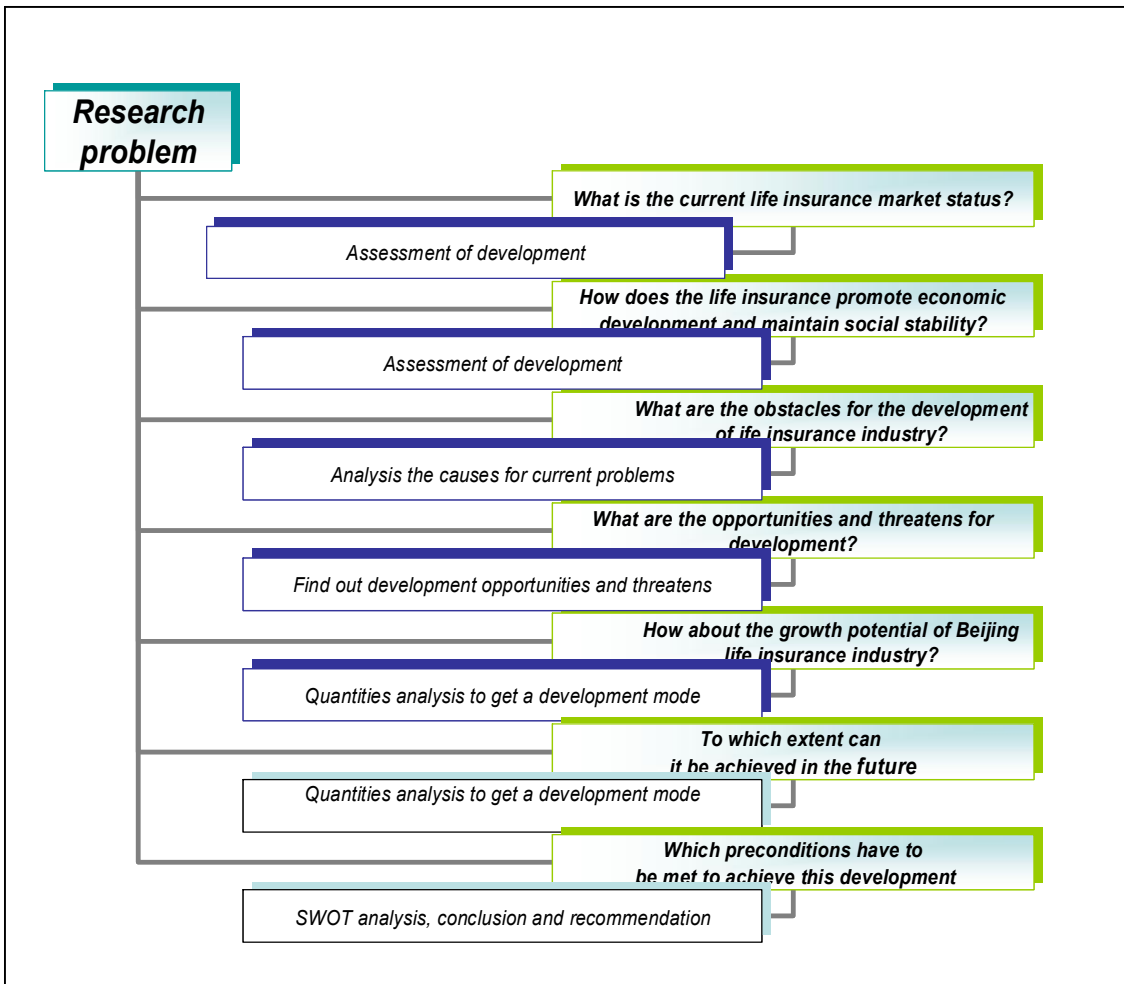
For answering questions 3 and 4, I will try to find out potential causes for the observed problems in the Beijing life insurance industry investigating different aspects, including society, foreign investment, human resource and historical issues and so on.

As for the topic of forecasting future development (question 5), I will mainly try to predict development of the Beijing life insurance industry on the basis of economic and society prospective. Through a summary of all the opportunities and threats, I hope I can with some certainly say that the Beijing life insurance market will grow rapidly in the future.

The answer to questions 6 and 7 is based on the construction of a model, using quantitative statistical methods. I will try to construct some forecasting models based on current data, and predicting the near term development level in the future. Moreover, two different models will be constructed to reduce systematic and stochastic errors and enhance the accuracy.

Finally, for answer the last question, I will combine the data acquired to answer future development with the threats and opportunities stated previously to put forward recommendations for both managers and government. The flow chart of the question scheme is shown in figure 1-3.

Figure 1-3. The flow chart of the questions



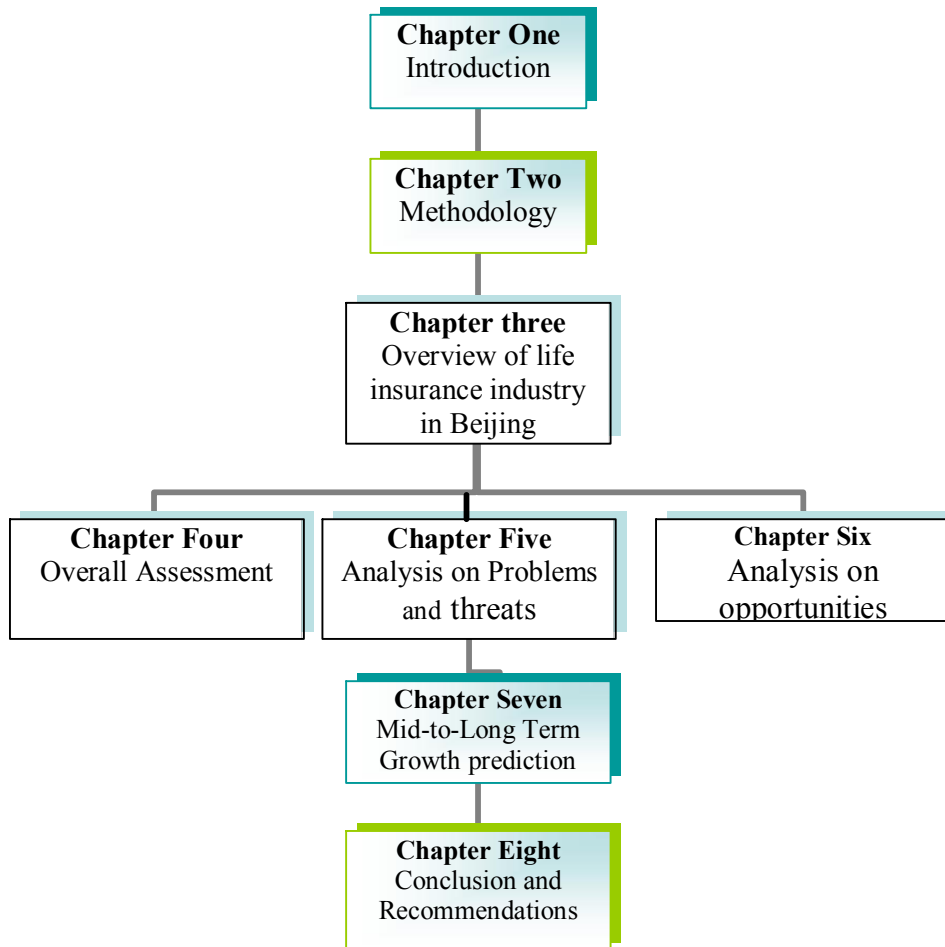
1.5 Disposition

We structure our thesis into eight chapters (See figure 4).

In the chapter one, I will describe the general background and research area of the thesis; identify our research problems and purpose. Furthermore, the delimitation also will be given as well as disposition. Chapter two is mainly focused on the methodology, in which the methods that I am going to use will be discussed. In chapter three, I will give an overview of Beijing life insurance industry. Then I will perform a systematic assessment of insurance industry in Beijing in chapter four. The threats and opportunities for future development in Beijing life insurance industry will be discussed in chapters five and six. A quantitative

statistical analysis to predict medium-to-long term development potentials will be discussed in chapter seven. Finally, conclusions and recommendations will be presented in chapter eight.

Figure1- 4 .Disposition of the thesis



Source: own

Chapter 2 Methodology

Choosing scientific and suitable methods is the primary requirement for academic research: no one can get correct answers and results based on wrong methodology. In this chapter, I will present the research methodology and research approaches used in this thesis as well as the data collection method adopted. This chapter will provide a clear idea to readers about how the research was carried through and why the chosen methodology and approach was preferred over others and implemented. In the last paragraph of this chapter, a summary of methodology will be indicated.

2.1 Research method

Three research methods can be used in this thesis. They are qualitative, quantitative, and mixed-methods approaches. I should choose the most appropriate one.

Qualitative research is a field of inquiry that crosscuts disciplines and subject matters. Qualitative researchers aim to acquire an in-depth understanding and rely on reasons behind various aspects of behavior. Simply put, it investigates the why and how of decision making, not just what, where, and when. Hence, the need is for smaller but focused samples rather than large random samples, which qualitative research categorizes data into patterns as the primary basis for organizing and reporting results. Qualitative researchers typically rely on four methods for gathering information: (1) participation in the setting, (2) direct observation, (3) in depth interviews, and (4) analysis of documents and materials.⁷

Quantitative research is the systematic scientific investigation of quantitative properties and phenomena and their relationships. The objective of quantitative research is to classify features, count them, and construct statistical models or develop and employ mathematical models, theories and/or hypotheses pertaining in an attempt to explain what is observed. The

⁷ Marshall, Catherine & Rossman, Gretchen B. (1998), Designing Qualitative Research

*process of measurement is central to quantitative research because it provides the fundamental connection between empirical observation and mathematical expression of quantitative relationships.*⁸

Multi-methodology, or mixed methods research, is an integration approach of above two methods; which combines the collection and analysis of quantitative and qualitative data.⁹

The Multi-methodology, or mixed methods research method were used in this thesis. The reason for choosing them is that both quantitative research method and qualitative research method had to be used. When we want to evaluate the current life insurance market, we need in-depth data, and thus qualitative methods have to be implemented. However, when we want to find out the relationship between life insurance and economic development or to predict the medium term market potential of the life insurance industry using a statistical model, quantitative research methods need to be applied.

2.2 Data collect methods

Data and information can be divided into two categories: primary data and secondary data. Primary data is the information collected for the first time; it means the data was collected by me on purpose for this research. To get the primary data, interviews surveys and questionnaires can be used. Primary data collection is necessary for some specific research questions, such as personal opinion about development. But it costs more money and time. Moreover, difficult answers and results can be got for the same questions represented different people's idea.

The secondary data are the information and data that already exist. I do not need to collect directly, only need to collect them from books, articles, papers and so on. It is cheaper and more quickly available but I need to process them before it is useful.

⁸ Miles & Huberman (1994, p. 40). *Qualitative Data Analysis*

⁹ Creswell, John (2004). *Educational Research: Planning, Conducting, and Evaluating Quantitative and Qualitative Research*.

2.2.1 Limitation of primary data

The readers of my thesis might find at some point that its content mainly focuses on secondary data rather than on my own analysis of facts and data. I want to express my apologies for this eventual weakness and hope readers can understand that the main reason for this is the difficulty of accessing and creating reliable primary data in China being most of the time in Belgium as a student. As a native Chinese with nearly four years working experience in this field, however, I certainly can give an analysis from my point of view. This has been complemented by interviews with a limited number of experts in the month of February 2008. However, future academic research and thesis in this field should be based more on in-depth data and larger surveys rather than on more general knowledge and limited expert opinion. In this sense, my thesis lays the groundwork for further exploration.

Primary data mainly came from face-to-face interviews with experts and experienced labors in life insurance field. These interviews were approximately two hours in length respectively, and were conducted in Beijing, Tianjin city, Shenyang city in Feb, 2008. As a complementary to these face-to-face interviews, telephone consultations and on-line consultations also were used to reach the people I could not meet at that time. The contacted people all have long time experience and in-depth sight of the Beijing life insurance field. Through the interviews with these people who came from different companies and a large amount of secondary data and information, the thesis attempts to bring diverse viewpoints together, and give a clearer insight into the Beijing life insurance industry. I thank those Interview respondents for their kindness to provide me valuable information and data. My good private relationship with them helped in gathering the data. Their names, positions are listed in *table 2-1*.

Table 2-1 Interview respondents

Name	Company	Position
Mrs. Ma xiaohong	Ping An , Beijing	General manager in Beijing
Mr. Shan yingwei	Tai Ping , Beijing	General manager in North-East district
Mr. Liu jun	Ping An , Beijing	Marketing department manager
Mr. Gao hong xun	China life , Beijing	Marketing department manager assistant

Mr. Zhao shouguo	China Pacific Insurance, Beijing	Training department supervisors
Ms. Gao yan	AIA, Beijing	Health insurance department
Ms. Dongzhaohui	AIA, Beijing	Pension and banking department
Ms. Wangyu	ING, Beijing	Market department manager assistant
Mrs. Shi chunyan	AXA , Beijing	Training department supervisors
Ms. Ji hong	Xin hua, Beijing	Training department supervisors
Mrs. .Wan jing yi	CIRC, Beijing	Governmental officers

Source: own.

Structured and non-structured interview and conversation were all used to get more precise and extensive data and information, due to the personal relationship and their professional background, primary data collection was successfully executed. But because of the limitation in time, I could not get all the data that I needed from primary data collection sources.

2.2.2 Secondary data collection

The secondary data collection began in the first period of research, the end of last year, huge amounts of information and data came from books, journeys and the internet and statistics calculation was carefully executed to better understand the collected data. It is really hard to filter and choose useful data, at the same time. I also needed to check the accuracy of the information and hope I have been able to do so. On the purpose of increasing the accuracy, I mainly use the data from China statistical bureau, Chinese statistical yearbook and CIRC rather than from commercial insurance companies.

2.3 The possible errors in the report

I tried to prevent mistakes as much as possible, but there are still some chances for errors occurring in this research process. The errors will mainly be due to the following sources:

- Time and financial limitations mainly when gathering primary data
- Errors in the gathered primary data and secondary data

- Translation mistakes from Chinese literature to English

The methodology table summarizes this chapter (*see table 2-2*),

Table 2-2 Methodology table

Research Method	Mix-structured method Both quantitative and qualitative analysis
Data Collection- primary data	Limited respondents
Data collection- secondary	Extensive
Possible errors	Time limitation Financial limitation The primary and secondary data The translation mistakes from Chinese literature to English

Source: own.

Chapter 3 Overview of Beijing life insurance industry

In order to give reader a clearer picture and gain better understanding of the Beijing life insurance industry and market, and also to lay the foundation for our research, an introduction of Beijing life insurance industry in all its aspects will be presented in this chapter.

Over the past 20 years, the Beijing area has achieved tremendous economic growth. A result of this economic growth, the Beijing insurance industry, especially has also witnessed the finest period of its development in the period from 2000 to 2007, both in life insurance industry and property insurance industry.

Many factors correlated to insurance can be used to prove this growth in insurance industry, such as bigger market scale, more insurance companies and more premiums as well as fiercer competition among the participants. I will present these factors one by one.

3.2 Development Status

3.1.1. The insurance business has grown rapidly both in insurance companies and premium

With the opening of Beijing insurance market after China entered the WTO in 2001, and more specially, when the transition period agreed upon at the moment of WTO accession for insurance industry expired on December 21, 2004, the Beijing life insurance industry has entered a new era of overall development.

More and more investors from China and from foreign countries entered the market to establish new insurance companies or local branches. There were only 9 insurance companies in Beijing in 2000; five of these nine were life insurance companies, whereas at the end of 2007, 64 companies are currently working in the insurance sector and thirty-six of these 64 are active in the life insurance business¹⁰. (See figure 3-1)

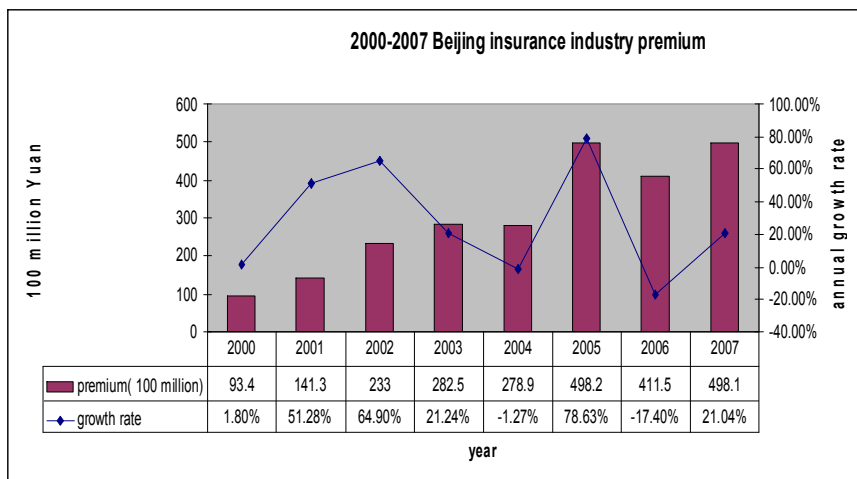
¹⁰ Beijing Insurance Regulatory Committee



Source: Beijing Insurance Regulatory Committee

Insurance business is one of the industries enjoying among the highest growth rates in the Beijing area. Total insurance premium income has grown by an average more than 30% annually since 2000. The total premium income in the Beijing area reached 49.81 billion Yuan in 2007, more than 5 times of the premium amount in 2000¹¹. (See figure 3-2)

Figure 3-2 the amount of Beijing insurance premium



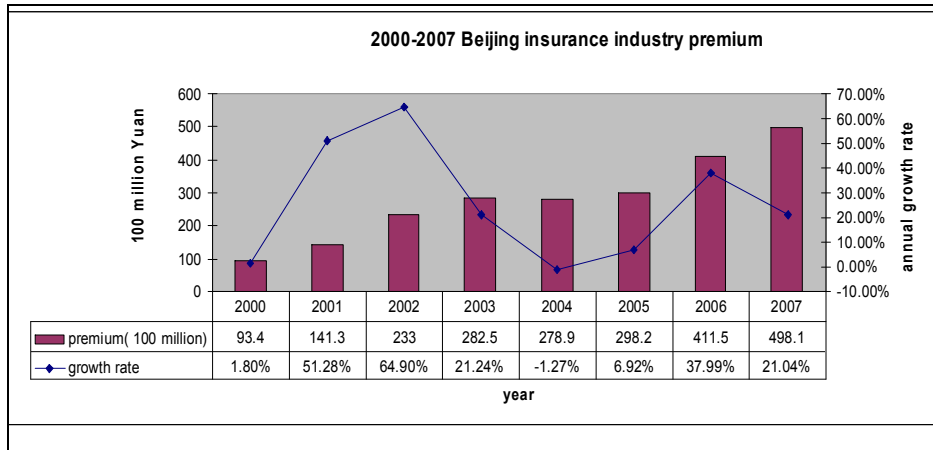
Source: Beijing Insurance Regulatory Committee

The reader will notice a steep increase in the 2004-2005 period compared to other years and what would look like a normal growth pattern. The reason is that one foreign insurance company, “Generali China Life Insurance CO, LTD”, which is the joint venture of the Italian

¹¹ Beijing Insurance Regulatory Committee

Generali Insurance Company and the China Petrol Company, gained one incredibly big life insurance contact by selling in 2004 a group life insurance contact to all the retired employees of China Petrol, valued at 20 billion Yuan.¹² If one does not take this contact into account, the normal increase curve, showing a slowdown after 2002 and going up again normally starting 2004, can be shown (*figure 3-3*).

Figure 3-3 the amount of Beijing insurance premium (adjusted)

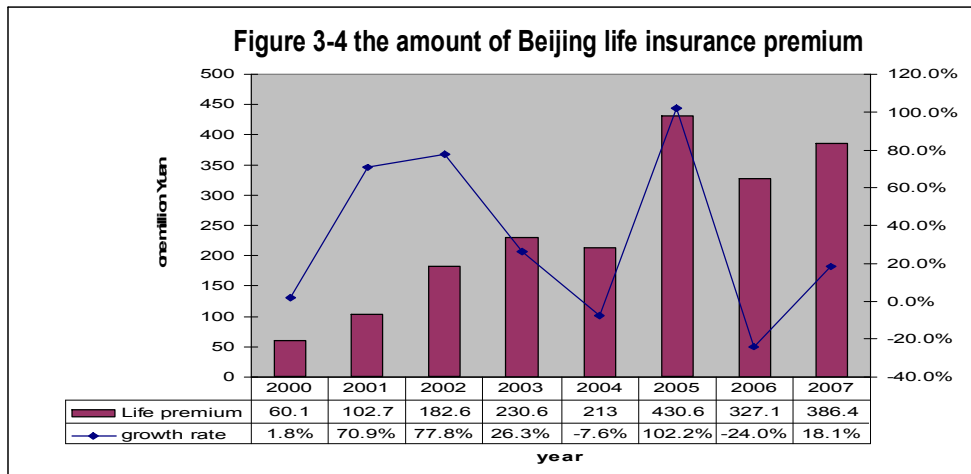


Source: Beijing Insurance Regulatory Committee

Because this thesis only focuses on the life insurance market in Beijing, I subtracted the property premium from the total insurance premium to obtain *figure 3-4*, which shows that the life insurance premium on its own was valued at 38.64 billion Yuan in 2007, thus representing nearly 75% of the total premium volume. Moreover it was nearly 6.3 times as big as the total life insurance premium in the area 2000.¹³

¹² China insurance regulatory committee(CIRC)

¹³ China insurance regulatory committee(CIRC)

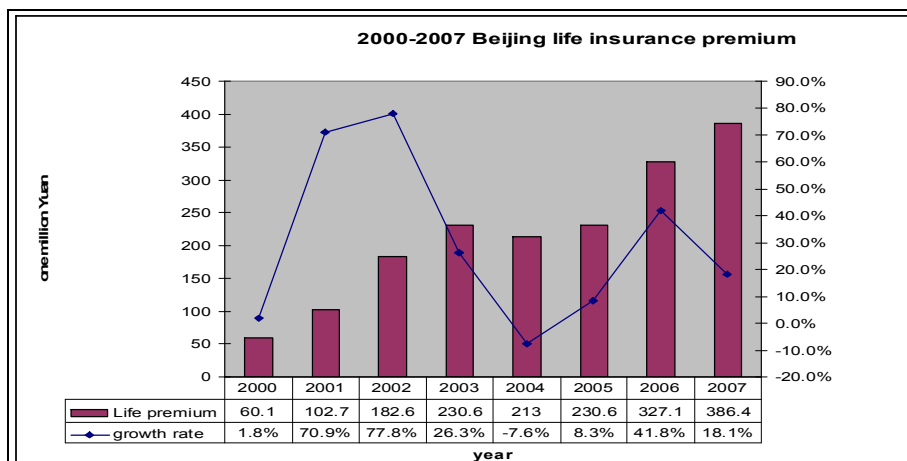


Source: Beijing Insurance Regulatory Committee

Based on the higher growth rate and the high percentage it represents in the insurance market, life insurance has much more market potential than property insurance. This is also the reason why we focus on the life insurance industry only.

If, just as before, we do not take the big life insurance contact of Generali China with China Petrol into account, the normal growth curve looks like figure 3-5, and the average growth rate was still very high (29.47%).

Figure 3-5 the amount of Beijing life insurance premium (adjusted)

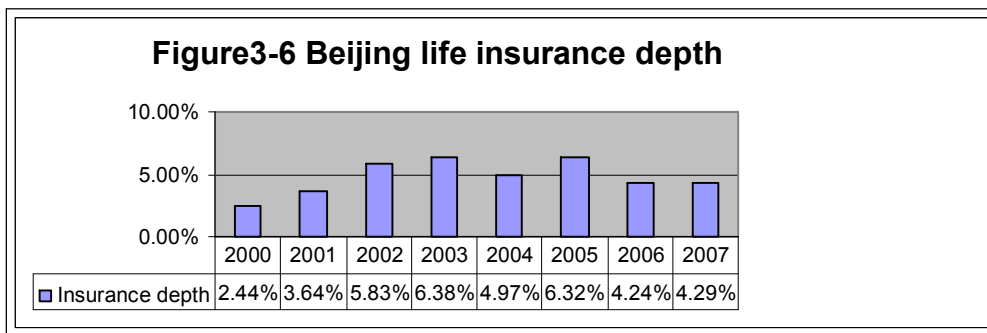


Source: Beijing Insurance Regulatory Committee

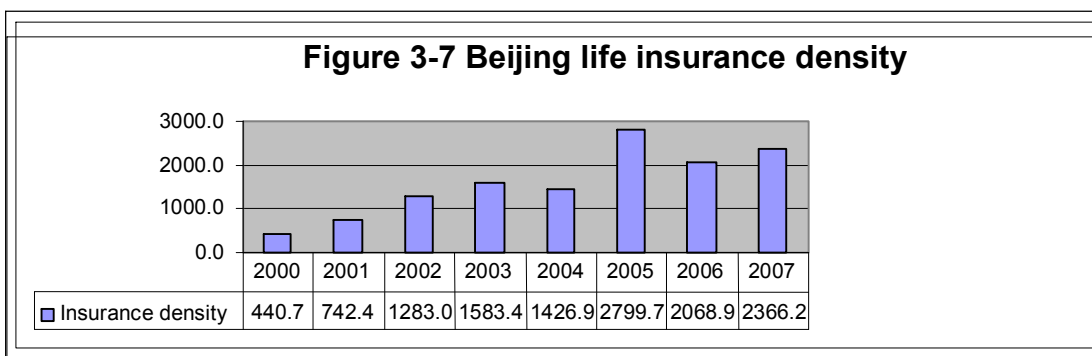
3.1.2. The business indexes of the life insurance industry have increased very rapidly.

There are two very important indexes, life insurance density and life insurance depth, used to evaluate the development situation in life insurance industry.

Insurance density is defined as life insurance premium income divided through average living population. Insurance depth can be defined as life insurance premium income divided through local GDP.¹⁴Through the calculation, it is easily find that life insurance depth increased from 2.44 in 2000 to 4.29 in 2007 and life insurance density increased from 440.7 Yuan in 2000 to 2366.2 Yuan in 2007. These two indexes thus show a remarkable growth in life insurance business in Beijing.¹⁵(See figure 3-6, 3-7).



Source: Calculated myself according to the GDP data from National Bureau of Statistics



Source: Calculated myself according to the population data from National Bureau of Statistics

¹⁴ Beck A New Database on Financial Development and Structure, World bank, 1999

¹⁵ GDP and population data : National Bureau of Statistics China

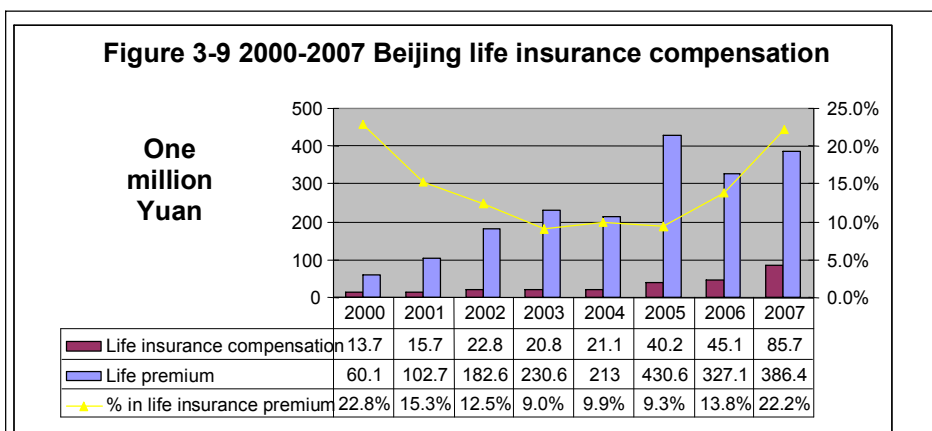
Readers will notice that the growth rate in life insurance depth was higher before 2005 than after 2005. The reason for this is that the denominator of this index (GDP) has changed much. Beijing invested billions of dollars to construct many stadiums for the Olympic Games and to reform and reconstruct old basic building, roads and metro lines to prepare for 2008, causing its local area GDP to increase dramatically from 2004 onward. (See figure 3-8).



Source: National Bureau of Statistics China

3.1.3 The insurance compensation has increased rapidly.

The total insurance compensation increased from 2.37 billion Yuan in 2000 to 13.54 billion Yuan in 2007. It represented 27.2% of total premium income (see figure 3-9). For life insurance, the total compensation increased from 1.37 billion Yuan in 2000 to 8.57 billion Yuan in 2007, a nearly 9 fold increase, and this compensation represented 22.2% of the total life insurance premium income.¹⁶



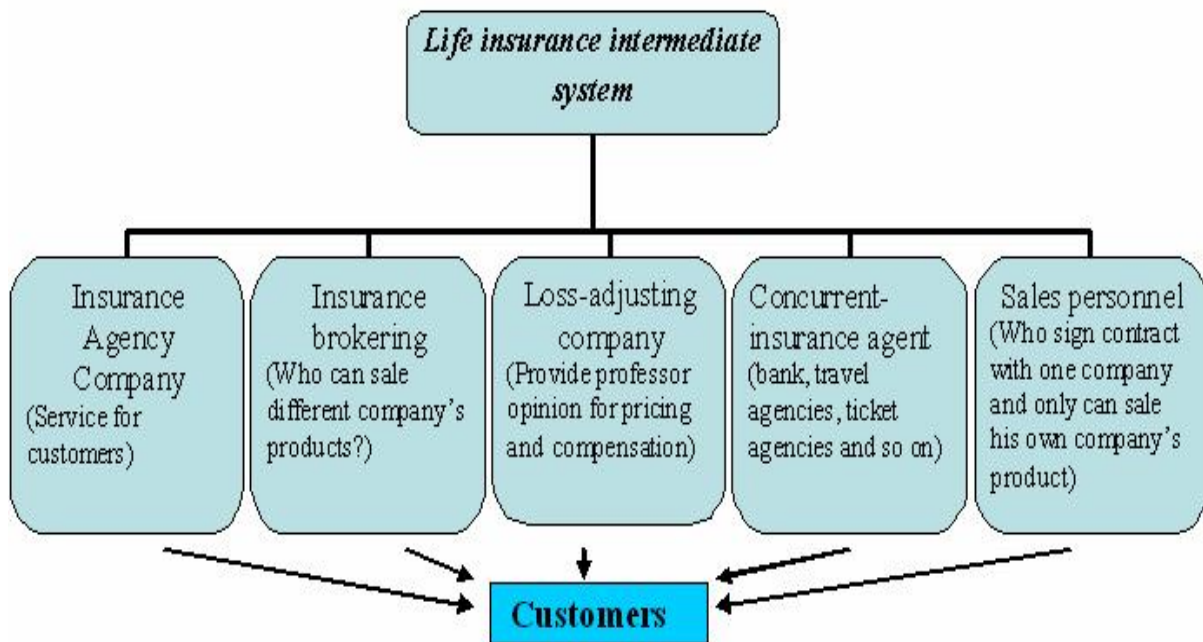
Source: Beijing Insurance Regulatory Committee

¹⁶ Beijing Insurance Regulatory Committee

3.1.4. The insurance intermediate market system has been greatly improved.

Mature insurance normally has a complicated intermediate system, using different kinds of participants at different levels, such as insurance agency companies, insurance brokering companies, loss-adjusting companies, concurrent-insurance agents and sales personnel. (See figure 14). The loss-adjusting companies are mainly active in the property insurance business, so this thesis does not mention them specifically.

Figure 3-9 The insurance intermediate market system



Source: own

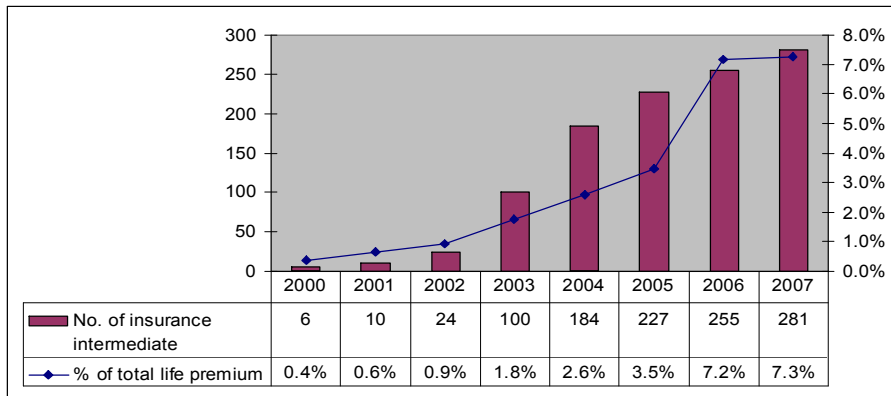
There were only 5 insurance agencies, 1 insurance brokering company in Beijing in 2000. At the end of 2007, among the life insurance intermediaries, 131 were agencies, 116 were brokerages and 34 were loss-adjusting companies, 8416 were concurrent-insurance agents. The sales personnel of the whole industry amounted to 43,270.¹⁷ (See figure 3-10)

At beginning of the period, the premium income for life insurance industry mainly relied on sales personnel, but with the further development of the intermediary system, other segments started to provide important an contribution to the total premium income. Premium income from agencies and brokering for instance, which represented only, 21 million Yuan in 2000, a

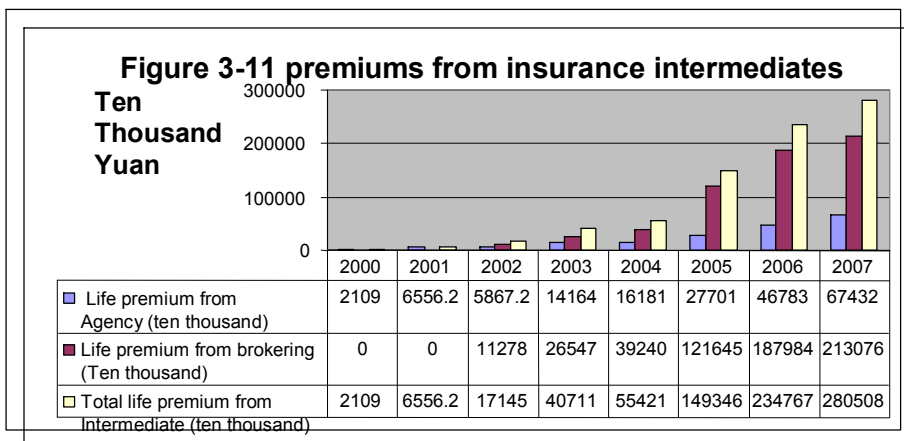
¹⁷ Beijing insurance development research

mere 0.4% in total life insurance premium income, has increased more than 1000fold to 2.8 billion Yuan at the end of 2007. It represents 7.3% of the total premium income now. (See figure 3-11)¹⁸

Figure 3-10 The amount of insurance intermediate



Source: Beijing insurance development research

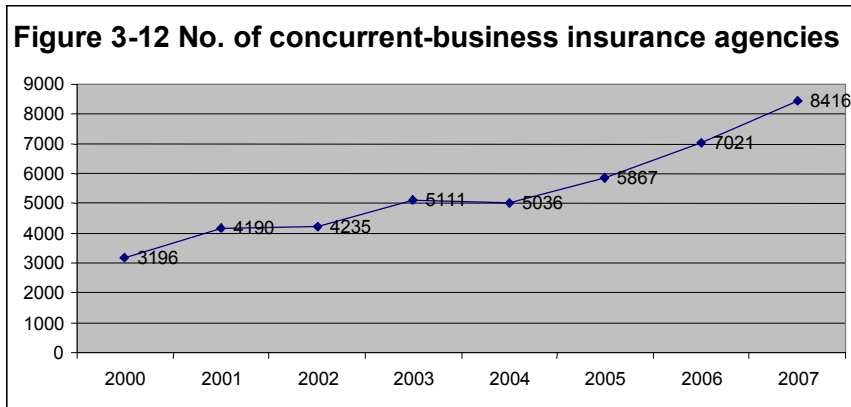


Source: Beijing insurance development research

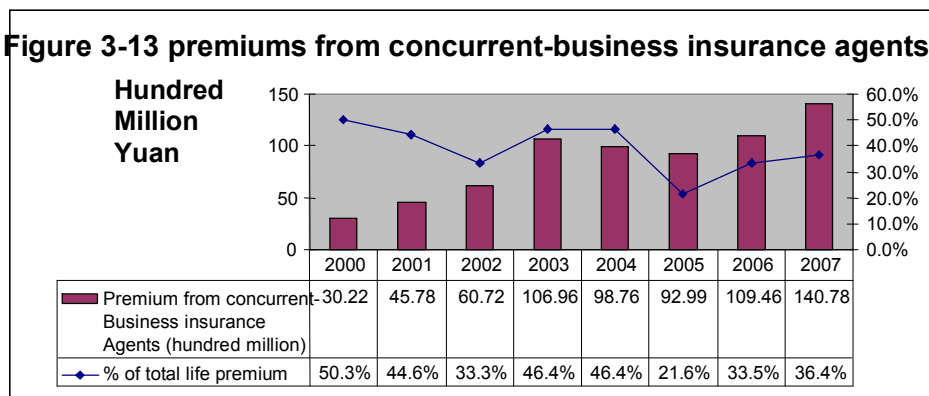
The number of concurrent-business insurance agents grew from 3196 in 2000 to 8416 in 2007, and contributes 14.078 billion Yuan to the total premium income now, representing 36.4% of the total premium income. (See figure 3-12, 3-13)¹⁹

¹⁸ Beijing insurance development research

¹⁹ Beijing insurance development research



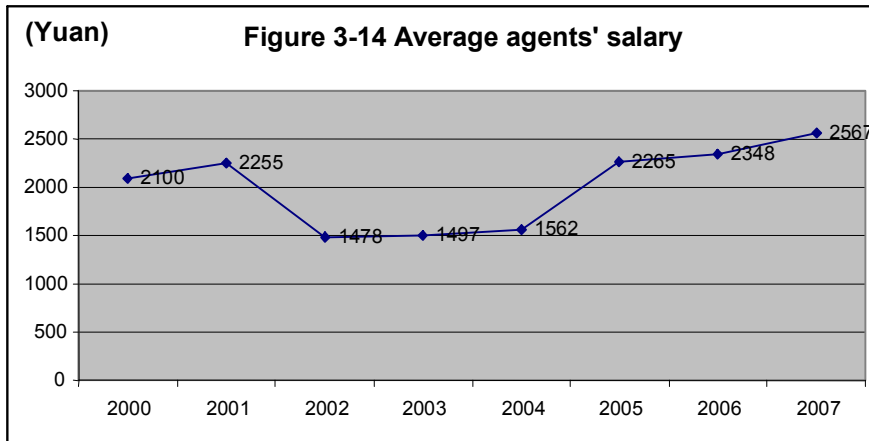
Source: Beijing insurance development research



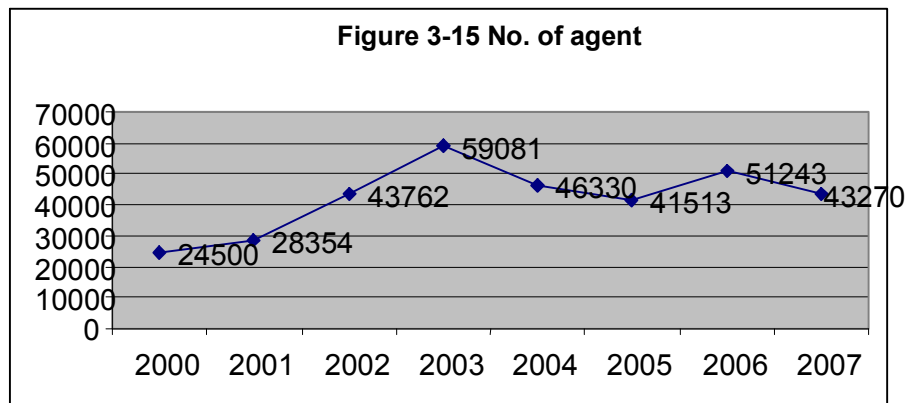
Source: Beijing insurance development research

Sales personnel amount increased rapidly before 2004. However, due to the problems in agents system, such as social prospective, insufficient experience, high turnover rate and increase of sales channels, the salary of agents did not grow in a stable way. From 2002 to 2004, the average salary of all agents went down to nearly 1500 Yuan/month from 2100 Yuan/month on 2000(see figure 3-14). After this period, the agent salary went back to normal levels and shows stable growth, at the same time, the amount of agents did not change much after 2004 either (see figure 3-14). In 2007 the total amount of sales personnel active in the Beijing life insurance sector is 43270.²⁰

²⁰ Beijing insurance development research



Source: Beijing insurance development research

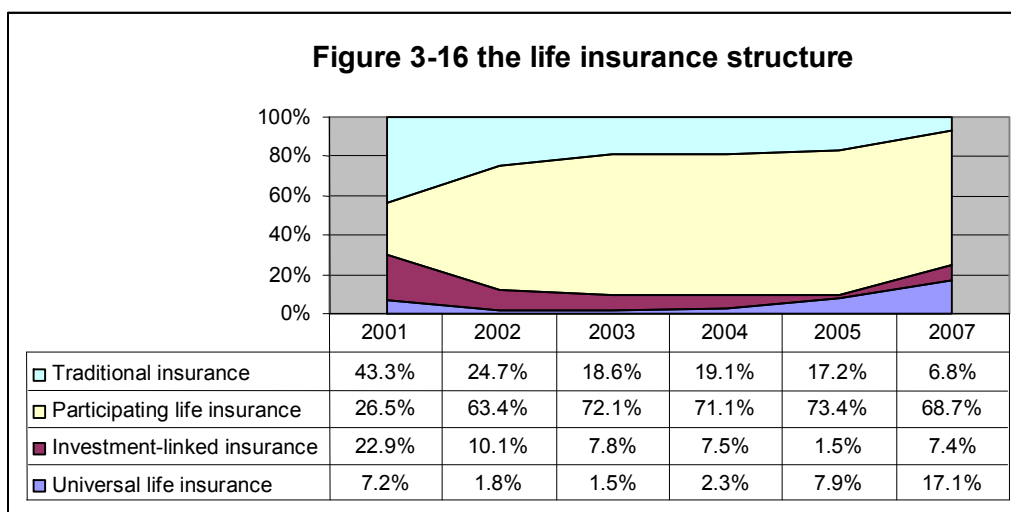


Source: Beijing insurance development research

3.1.5. The life insurance structure has changed a lot since 2000

Since 2000 new and different products have been launched on the Beijing life insurance market. Following this product development process, the composition of current life insurance market has changed dramatically over the past decade. The percentage of traditional insurance has decreased and while participating life insurance still represents the major part of the current market, after universal life insurance was launched on the market, more and more people began to choose this new multiple product. *Figure 3-16* represents this alternation clearly.

Universal life insurance represents 17.1% of the market now while the percentage of participating life insurance declined from 73.4% to 68.7%. Traditional insurance has the smallest market share that is only 6.8%²¹.



Source: Beijing insurance development research

3.1.6. The legal framework has been changed and improved.

Along with the development of insurance industry, a new legal framework, regulations and authorities have been founded by the government. The “*Insurance Law*” was promulgated at the end of last century and amended in 2002 and the “*Regulations on Administration of Foreign-invested Insurance Companies*” was promulgated in 2001.

The China Insurance Regulatory Commission (the “CIRC”) was established on November 18, 1998, which was authorized by the State Council. It is responsible for conducting administration, supervision and regulation of the Chinese insurance market and ensuring the insurance industry operates stably in compliance with law. Its major responsibilities are enumerated following:

(1) The CIRC formulates policies, strategies regarding the development of the insurance industry and makes relevant rules for the insurance industry.

²¹ Beijing insurance development research

- (2) It examines and approves the establishment of insurance companies and their branches, insurance relevant organizations.*
- (3) It examines and confirms the qualifications of the senior managerial personnel in all insurance-related organizations; establishes the basic qualification standards for insurance practitioners.*
- (4) It examines and approves the clauses and premium rates of insurance lines related to the public interests.*
- (5) It supervises the solvency and market conduct of insurance companies according to law.*
- (6) It supervises the business operation of public-policy-oriented insurance and statutory insurance.*
- (7) It conducts investigation into the irregular market actions and imposes penalties.*
- (8) It supervises overseas insurance organizations established by domestic insurance and non-insurance organizations according to law.*
- (9) It lays down standards for the information system, risk-assessment, risk-warning and risk-monitoring systems of the insurance industry in accordance with relevant regulations of the State.*
- (10) Other duties commissioned by the State Council.²²*

3.3 Characteristics of Development

Based on the data in the preceding paragraph, we can summarize the major characteristics of development of the Beijing life insurance market as follows. Six aspects are very important:

- A new and more liberal legal framework has been established.
- Total premium income has increased dramatically
- The number of life insurance companies quickly increased as well, thus decreasing the concentration rate of the market
- Competition on the market has become fiercer.

²² China Insurance Regulatory Commission

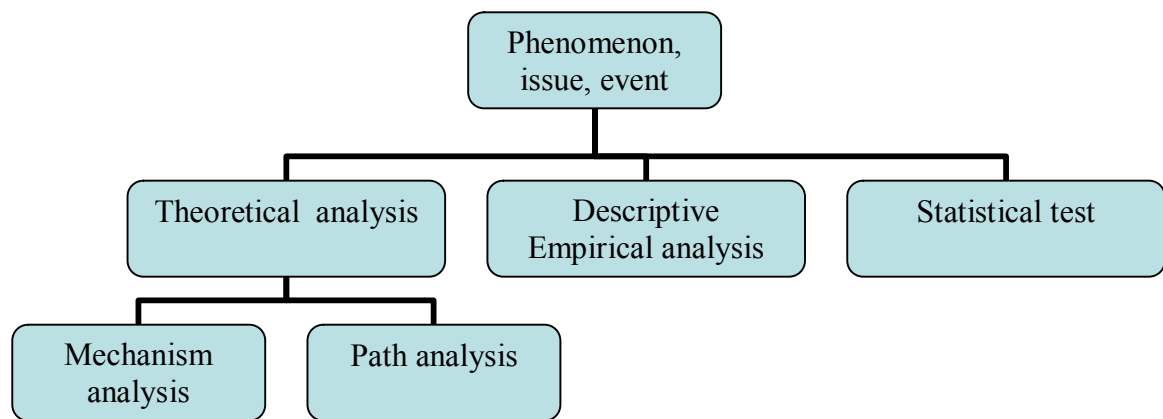
- The innovation of products and distribution channels became one of the major determinants and characteristics of this rapid development.
- The life insurance intermediate system has been greatly expanded and improved.

Chapter 4 Overall assessment of the development of the life insurance industry in Beijing

This chapter presents a systematic evaluation of the development of the life insurance industry in the Beijing. It starts with a theoretical and empirical analysis of the mechanisms through which life insurance promotes economic and social development in society. After that, some standards will also be used to assess the level of development of the life insurance industry from the perspective of economic and social development in Beijing

In this section, an analysis framework developed by Allen and Santomero²³ will be used to analyze the relationship between the degree of development of the life insurance industry and economic and social development in society. This framework mainly uses the functional point of view (*see figure 4-1*).

Figure 4-1 The processes of this analysis frame



Source: The Theory of Financial Intermediation

4.1. The Life Insurance Industry Advances Economic Growth

4.1.4 Theoretical Analysis

4.1.1.1 Mechanism analysis of life insurance advances economic growth

²³ Allen and Santomero ,The Theory of Financial Intermediation

Through following three mechanisms, life insurance advances economic development: it constitutes risk protection; it serves as a savings substitute and is an asset investment. Each of them is explained below.

➤ ***Risk protection***

Providing protection against risk and expense is the core function of life insurance. Through reduce the uncertainty and fluctuation, life insurance have position attribution to following aspects:

Firstly, insurance provide compensation for lost caused by natural disaster and accident, then promote the development of some business sectors, such as transformation, logistic and loan and so on.

Secondly, insurance can reduce people's future uncertainty, then increase loan and consumption..

Thirdly, insurance provide protection for the individual's high risk activity, and then promote the development of tourism and high risk business investment.

Although life insurance increases customers' costs in short-term, it increases economic efficiency and advances economic growth.

➤ ***Saving substitute***

Life insurance increases the choice options in the financial market, enriches investment channel, raises financial competition, and reduces market risk. On the other hand, based on its protective function, life insurance reduces preventive savings, encourages consumption, enlarges demand and thus advances economic growth.

➤ ***Asset investment***

Through the utilization of assets, insurance companies have already become one of the most important investors on the global capital market. Because of the long-term vision and contract terms in the insurance industry, insurance companies moreover provide long-term investment and directly or indirectly pump huge amounts of money into the capital

market, while at the same time increasing competition in the financial market and thus enhancing market efficiency.

4.1.1.2 Path analysis of life insurance advances economic growth

Several theories support these phenomena and constitute a path analysis of life insurances' influence on the advancement of economic growth. They are the "*New theory of financial development*" and the "*Efficient Demand Theory*".

➤ The New Theory of Financial Development is the theory endogenous growth. It explains the internal mechanism for the financial development advancing economic growth. ²⁴This thesis quotes just one representative model, the Pagano model ²⁵to illuminate the relationship between life insurance industry and economic growth.

The Pagano model states that

$$g = A\sigma s - \delta$$
²⁶

In which:

G is the economic growth rate,

A is the capital output rate,

σ is the translation rate from savings to investment,

S is the total savings rate, and

δ is the depreciation rate.

Life insurance industry advances economic growths mainly because its protective function encourages people to reduce preventive saving. This actions increases σ , and then increases g and advances economic growth.

²⁴ Shen jun, Construction of new theory of financial development and Chinese financial innovation of efficiency

²⁵ Pagano, Financial markets and growth: An overview

²⁶ Zhu baohua, New theory of economic development

- The Efficient Demand Theory developed by the British economist Keynes furthermore told us that:

$$GDP = C + I + G,^{27}$$

This signifies that

Gross Domestic Product = consumption + gross investment + government spending

Assume the government spending do not change, the above equation changes to:

$$GDP = C + I$$

Using growth rate (Δ) to replace above equation, then

$$\Delta GDP = \Delta C + \Delta I$$

As mentioned in the part of mechanism analysis, The life insurance industry can provide protection for people in health and income stability, reduce people's risk awareness and risk aversion, and then reduce people's preventive savings, increase consumption and gross investment, and then advanced economic development

These affects have to be viewed finally against the background of profound economic transition China is currently experiencing from planned economics to full market economics. In this light, the life insurance industry was established and developed to deepen the system change and speed the transition effectively.

- The following aspects are extremely important with respect to the transition phenomenon and render the insurance industry an extremely important role during the transition period:
- Life insurance industry is one of the necessary components of a market economy.
- Life insurance industry is one of the most important components of a market oriented financial system.
- The Insurance industry in general is an important component of every social security system as well.²⁸

²⁷ N,Geogory Mankiw, Principles of economics

²⁸ China insurance industry research

4.1.5 Descriptive Empirical Analysis

4.1.2.1. The life insurance industry in Beijing has a great positive attribution in reducing risk and allocating resource.

The main analysis has already been mentioned in Chapter 3. We recapitulate the most important data. From the *figure 3-4*, we can find that total life insurance premium in 2007 was 38.64 billion Yuan, representing nearly 75% of total premium income. It was nearly 6.3 times as large as the total life insurance premium in 2000. The life insurance depth and density also increased continually. (*See figure 3-6, 3-7*) Total compensation also increased from 1.37 billion Yuan in 2000 to 8.57 billion Yuan in 2007, it was nearly 9 fold the 2000 figure. Compensation represents 22.2% of total premium income. (*See figure 3-9*)

4.1.2.2. The life insurance industry accelerates the capital market development and financial system reform.

With the continuous increase of total premium, assets of life insurance companies have increased dramatically. More and more funds entered the Chinese and world capital markets and promoted market development, supported the reform of commercial banking and enhance the bond market in China. By the end of 2007, insurance assets represented 9% of total GDP in Beijing.²⁹

4.1.2.3. The life insurance industry optimizes the financing structure.

At present, the finance market in Beijing mainly relies on the indirect financing like bank loans (90% of the financing market is represented by them). The direct financing market, such as the stock market and corporate bond market are only small scale and represent less than 10%³⁰ of invested funds. This unbalanced financing structure is not only typical of the Beijing area, but is also present all over China.

²⁹ Beijing insurance industry development research

³⁰ China bond industry yearbook 2007

With more insurance assets entered the financing market, especially most of assets input to long-term bond, the financing structure will be improved.

4.1.2.4. The life insurance industry increases employment

The life insurance industry is human-capital intensive. In Beijing, the number of employees in the life insurance business is more than 46.000 in 2007 and represents 45% of total employment in the financial industry.³¹

4.1.2.5. The life insurance industry increase GDP directly

Obviously, as one kind of economic activity, life insurance industry increases GDP automatically.

4.1.6 Statistical Analysis Model

According to the previous analysis, we can make an assumption that the life insurance development level in Beijing is an important factor that can influence economic development. Statistically, this can be analyzed by a logistic regression equation:

$$LNGDP=f(LNPRE) + \epsilon$$

In which:

Lngdp is natural logarithm of GDP in Beijing

Lnpre is natural logarithm of life insurance premium income in Beijing

Epsilon is error term.

All the data came from China national statistic bureau and the CIRC. The Spss 13 programme was used to perform all the calculations.

Table 4-1 GDP and life insurance premium income in Beijing

Year	2000	2001	2002	2003	2004	2005	2006	2007
GDP (hundred million Yuan)	2460	2817.6	3130	3612	4283.3	6814.5	7720.3	9006.2

³¹ Beijing insurance industry development research

Life premium (hundred million Yuan)	60.1	102.7	182.6	230.6	213	230.6	327.1	386.4
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Statistic results and interpretation of the correlation are:

Table 4-2 Correlation coefficient between GDP and premium income

		GDP	PREMIUM
Pearson Correlation	GDP	1.000	.862
	PREMIUM	.862	1.000
Sig. (1-tailed)	GDP	.	.003
	PREMIUM	.003	.

The table shows there is a very strong correlation relationship between GDP and life insurance premium. The correlation coefficient is 0.862. The further statistical analysis provides us with the following model summary.

Table 4-3 R-value of model

Model	R	R Square	Adjusted R Square	Sig. F Change
	.862(a)	.743	.700	.006.

Table 4-4 model coefficients

Coefficients(a)						
Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
	(Constant)	4.734	0.887		5.341	0.002
	PREMIUM	0.700	0.168	0.862	4.165	0.006

a. Dependent Variable: GDP

From the above tables, we can find a less than 1% significant level. The regression equation existing between GDP and premium is:

$$LN GDP = 4.734 + 0.7 (LN PRE)$$

Since $R=0.862$, $R\text{ Square}=0.743$ and adjusted $R\text{ square}=0.7$ and the P -value for the F -test is 0.006 , the result of statistical tests prove that the life insurance industry is an important factor of economic growth.

4.2. Life Insurance Industry Advances social development

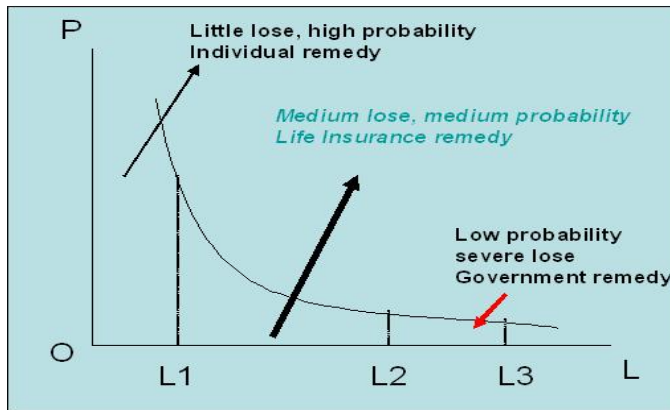
4.2.1 Mechanism and path analysis

The current social development goal in China is constructing a harmonious society. Undoubtedly, the life insurance industry in Beijing advances the building of a local harmonious society. The mechanism behind this is that the properties and characteristics of life insurance are inherently consistent with the goal of building a harmonious society.

The life insurance mechanism is a unity of compensation to damage and management of risk. The main function of life insurance is to remedy damage and keep the stability of living of the contractant party, which is the same as the goal of a harmonious society. Life insurance is thus a complementary part for the social security system as well. According to insurance theory, the risk is indicated by a Pareto distribution (see figure 4-2). The meaning of the figure is that individual, government and insurance companies all compensate the loss, for loss that happened frequently but with little damage level (from zero to $L1$ indicated in the figure), individual remedies himself, for the loss that happened in very low probability but caused heavy damage (from $L2$ to $L3$ indicated in the figure), government is responsible for remedying it. Life insurance remedies the medium loss with medium frequency (from $L1$ - $L2$ in this figure).³²

Figure 4-2 loss/ damage happen distribution

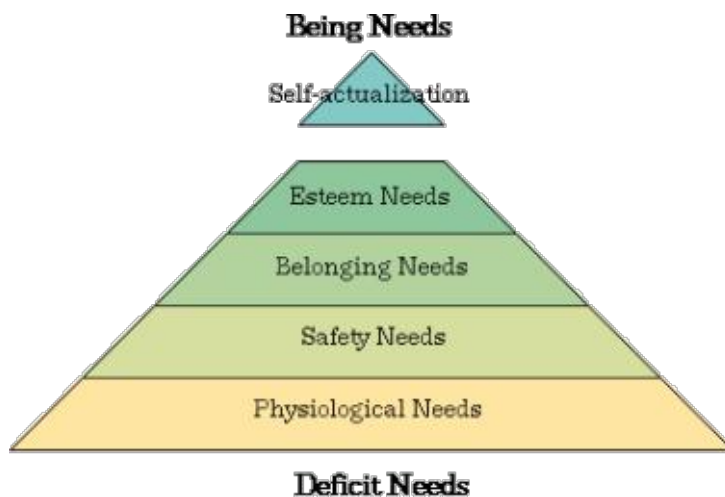
³² Risk theory – Actuary exam



Source: Risk theory –Actuary exam

- The main characteristic of insurance is mutual assistance, which is consistent with the basic characteristic of harmonious society.
- According to Maslow's hierarchy of needs (see figure 4-3), everyone has safety needs³³; the core function of insurance is providing protection against risk. Thus insurance can satisfy people's needs as a risk transfer method. It promotes the realization of harmonious society by giving people the chance to realise other needs than safety needs more easily.

Figure 4-3 Maslow's hierarchy of needs



Source: Philip Kotler, Principle of marketing an Asian prospective

³³ Philip Kotler, Principle of marketing an Asian prospective

4.2.2 Descriptive empirical analysis

Undoubtedly life insurance plays an important role in Beijing's social development. As mentioned in the chapter three and the first part of chapter 4, the compensation by Beijing life insurance industry has increased dramatically and continually remedied the people's loss, promoting a more stable and healthy social development. In terms of economic compensation, the insurance industry has settled claims of 0.1354 billion Yuan in 2007, which is 27.4% higher than in 2003.

Moreover, the life insurance business also provides annual income, pension, and health insurance for the population. All these activities accelerate the increase of living standards. More and more people look to commercial insurance as an important approach to solve the problems of aging, health care and accidents. Some people also look to insurance as another kind of investment tool.

4.4 Standards for Evaluation

Through perfecting the social security system and thus assisting in social management, the life insurance business advances societies' healthy development as well as supporting the creation of a more harmonious society. In this paragraph, some standards will be suggested and used to assess this contribution of the Beijing life insurance market to society. But first, an important distinction between growth and development of the insurance business should be emphasized. The growth of the insurance market can only be measured in terms of growth of premium and assets, whereas the insurance business development must be measured in terms of the life insurance market performance. In other words, insurance development focuses on quality, whereas insurance business growth focuses on quantity and scale or volume. In this section, we want to evaluate the life insurance industry's development in Beijing mainly.

A few standards can be used to do this³⁴:

³⁴ China insurance industry research

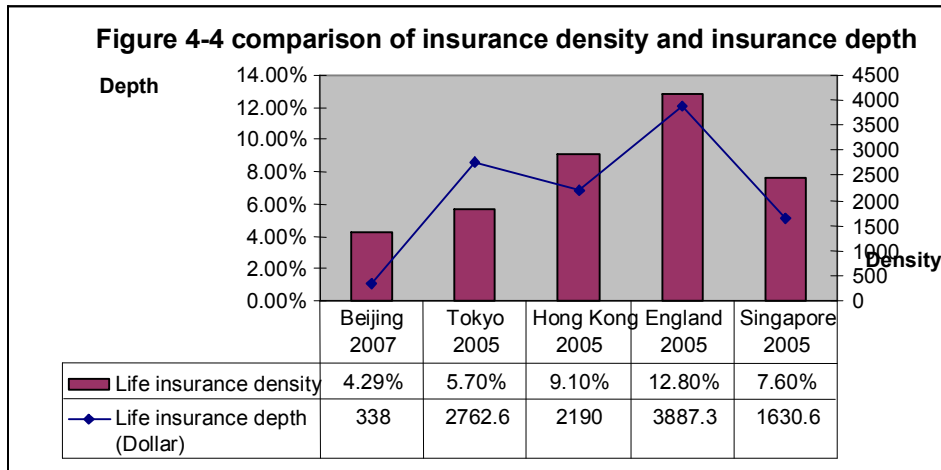
- **Insurance depth and insurance intensity**, which are special indexes in the insurance industry and common used in the international insurance market for indicating the industry's development situation.
- **The position of insurance assets in the social security system**. This index evaluates the relative position between commercial life insurance capital and social security capital and indicates the utility of commercial life insurance in protection people.
- **The position of insurance in the financial system of an area**. This index indicates the position of insurance assets in the total of financial assets by comparison with the bank industry's assets.
- **The efficiency of life insurance companies**. This index measures the ratio between cost and benefit in the business process of life insurance companies and evaluates the sustainable development ability of these companies.
- **The rationality of structure and resource allocation**. This index indicates the efficiency of resource allocation in the insurance industry and evaluates the rationality of the industry's structure.

4.4 Overall assessment

4.4.1. Insurance depth and insurance intensity

As mentioned in the last chapter, life insurance depth and life insurance density largely increased over the last eight years. Life insurance depth increased from 2.44 in 2000, to 4.29 in 2007 and life insurance density increased from 440.7 Yuan in 2000, to 2366.2 Yuan in 2007.

Although these two indexes have increased, comparing them to other developed areas in Asia and beyond indicates that they are still much lower. Detailed data are listed in *figure 4-4*.



Source: China insurance industry research/ Beijing insurance regulation committee

Unfortunately, data for these other four cities were only available till 2005, which makes the comparison somewhat difficult, but clearly indicated that the Beijing life insurance market is still lagging behind. There is a huge gap in life insurance development between Beijing and other developed countries.

4.4.2. The position of insurance assets in the social security system.

According to the statistical data from CIRC, the current proportion between life insurance compensation and social security fund payments in Beijing was nearly 9:100. This figure is also much lower than the world average level, which stands at 22:100³⁵

4.4.3. The position of insurance in the financial system.

From the point of view of assets compared to assets of the bank industry in Beijing, the position of life insurance grew slightly from 2.19 in 2000 to 4.29 in 2007³⁶. This still reflects the pattern of “a strong bank and weak life insurance market”. Any strong substitution effect was not visible. (See table 4-5)

Year	2000	2001	2002	2003	2004	2005	2006	2007
Life premium (hundred million Yuan)	60.1	102.7	182.6	230.6	213	430.6	327.1	386.4

³⁵ China insurance regulation committee

³⁶ Beijing statistical yearbook 2000-2007

bank deposit (hundred million Yuan)	9705	12223.4	15392.7	18321.9	21625.9	28970	33793.3	37700.3
proportion	0.62%	0.84%	1.19%	1.26%	0.98%	1.49%	0.97%	1.02%

Source: Beijing statistical yearbook 2000-2007

With regards to added value, the annual growth rate in life insurance industry in Beijing was nearly 34%, which is much larger than growth in GDP. However, as a proportion of added value in total GDP, the index in Beijing was much lower than the world average level. It only represented 0.34% of GDP.³⁷ So the contribution of the Beijing life insurance industry to the GDP is still low.

4.4.4. The internal structure of the financial system.

When we investigate the internal structure of the financial system, we also found that the added value of the life insurance industry only represented 8.5 % of the total system's added value, comparing to an average level of nearly 30 %³⁸ in many European countries. Beijing life insurance industry is still a very weak factor in the financial industry as a whole.

4.4.5. The rationality of structure.

The structure of life insurance industry in Beijing is not so good. This problem is due to two aspects: an unbalanced development between urban and rural areas and an unbalanced development between insurance companies and intermediates. We explain both of them.

Unbalanced development between urban and rural area

This problem was embodied by an unbalanced total premium, an unbalanced insurance depth, and an unbalanced compensation total. The rates of all these indexes from urban to rural areas still range around 6:1 in 2007.³⁹

Unbalanced development between insurance businesses and intermediates

³⁷ Beijing statistical yearbook 2000-2007

³⁸ Beijing statistical yearbook 2000-2007

³⁹ Beijing insurance regulation committee

As we mentioned in the last part of the previous chapter, life insurance intermediates dramatically increased in total over the last few years. But there remain important problems.

First of all, most agencies are too small to build long-term cooperation with big insurance companies. Secondly, in as far as bank-insurance companies are concerned, banks ask higher commission rates. Moreover most of their clients are insufficient skilled, which leads to a poor profit performance of insurance companies. Thirdly, there is an important imbalance between agencies and sales personnel. Currently sales personnel still represents more than 70% of the total premium income, which is totally different from other developed countries, where brokering creates as much as 65% of the total premium volume (figures from the UK in 2007). Fourth, the lack of channels is paramount. There are much more channels available in other countries than in Beijing. Post-marketing, internet-marketing, tale-marketing and so on, do not exist in Beijing yet. All of the above mentioned problems reduce the utility of insurance distribution channels in the Beijing area.

4.4.6. The efficiency of insurance firms with regard to resource allocation.

This index focuses on the effectiveness and efficiency of insurance companies. It indicates the status of resource allocation in the life insurance companies. Currently, the limited resources have not necessarily been effectively allocated due to several affects, such as:

- Poor investment in research and development for new products;
- The different categories of distribution channels used;
- The poor internal cooperation and harmony based on the used information technology.

We investigate each of these factors in the following paragraphs.

Poor investment in product research and development

Table 4-6 The percentage of R&D investment /total investment					
	USA	UK	KOREA	JAPAN	BEIJNG
R&D %	4.36%	3.15%	3.33%	4.00%	1.12%

Source: Beijing insurance industry development research

In *table 4-6*, we can clearly observe that there is a big difference between financial investments in R&D in the life insurance sector in Beijing compared to some developed countries. Insurance companies in Beijing as of yet did not invest enough money in R&D. This leads to unsuitable products and development restrictions. A more in-depth analysis of this particular problem will be presented in next chapter.

Categories of business and distribution channels

The different categories of insurance business and distribution channels are also determinants of the profit rate in the business. Unfortunately, because most insurance companies in Beijing have mainly been focused on the development in terms of scale and volume, they lost track of the profit objective. Consequently their profit was rather low, even sometimes negative. *Table 4-7* indicates the profit margins of New China Life Insurance Company in Beijing as an example. It is representative of the sector, rather big in the life insurance business and ranks fifth in Beijing market.

Table4-7 profit margins of New China Life Insurance Company

	PERSONAL INSURANCE		GROUP INSURANCE		ACCIDENT AND HEALTH INSURANCE	
	2005	2006	2005	2006	2005	2006
NET PROFIT (MILLION YUAN)	8503	10670	-296	-513	1172	1280
PREMIUM INCOME (MILLION YUAN)	54909	68888	742	1267	10606	10867
PROFIT MARGIN (%)	15.5	15.5	-39.9	-40.5	11.1	11.8

Source: primary data from consultation

From *table 4-7*, we can conclude that the profit margin for group insurance activities is negative, although it represents an essential part life insurance business and cannot simply be stopped as an activity. Insurance companies apparently face a dilemma when they have balance volume of activities and profit potential and have until now given priority to volume of business as a parameter.

The choice of distribution channels also influences the insurance companies' profit margin. *Table 4-8* shows for the same individual insurance company as in the previous example its profit margin when selecting among different distribution channels.

Table 4-8 PROFIT margin among different channels			
	sales personnel	agency	concurrent-business insurance agent
PROFIT MARGIN(%)	13.20%	-7.30%	4.60%

Source: primary data from consultation

The big difference between different types of distribution channels with regard to the profit margin of insurance companies influences the structure of the market considerably. Moreover, due to fierce competition, insurance companies are not entirely free to choose distribution channels offering higher profit margins. Sometimes they have to settle for less profit.

Internal cooperation and harmony based on information technology

Due to the large number of customers, life insurance companies should be able to gather many data on customer's preferences in order to promote service and create better value. The development of a well functioning and integrated internal information system is paramount to this. It would further allow insurance companies to harmonize the functioning of each department separately and amongst one another to achieve maximum efficacy and effectiveness.

Currently, more and more management systems, such as ERP and CRM have been implemented by the insurance companies in many developed countries. Compared to them, the development progress of the information systems in insurance business in Beijing has been lackluster. Only some very large companies in the insurance business, such as Ping An (where I worked before) and China Life, use up-to-date information technology and have a functioning information system based on advanced CRM technology and software. Other companies still do not realize the importance of these systems. Due to the specificity of the insurance business, which bases its services on reliable statistical data more than on the quality of a material product, collecting and utilizing information can largely influence the

competitive capability of any company, now and certainly even more in the future. Most Chinese domestic insurance companies should thus enhance their information technology.

4.5. Conclusion of this chapter

Experts using a data envelope analysis (DEA) model to evaluate the productivity of commercial life insurance firms state that: *“Low efficiency in resource allocation is a pervasive problem among Chinese insurance firms and this has led to a structural imbalance of the industry as well as various difficulties in operation”*.⁴⁰ Due to the limitation of data, I could not perform any new in-depth analysis of this phenomenon, but both the empirical data gathered and my real work experience show that the Beijing life insurance sector has yet to improve its productivity. In spite of its fast growth in terms of volume, the Beijing life insurance business sector plays only a limited role on macro-economic level given its small contribution to GDP and has a very limited impact on the social security and financial system in China and Beijing more in particular, given its structural problems. In general, it shows a low degree of efficiency and a lackluster profit margin compared to other comparable cities in Asia and to more developed countries. As a result, in order to facilitate the development of the Beijing life insurance industry, focus should shift from scale effects and volume interest to efficiency of the industry and its operation.

⁴⁰ yao shuji, using DEA method to analyze China insurance industry efficiency

Chapter 5 Analysis of the Problems and threatens facing the insurance Industry in Beijing

In this chapter, I will summarize the problems currently facing the life insurance industry in Beijing and try to find out which factors have contributed to these existing problems. Three aspects will be discussed: Beijing-specific internal and external factors as well as the influence of common industry specific factors, blended with historical factors. These factors will be discussed from both an economic and a social development perspective. Thus I take into account the rapid development of the life insurance industry in Beijing and in China at large, due to which many problems merge at the same time.

5.1. The influence industry-wide common factors, blending with historical factors

Life Insurance industry differs from manufacturing industry and other service industry in terms of the way of operation, the scope of business, product characteristics and so on. These differences constitute specific industry wide common factors. Among them I state technical characteristics of the insurance business, market structure, transaction cost structure and information asymmetry. All of these lead to problems in the industry. Moreover, these problems become more serious when these industry-wide common factors are viewed in the perspective of the special historical background of the Beijing's life insurance industry and are blended with it. Indeed, changes have only recently been happening in China and Beijing more specifically with regard to the insurance business.

The problems caused by the composite effects of historical factors and industry-wide specific factors in the life insurance industry are fourfold: a likely overemphasis of expansion in volume, a willingness to rely heavily on price competition, a poor reputation and poor operating efficiency .

5.1.1. Overemphasis of expansion in volume and heavy reliance on price competition

By analyzing the historical background of this industry and the resulting imperfection in the current market structure, I can identify some special factors which have contributed to the problems mentioned in the previous chapter.

As already mentioned in the introduction and in chapters 1 and 2, the history of Beijing's life insurance short is relatively short, only 27 years to be precise. In the beginning, only one insurance company was allowed to operate in the market and enjoyed a full monopoly. Moreover, during this initial period, this state owned company took large advantage of government assistance and preference. All these factors refrained other insurance companies from entering the market. Even now, the market concentration rate is still very high. The three biggest companies represent more than 75% of the total market⁴¹, which it is not supportive of a more competitive attitude and does not stimulate improvements in efficiency.

New participants entering the market can only sell the products allowed by the CIRC, which are identical to the ones promoted by the longer established big three companies. If they want to take a larger share of the market, the only option available to them is to compete outright with the big players by using price incentives as market tool, which finally leads to a very hostile competitive environment. The nearly exclusive use of this strategy by the insurance sector not only caused a considerable drop in insurance companies' profit margins, it also damaged its reputation seriously.

By overemphasizing expansion in volume to the detriment of others, another problem emerged. Since the industry has only limited resources, volume expansion is limited to the fastest possible growth allowed by the weakest link the insurance service process: capital or human capability. The lack of experienced human capital and resources currently poses the most important problem in this respect and is due to the short history of the industry, which did not have sufficient time to invest in better and enough human capabilities. Most insurance companies cannot satisfy the requirements of market development or in trying to do so anyway cause quality problems, aggravating the poor image of the life insurance sector and deteriorating the operating efficiency. We will take this point further in the next paragraph.

⁴¹ Beijing insurance industry development research

5.1.2. Shortage of human resources.

One of the disadvantages the life insurance industry faces in Beijing is a short supply of skilled workforce.

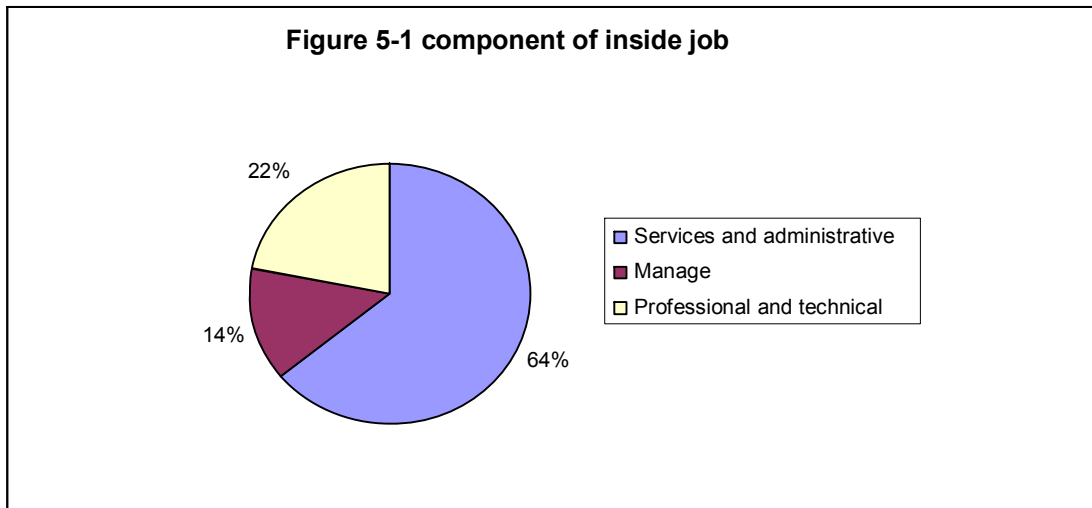
Although the Beijing insurance market comprises 52.137 staff, it accounts for nearly 40% of the total number of employees working in financial enterprises. More than 90 percent of them are sales personnel, and only 3,875⁴² are working for insurance companies directly. In spite of this it is very difficult for insurance companies to find qualified people to carry out the job. Taking this into account with the intensive growth in market demand and the fierce price competition going on, this huge shortage in workforce supply is not going to stop soon. Human resources are thus a critical concern to the whole life insurance sector in Beijing. The most pressing issues are the recruiting and training of competent staff and of staff working in the various distribution channels.

The supply of competent staff is indeed lagging far behind the rapid development of the life insurance market in Beijing. Professional knowledge and experience is very scarce. Two aspects can be described shedding more light on this phenomenon.

First, there are 509 managers among the 3,875 jobs in insurance companies, representing 14 percent. Only 2372 employees directly work in services and administrative departments (64 percent of the total) and a mere 22 percent (825 people) work in the professional and technical field⁴³ (*see figure 5-1*).

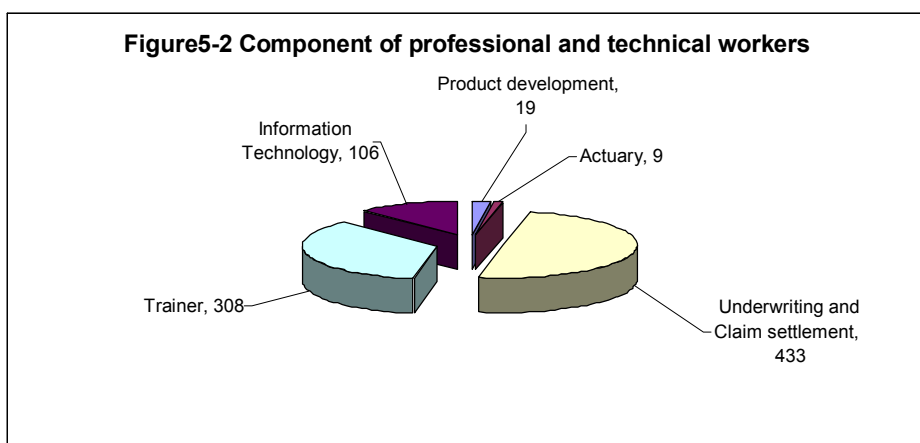
⁴² Beijing insurance industry development research

⁴³ Beijing insurance industry development research



Source: Beijing insurance industry development research

Secondly, of the total of 825 real professionals, only 19 people work in the product development sector, 9 are actuaries, 433 people work in underwriting and claim settlement and only 308 are trainers. Moreover, there are only 106 people responsible for information technology (see figure 5-2). Obviously, there is insufficient professional and technical staff leading to ineffectiveness and inefficiency. This is aggravated by the small number of trainers, leading to a large backlog of staff willing to be trained, but not capable of following the necessary training programs.⁴⁴



Source: Beijing insurance industry development research

⁴⁴ Beijing insurance industry development research

The result of this situation can be summarized in the following *table 5-1*, listing the major consequences of this insufficiency in experience, skills and training.

Table 5-1 the major consequences of this insufficiency in experience, skills and training

<i>Category</i>	<i>No. of staff</i>	<i>Resulting Problems</i>
product development	19	without enough product development ability, only can copy existing products no matter whether it is suitable or not
actuary	9	without enough risk management capability, the company will operate in a higher risk and unstable environment
underwriting and claim settlement	433	The company will operate again in a higher risk situation and will not be able to provide service and compensation on time. Claim settlement moreover is understaffed, leading to a bad image with complaining customers who are already very unsatisfied.
trainer	308	The salespeople cannot receive enough training, which will lead to a high turnover ratio.
information technology	106	There are no advanced information management systems and knowledge management systems in many companies, thus limiting improvements and product development in the system.

Source: own

5.1.3. High turnover rate.

Due to the lack of competent staff, each life insurance company attempts to acquire capable employees. An attractive salary, a higher position in the hierarchy and training abroad are the methods used predominantly to encourage people to enter a company. Furthermore, since the government regulations became less stringent since 2004, competition for human resource

capital has become fiercer: some foreign companies normally offer extremely high commissions and higher salaries to increase the number of their agents and employees as fast as possible and to hire the best people available on the market.

Given this situation, the turnover rate of staff was very high in last few years. It stands at nearly 25%, increasing competition in the race to hire competent people and meanwhile also disturbing the development and operation normal business processes. One personal example illustrates this situation amply: of the 20 people I used to know as colleagues at Ping An insurance, in last five years, only four people did not change jobs and four of them changed more than twice.

5.1.4. Agent systems

As mentioned before, one of the biggest differences between the Beijing life insurance business and the sector in other developed countries is the agent system. The system was introduced by AIA and developed very well in Beijing and the rest of China. Since many new companies were established, they had to hire a huge network of agents in order to sell insurance policies or contracts. Obviously, most of the success of the current life insurance industry in Beijing can be attributed to this agent system, but the system also caused many problems and restricted further development of the sector.

First of all, this system is very costly to many insurance companies, not only in terms of money, but also in terms of the necessity to train this new labor force, the difficulty and complexity of managing them and so on. If the insurance companies could focus more on the quality of their products and product development, they could provide the market with much better and more adapted services.

Second, there are fewer requirements for insurance companies to hire new agents than proper staff. Thus very often, the competence of these agents cannot be guaranteed. In addition, due to lack of training, some of the agents lack essential professional knowledge and skills and do not know how very well how to introduce and sell standards products, let alone specific ones. Sometimes agents thus cause misunderstandings between customers and companies.

Furthermore, in their eager to earning a living (based on commissions), some, though only a few of these agents, tend to cheat customers, providing them with illusive information. Of course this behavior can seriously harm the reputation of the life insurance companies and sector as a whole.

Thirdly, due to inefficient knowledge and experience, the turnover rate of agents is also very high. By the end of 2006, the agents having at least 6 years of experience only represented 10 percent of the total. The percentage of agents working more than one year for the same employer is only 22%.⁴⁵This very high turnover rate seriously disturbs the market and causes a further decline in the image of professional life insurance companies in Beijing.

Finally, for the new foreign insurance companies entering the market, it is necessary to choose the best local partners, who can build a viable and well performing network of agents. For them this is a prerequisite to become competitive with local companies. Based on their experience they are better in hiring and training the best networks, thus increasing the likelihood of local insurance companies facing even more problems in their agent networks.

5.1.5. The occurrence of fraud

Reliability is the cornerstone underlying the development of any industry, particularly the insurance industry. Suppliers as well as customers on the market should both pay attention to the long-term effect of unreliability. However, fraud by policy makers has caused losses to insurance companies and fraud in sales channels has caused loss to the insured customers recently. This problem mainly originates from the imbalance between information insurance companies possess and insured customers' posses. When fraud happens, the reputation of the business is seriously damaged and the development of the insurance sector is slowed down for a longer period because of the fading trust by customers in the system.

The above mentioned poor image of agents seriously harms the reputation of the sector in the society at large. Their unprofessional behavior, inefficient knowledge and skills, as well as

⁴⁵ primary information from survey

their tendency to rely on fraudulent statements to customers are not common, but still considered to be widespread by the industry and its customers.

Not everything offers such a bleak outlook nevertheless. In general, problems in the speed with which compensation is provided to customers, with efficiency and transparency of the system and with regulations have been addressed intelligently in the interest of protecting consumers in China thus sustaining a healthy and rapid growth of the insurance industry.

5.2. The importance of specific factors in the Beijing life insurance industry

I will summarize some of Beijing-specific factors aggravating the problems previously mentioned as being predominantly present in the Beijing life insurance industry and also aggravated by them. They are: problems in product development, problems encountered by foreign companies entering the market and the regulatory influence of the CIRC.

5.2.1. Product development problems

The main problem in product development in services in general and in the life insurance business in particular is that very often the costs of innovation are spent by individual companies, whereas the benefits are shared publicly. This is amongst others due to the fact that new products cannot be patented in a service environment as they are intangible in nature and due to the poor protection of knowledge based rights all over the world. The motivation to create really new products is thus very low.⁴⁶

At present, more than 100 different life insurance products are offered on the Beijing market, but customers still seem to have a limited choice. At first glance, this seems very illogical indeed, but since many companies only offer very similar products and do not want to invest heavily in new product development, it is true nevertheless. Moreover, when new products are offered, in many cases they are just copies of existing contracts offered in foreign countries. This does not necessarily take the difference between the Beijing area and other countries into

⁴⁶ Earl Sasser, Jr. (1995). Why Satisfied Customers Defect

account. Furthermore, most companies only copy those products that are selling better, and make little change to them when launching their equivalent.

Each time a company creates something really new and launches it on the market; others copy it immediately at nearly no cost at all. Moreover, the latter companies can rewrite or change something in the basic contract and thus improve the product slightly by just integrating elements they learn from the initial market response. This brings even more extra benefits to the latter companies at nearly no cost at all, while the innovating company just has to spend more to learn from their initial experience, thus incurring an even larger research cost. It is rather unfair but unavoidable and diminishes the motivation to develop new products. This problem largely limits the development of the life insurance industry at large.

Another objective reason limiting the efficiency of the research and development process exists. It is true that research and development of insurance products needs a lot of empirical and statistical data, interpreted by staff capable of creating information systems and data (professional actuaries and computer specialists), which are scarce on the Beijing market.

The competition among life insurance companies thus is not primarily focused on the product and service quality, but mainly on aggressive price and premium competition, leading to an even larger scarcity in funds to develop new products. This is a vicious negative cycle!

5.2.2. Constraints foreign insurance companies meet when entering the Beijing market.

There exists an important conflict within Chinese economic life and the insurance market in particular between on the one hand promoting competition and on the other hand protecting the local industry.

The Beijing life insurance market certainly has a huge development potential and promises a healthy profit margin to foreign insurance companies, consequently they certainly would like to enter this market and take a share of this “big insurance cake”. But ever since the start of the opening of the market to them, foreign insurance companies in China have been facing a lot of regulation in nearly all of their business aspects and operations. Thus they cannot freely

compete with domestic insurance companies: the restrictions imposed on them do not put them in a fair competitive position. This situation limits their initial enthusiasm and curtails development opportunities in the sector.

Since China has entered WTO in 2001, protectionist mechanisms have been relaxed little by little. However, there are still more barriers for foreign insurance companies than in other sectors of industry. For instance, the foreign companies must be operating at least 30 years in their home countries. Moreover, they cannot enter the Beijing market when their financial structure shows a 100 % foreign capital ownership, the only exception to this rule being AIA, the first foreign company that invested in the Beijing insurance market. In 1999, the Chinese government changed policies on the basis of this example and now imposes foreign investors in the insurance business to form a joint venture with a Chinese partner. This is of course a good policy to protect Chinese insurance companies and to promote the growth of domestic insurance companies, but at the same time, it causes more restriction on foreign insurance companies.

The Chinese government acknowledges this problem by stating that:

“There are still many factors that frighten foreign insurance companies to enter China including branch/sub-branch establishment procedures, capitalization requirements, the Chinese pension system, health insurance underwriting policies, and limited rulemaking transparency. All foreign companies encourage the China Insurance Regulatory Commission (CIRC) and relevant authorities to resolve these remaining issues.”⁴⁷

This white paper states a number of restrictions foreign investors in the insurance business face when entering the Chinese market. The authors specifically cite the following two: consecutive branch approvals and capitalization requirements.

The consecutive branch approvals

Foreign insurance companies’ branch approvals have always been made consecutively by Chinese authorities. In general, one approval is normally one per year, in spite of applications

⁴⁷ WHITE PAPER 2006 • AmCham-China

to establish different branches at the same moment. This policy seriously curtails the growth potential of foreign insurance companies in Beijing and in China in general. Compared to foreign insurance companies, the domestic ones easily receive permission to build a network of several branches at the same moment.

Capitalization requirements

Before China entered the WTO, the capitalization requirements for foreign insurance companies were very stringent. After 2004, standards were somewhat revised however. Currently the capitalization requirements for the initial establishment of a foreign life insurance company in Beijing stand at RMB 200 million (a reduction from the previously required RMB 500 million). For separate branches the requirements were lowered in 2004 from RMB 50 million to RMB 20 million.⁴⁸

Obviously, these reductions of capital requirements relaxed the limitations imposed on foreign life insurance companies somewhat, but the current requirements is still a lot higher than in other developed countries. Moreover, the experience from other countries proves that high capitalization requirements serve little to and are inefficient in ensuring financial stability and solvency of the business. Finally, they are highly unfair to potential new entrants, thus endangering future development of the Beijing life insurance market.

All the above mentioned problems do not only put the foreign insurance companies in an unfair competitive position, they also reduce their competence by further limiting their right to freely develop suitable products for the market. Furthermore, the inconsistent treatment between foreign and domestic insurance companies in fact violates WTO rules on the treatment of foreign companies, a set of rules to which China has committed itself as a nation when entering the WTO.⁴⁹

⁴⁸ China insurance regulation committee

⁴⁹ WHITE PAPER 2006 • AmCham-China

5.2.4. China insurance regulation committee (CIRC)

CIRC's position itself on the Chinese insurance market does not make this situation any better at all. In fact, CIRC is serving both as custodian of the industry and as regulator at the same time.

In the start-up period, the life insurance industry in Beijing behaved like an “immature child”: it badly needed “parental guidance from authorities”⁵⁰ to nurture its healthy and swift growth. At that time, many policies and regulations had to be established to achieve this objective. They were remarkably successful. Since then, the requirements of adjustment in policies and control have completely changed due to the rapid growth of the life insurance industry. Currently, the regulator's responsibilities should predominantly lie in the correction of some market failures. Control is largely redundant, but has not changed drastically from the start-up period. This leads to restrictions in development.

Serving both as the custodian of the industry as well as a regulator, CIRC faces some problems. As a department of government, it hopes that the industry develops fast, but it cannot guarantee its performance and efficiency. This aggravates the above mentioned problem of emphasis on volume at the cost of sacrificing profit margins and good reputation. It wants to protect domestic insurance companies, but knows that their efficiency can only be improved by increased competition. It wants to keep insurance assets safe but cannot provide enough return on investment to insurance companies due to its stiff regulation. CIRC is clearly doing a very difficult job balancing the management of risks with the generation of protection to domestic companies (and thus again generating new risks).

It is a complicated task to improve its performance when faced with opportunities of new development. Obviously, the original policies of supervision cannot nurture an environment positive to new developments. It is necessary for CIRC to change its direction and manage the promotion of the life insurance businesses' growth better and more intensely. As the insurance regulator, the current goal of CIRC to enhance its regulatory regime is not sufficient

⁵⁰ Mark V.T. Saunders, Eric Lu, China's insurance market- The giant awakens

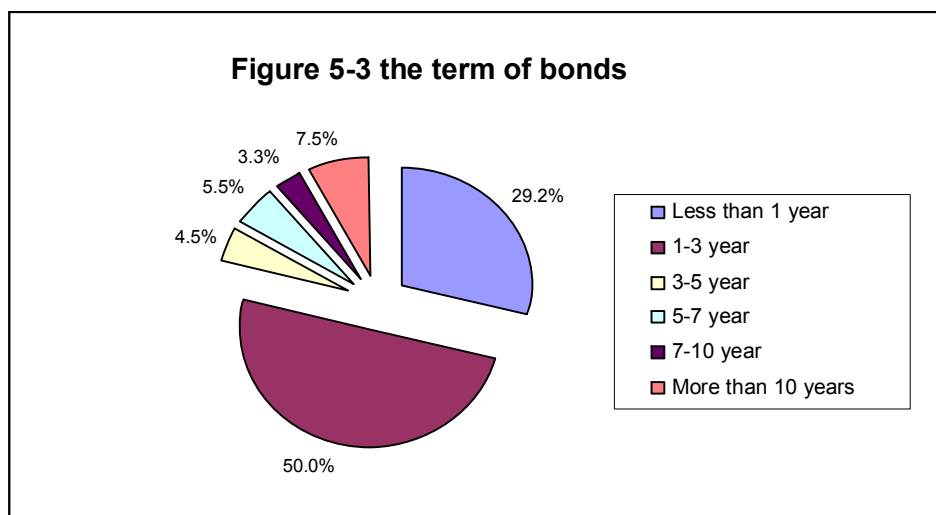
and rather inadequate to meet the challenges of a dynamic and competitive marketplace. There is still a long way to go for CIRC.

5.3. Specific factors external to the Beijing life insurance business.

In this section, I identify several external factors that may have imposed constraints on the growth of Beijing life insurance industry.

5.3.5. The financial market in China poses high risks and has an imbalanced structure, thus constraining development of the insurance business sector.

The premium volume collected by insurance companies actually serves to provide policyholders with protection, compensation and annuity. All these payments are based on profit those companies realize from their investments. At present, insurance companies are confronted with big challenges to do so. There is a lack of suitable investment channels, and it is difficult for insurance companies to earn enough money because of the price competition on the market (mentioned before). CIRC moreover requires insurance companies to deposit most of their money into bank deposits to keep investments safe, but the result of this policy is that insurance companies can only get little interest. Even when CIRC loosened this requirement in 2005, insurance companies still faced a severe shortage of potential assets, specifically in long term investment. This is visible in *figure 5-3*



Source: *China bond market yearbook 2007*

Due to the structure of the long-term assets of life insurance companies, the best investment tool for insurance companies at the moment are bonds, but there are not enough long-term bonds available in China. Only 7.5% of these bonds represent investments with a lifespan of over 10 years⁵¹. Moreover, it is forbidden for insurance company to invest in foreign bond and foreign capital market. The lack of investment channels thus seriously damages to the profit margins of insurance companies.

5.3.6. Taxation issues

The taxation policy of the Chinese government also impacts the demand and supply structure of the market for insurance products and its support of the industry.

At the moment, the Chinese governments' taxation of both employers and employees' pensions badly influences the implementation of pension systems.⁵² This stands in contrast to fact that the premium of life insurance allowances is tax-free in other developed countries. The development of the private pension systems in China still needs further authorities' support.

Currently, in the commercial sector, pensions provided offered by employers to employees have already become a strategy to hire the most competent employees, since it provides them with additional, employer-sponsored retirement income without supplementary costs nor assistance from the state. More and more companies have begun using this method in their process of engaging and keeping the most experienced workers. The development of such a "commercial (private)" pension system also offers growth opportunities for the life insurance industry. As Beijing is one of the more rapidly developing cities in China and the market for employees has become competitive, this private pension system is particularly interesting for the Beijing's business sector. But, as previously mentioned, taxation systems still obstruct the development of this system.

⁵¹ China bond market yearbook 2007

⁵² primary information from survey

A more favorable tax environment would give customers the incentive to purchase more insurance services. Actually, from a societal point of view, a “commercial” life insurance package covering health and old age issues would be very complementary to the existing social welfare system in China. It would be good to government in keeping costs of the welfare system down and to social stability as well. This is all the more true since the current Chinese social welfare system cannot satisfy all the needs of people. If customers would perceive insurance as a well performing savings product with protective characteristics for their old age, they would be willing to subscribe more insurance policies.

5.3.7. Awareness among customers of insurance systems and their opportunities.

Although the life insurance business exists for more than 25 years now in Beijing, some potential customers still do not understand its importance and characteristics. From a sociological perspective, Beijing’s special social structure has a large impact on demand and supply of insurance services, as well as on the social psychology and traditional ideology of social groups and individuals in Chinese society.

As a communist country, the Chinese government does not put emphasis on insurance systems since the party came to power in 1949. The communist party and government believe “everyone has to work and then get everything for free”. The first Chinese government thus closed all insurance companies and started to provide “free healthcare” to the people and looked after the aging people as well.

No matter how great and advanced this idea seemed, it was ill suited for the China of the fifties with weak economic growth and a large population. This system could only provide in a very low protective level to the people and was not always able to maintain its lowest level from 1956-1978.

In 1980, the life insurance system became more market oriented again, and at the same time, the kind of “free healthcare” and “free care for aging people” began to fade away gradually. However, the consequence of the existence of such a free system between 1949 and 1980, is

“unawareness and unacquaintance of a whole generation of Chinese with insurance services” Many Chinese still do not understand the concept and value of life insurance nowadays and they still prefer saving all their money in bank accounts to prepare for the education of their children, the purchase of a house, and their needs when they start aging. They do not understand nor believe that life insurance can achieve identical or even better results as saving, and even when they do believe it, it is still difficult to change habits easily. This will still be the case for many years without special efforts in “selling” the idea of life insurance to the public. Consequently, the current social structure in China and Beijing in particular has fundamental negative implications to the mid-and-long term growth of the Beijing life insurance industry. This effect will be prolonged in the near future, but it will diminish over time.

5.3.8. Inequality between rich people and poor people

A big gap exists in China between rich and poor people. Wealth distribution is very imbalanced in China. GINI Index is used to measure the income inequality, from 1978 to 2004; the GINI Index has already increased from 0.16 to 0.468⁵³. Moreover, income equality is still increasing. A very large inequality in income exists between rich and poor people in Beijing. Many people are still living in poverty, and there are big also a lot of people only working to support a basic living standard. Based on current growth models in Beijing, this problem cannot be solved in the immediate future and it will still exist for a sustained period of time.

For these poor people, life insurance is still not only a relatively new concept. They also have no clear idea of its benefits. Moreover, even when they understand the benefits, life insurance is not their primary need either. They have to use their income for daily expenses. In other words, they cannot afford life insurance, unless their income would substantially increase.

⁵³ The abstract of China statistics (2005)

Chapter 6 Development Prospect for the Beijing Life Insurance Industry

Undoubtedly, Beijing will keep growing economically at a rapid rate due to globalization, industrialization, urbanization, better education standards, technology reformation and social transformation. Moreover, as the city hosting the 2008 Olympic Games innumerable economic benefits will accrue to Beijing. In this chapter, I will carefully discuss these macro-economic opportunities for the life insurance business in Beijing.

In recent years, the life insurance industry has continually grown in the annual rate of more than 30% in Beijing. Moreover, this growth continues to be fueled by Beijing's rapid economic expansion, by changing demographics, social welfare reforms and by a more supportive regulatory framework.⁵⁴The life insurance market in Beijing is large; it grows rapidly and offers plenty of opportunities to all the insurance companies. This chapter will discuss these opportunities from the prospective of an environment being in rapid change due to economic and social development.

6.3 Social factors influencing the insurance business.

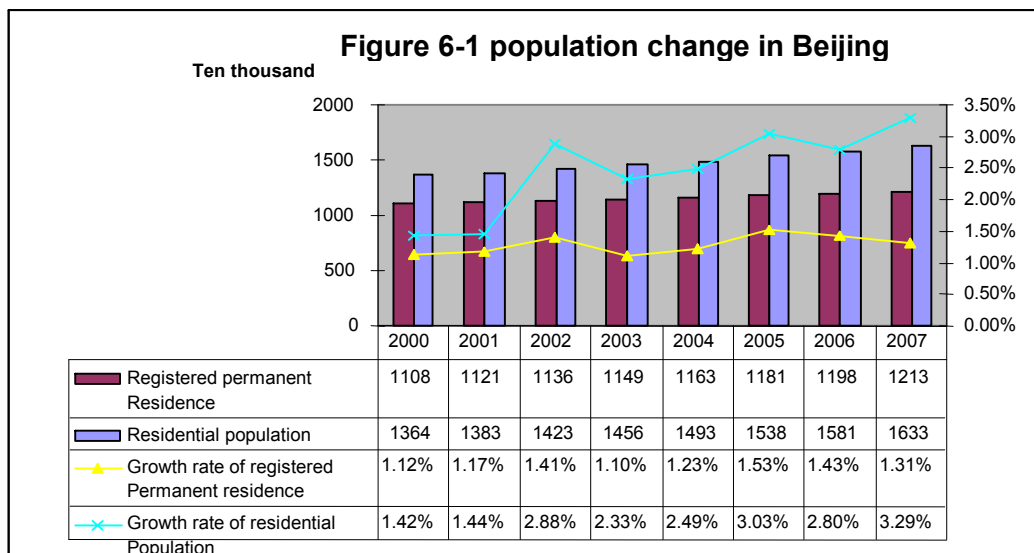
6.1.2. Continuous growth of the population

The continuous growth of the population will provide a large opportunity for the life insurance business as the market will grow in volume. But when talking about population in Beijing, one thing we should notice is that there are two terms "Registered permanent residence" and "residential population". This is a specific Chinese characteristic. The difference is the following: "Registered permanent residence" refers to people who got a legal identity card to stay in Beijing, whereas "residential population" refers to people staying more than a half year in Beijing for working, studying or some other purposes and who do not possess a local identity card. Bearing these two terms in mind, readers can more easily

⁵⁴China's insurance market –the giant awakens

understand the current population situation in Beijing and will not be confused about the reasons why population increases so fast in Beijing. Most literatures only focus on the first category.

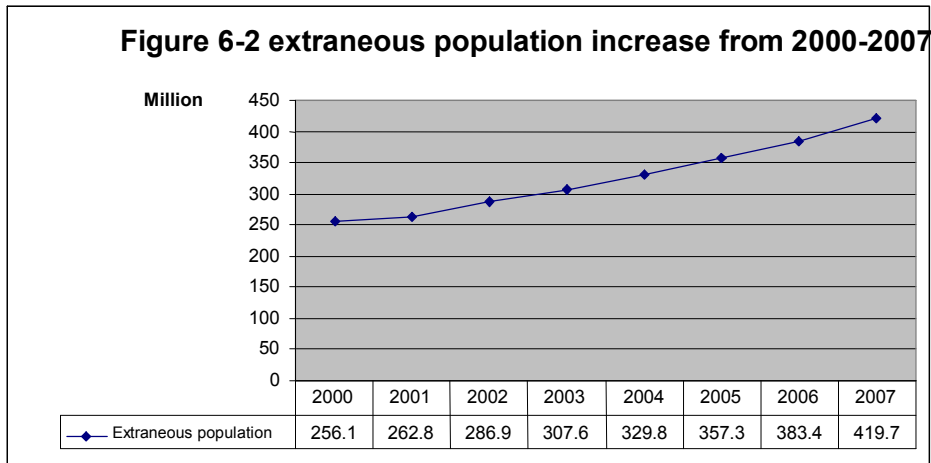
“Registered permanent residence” did not increase so fast in Beijing. Annual growth only stands at 1.31% in 2007. But the growth rate in residential population was much higher than that. It stood at 3.29% in 2007. According to demographic data, the total “residential population” in Beijing is more than 16.33 million, nearly 1.5 times of the Belgian population, “Registered permanent residence” was only 12.13 million.⁵⁵ (See figure6-1).



Source: *Beijing statistical yearbook 2000-2007*

As the capital of China, Beijing attracts millions people to work. The preparation of the Olympic Games in 2008 needed millions of workers, also on extraneous people (see figure 6-2) .According to the Chinese definition, these people are “residential population” rather than “Registered permanent residence”. But the “residential population” is also potential customers for life insurance products.

⁵⁵ Beijing statistical yearbook 2000-2007



Source: *Beijing statistical yearbook 2000-2007*

The relationship between population, its growth and life insurance premium can be statistically investigated. The correlation coefficient between population and life insurance premium is 0.907 ($p\text{-value} = 0.0018$). Thus the correlation is very strong.

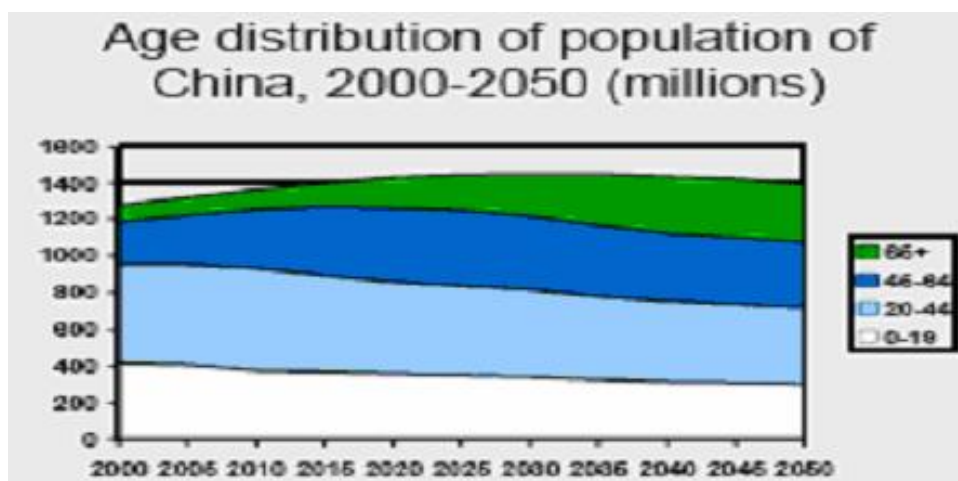
6.1.2 Appearance and growth of middle- class people

As the political and economic center in China, Beijing offers more potential development opportunities and relatively higher salaries. As a consequence, Beijing has a very rapidly growing middle-class. The middle-class society, which did not exist before, is composed of higher-education and higher-income people. They need better protection of their income and more specific health insurance schemes. Furthermore, they like to invest their money in lucrative investments much more than in bank savings, as many other people do in China. Generally, insurance is viewed by them as an interesting investment option. As this middle class keeps growing in Beijing and constitutes the main segment of the market targeted by life insurance companies in the future, demand for life insurance products is expected to keep growing as well.

6.1.3 The growth of the aging population in Beijing.

Due to the one-child policy and significant improvements in living standards, China's aging problem becomes more serious than in many other countries of the world. In 2000, the old age population (65+) represented 6.96% of the total population. Many countries have entered the stage of a society before, but the speed with which this happens in China is much faster than elsewhere. The average growth in aging population on world level is 2.5 % on world level, according to UN estimates, whereas in China it will be 3.3%.⁵⁶(See figure 6-3)

Figure 6-3 age distribution in China



Source: Chris Daykin, *the Ageing Society of China and the role of the Actuarial Profession*

Moreover, the situation is more serious in some major cities like Beijing than in China as a whole. The aging population represented 8, 4 % of the population of Beijing in 2000; it was 8.9% in 2001 and 10.4% in 2002. If this growth rate continues, it will be nearly 25% in 2020.⁵⁷

Obviously, Beijing did not prepare well for this problem. The government cannot provide enough pension and health care for 5 million people under current social security regulations and social welfare policy, which gives a wide covering at a rather low level. Moreover, this system only is implemented for urban people. People living in the countryside of Beijing cannot enjoy the same advantages when they grow old. They must rely on their own savings and on their family much more. People living individually do not have the support of their

⁵⁶ Wang Chengsi, *Speedy Aging in China: Its Problems & Policy*

⁵⁷ China national committee on aging

children and care which habitual families enjoy at home. A normal Chinese family pattern consists of a 4-2-1 structure, meaning that the composition is 4 grandparents, 2 parents, 1 child.

The importance of life insurance systems is clearer in view of this development, certainly in the Beijing areas. Individual households and aging people clearly represent an interesting segment as well.

6.1.4 People live longer

Due to the modern health services and significant improvements in the living standard, Chinese people live longer than before. At the end of 2005, the Chinese insurance business started implementing a new mortality table. The new life mortality table is derived from 100 million life insurance contracts owned by six big insurance companies from 2000 till 2003 (see table 6-1). This table indicates that life expectancy grew significantly since 2000.

Table 6-1 China life mortality table

Life Expectancy and Impact:	1993 China Life Ins. Mortality Table		2003 China Life Ins. Mortality Table	
	Male	Female	Male	Female
Expected Age	74.9	79	79.7	83.7
Increase (redefines retirement income need)			+4.8	+4.7

Source: 1993 China life mortality table and 2003 China life mortality table

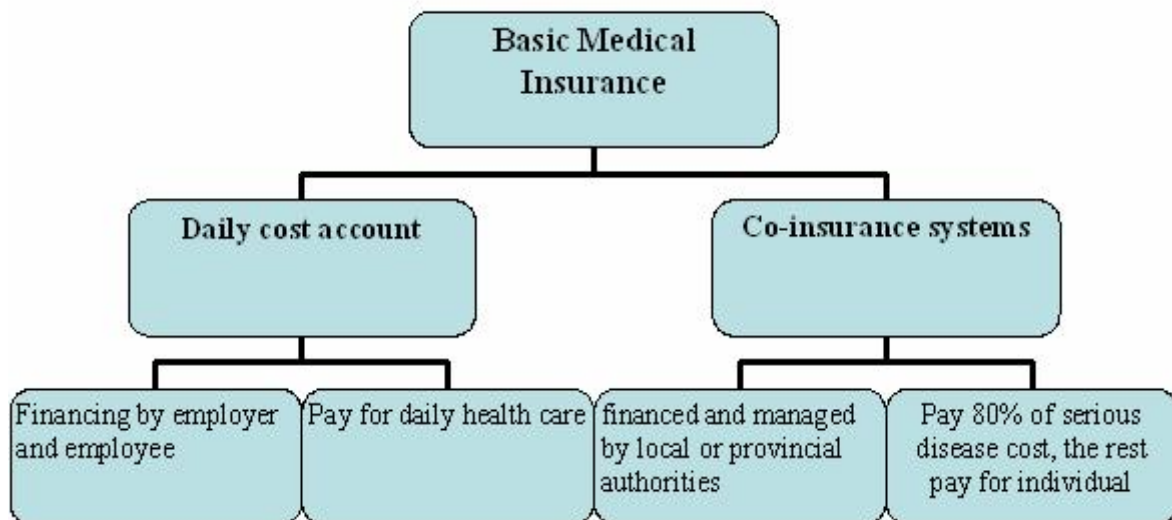
Comparing to these data to 1993, indicates that Chinese men live 4.8 years longer now and women live 4.7 years longer. For insurance companies it is a fact that the longer people live, the more pension and health care they need, the bigger potential market will be.

6.1.5 Health insurance system changes

The Chinese government began implementing the “Basic Medical Insurance” system⁵⁸ at the end of last century. Basic medical insurance consists of two parts: “daily cost account” and “co-insurance systems”. Urban employers pay extra money for their employees to fund a cost account monthly, on the other side, employees also need to save extra money into this cost account monthly. Currently, employees pay 4% of their monthly salary and employers pay the 8%. Day-to-day health costs are paid from this account.

If employees get seriously ill, the co-insurance system begins to use. Nearly 80% of the specific expenses will be paid by the co-insurance system however. This system is financed and managed by local or provincial authorities; the rest is paid by employees themselves.

Figure 6-4 basic medical insurance system



Source: China's basic medical insurance system covers 221 million people

Basic medical insurance provides a very basic health protection for urban employees, just like its name indicates. It also has many limitations in expenses for medicine, medical devices, surgical methods and material and so on. It also does not pay for Computed tomography (CT), magnetic resonance (MRI), CDI/CDF and other advanced medical examinations. In one word, Basic medical insurance does not pay for any expensive cost, no matter how well the clinical effect is.

⁵⁸ China's basic medical insurance system covers 221 mln people, <http://www.chinaview.cn/>

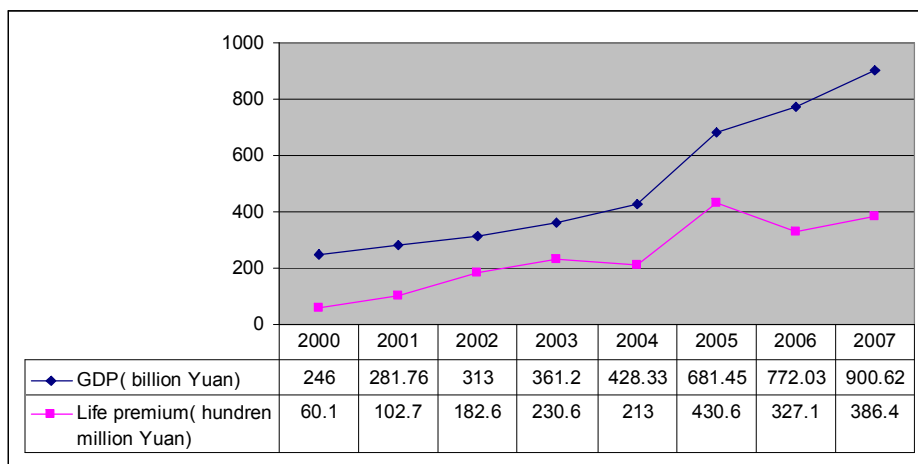
According to the WHO, China’s health care ranking is 144 out of 190 countries⁵⁹, and it is really difficult for common Chinese people to pay for the very expensive medical costs. Under these circumstances, health insurance has already become the most important insurance market in China. With more than 4 million of “floating” population in Beijing, who urgently want to find some protection for their health risks, the prospect for the health insurance market in Beijing is bright.

6.2 Rapid Economic Growth

6.2.3. Anticipation of fast economic growth

As mentioned before, the level of development of the insurance industry is ultimately determined by the level of economic development and the level of consumer recognition. The growth of Beijing life insurance industry closely relates to the increase in economic because the high economic growth will increase the income of the insured and thus increase the demand for life insurance service. The healthy, quick increase in economic is the foundation of the growth of life insurance. The correlation relationship also can be found in *figure 6-5* .it clearly shows that the volume of life insurance premium increases with the growth of GDP.

Figure6-5 life insurance premium increases with the growth of GDP



Source: Beijing statistical yearbook 2000-2007

⁵⁹ WHO website

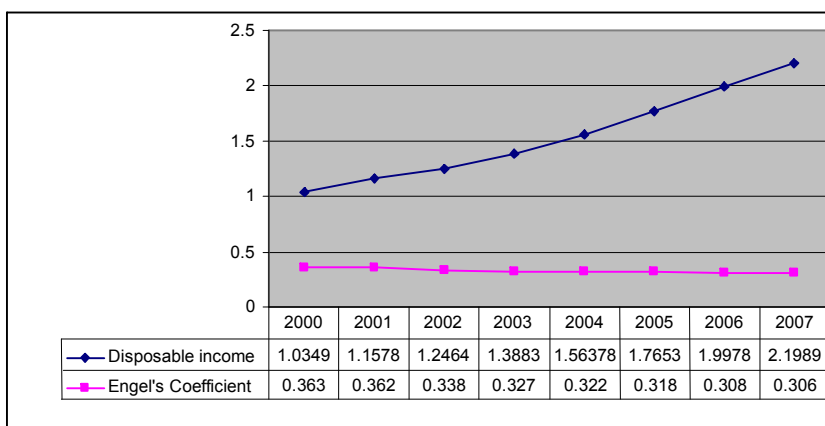
Undoubtedly, this trend in economic growth will not stop in the near future. According to current economic predictions, the economy in Beijing will maintain high growth figures for at least the next 20 years, which will provide guarantee strong growth in the life insurance business as well.

According to a survey of all the insurance companies, they expect the Beijing life insurance market to continuously grow in the future, in concordance with growth of GDP in China.⁶⁰

6.2.4. Growth in income

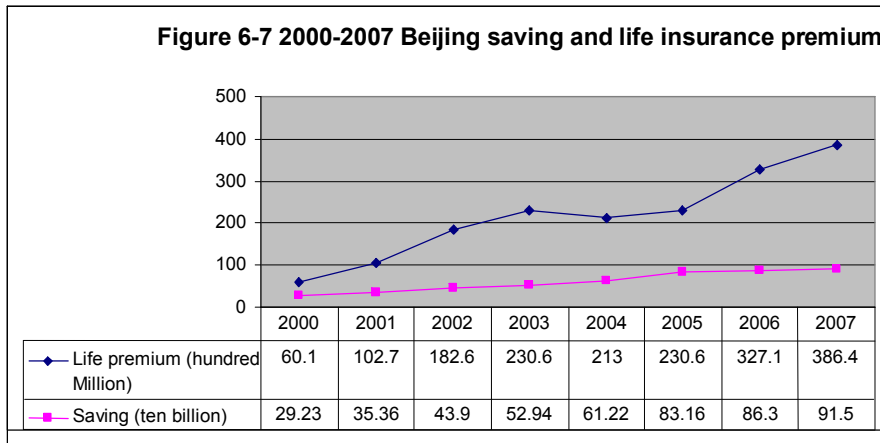
As a consequence of the above mentioned economic growth, life of people in Beijing has changed dramatically. The people's living standards have been improving and disposable income increased, while the percentage of expenditure for basic living costs in total personal expenditure has decreased considerably in all income categories. *Engel's Coefficient* was used to present this fact, (see figure 6-6). From 2000 to 2007, the average disposable income of people in Beijing nearly doubled and Engel's Coefficient decreased constantly.

Figure 6-6 Engel's Coefficient and individual income



Source :beijing statical yearbook 2000-2007

⁶⁰ Nian-Chih Yang, Chinese Insurance Market: Opportunities and Alternatives



At the same time, we also see that bank savings have also increased dramatically. Figure6-8 shows this phenomenon. Due to the fact that insurance can be considered as an alternative to bank savings, one can expect that more and more money will eventually be invested in life insurance funds in the future. This is shown clearly in the figure and statistical correlation tests also show the correlation existing between savings and life insurance premium. The correlation coefficient between them is **0.921 (P-value=0.001)** .

To some extent, life insurance is a “luxury” product: customers must have enough money to be able to afford it. The more money people own, the more they think about safeguarding their savings and the interest they can get on investments. Both theoretical approaches and experiences from other countries’ life insurance industries show that when people’s average income levels are high enough, there will be a tremendous impact on the life insurance industry.⁶¹ According to the growth levels in Beijing, this further development can be expected soon in Beijing, maybe just in 5-10 years.

6.2.3. Need for new investment channels

As mentioned before, people’s disposable income in Beijing has increased dramatically, which leads them to think about how to use their money wisely. For common people in Beijing, there are only limited investment options to choose from. People still like to save money in bank accounts and sometimes invest in the stock market. Compared to the above

⁶¹ China Life Insurance Industry Development Report, 2007

mentioned 12% investment rate in life insurance business in other developed countries, at present, the proportion of investments in life insurance is only 7% in Beijing. Nearly 93% of the financial assets of residents are thus deposited in banks or invested in stocks.⁶²

But the results of investments in these two investment channels are not necessarily good, interest rates of bank decreasing continuously. Currently, the interest rate for a one year deposit stands only 4.3 %. Moreover, government tax stands at 20% on interests. Finally, the real interest rate is only 3.4 %, ⁶³which cannot satisfy many customers forever.

On the other hand, although the stock market exists since 15 years in China, it is not as well developed as in other developed countries. People cannot earn money as these markets are still very instable, most stock prices are overvalued, corruption and business based on internal knowledge are very common. Moreover, a transparent and scientifically based stock market system was still not established in China. The political factor still heavily influences the stock market and big investors control the development of the stock market. Moreover, the immature Chinese stock market can not follow the international market transition, this cause more fluctuation in the market. This problem became more seriously in last 12 months. The stock markets' index changed dramatically, and millions of people lost much their investment. (See figure 6-9).

Figure 6-8 stock market index in China (from Jan, 09, 08 to May, 23, 08)



⁶² Beijing insurance industry development research

⁶³ China Bank

Source: <http://finance.sina.com.cn>.

Due to low revenues from investments in both bank accounts and stocks, more and more people are beginning to look for alternatives and to switch their investments from traditional investment channels to the life insurance sector, a phenomenon that will be strengthened in the future when the underlying reasons do not change fundamentally.

6.3 Changes in the law and government Policies

6.3.1. Changes in the authority of CIRC

Some changes have already been made to the strategy followed by the CIRC since 2006. Previously we have already explained the role of CIRC, in this section we will describe the major regulatory measures taken by it since 2006. The information source is the website of CIRC. ([http:// www.circ.gov.cn](http://www.circ.gov.cn))

I. Measures to Boost the Insurance Industry.⁶⁴

Adhering to the market-oriented principle, the CIRC has adopted a series of policies and measures to accelerate development of the industry and has made breakthroughs in tackling problems and removing obstacles endangering the development of the insurance industry.

- (1) Improving the Market Access Mechanism*
- (2) Broadening Insurance Fund Management Channels*
- (3) Increasing Financing Channels of Insurance Companies*
- (4) Pushing forward Administrative Reform*

II. Measures to Strengthen Risk Prevention

The CIRC considers risk prevention as a project of systematic engineering and tries to build 5 lines of defense against risks, namely, internal control as the basis, supervision of solvency

⁶⁴ CIRC, [http:// www.circ.gov.cn](http://www.circ.gov.cn)

and adequacy as the core, on-site inspection as an important means, fund management regulation as a key link and insurance security funds as a protective screen.

(1) Strengthening Internal Management

(2) Strengthening Supervision of Solvency Adequacy

(3) Reinforcing On-site Inspection

(4) Strengthening Supervision of Fund Management

(5) Establishing and Improving Insurance Security Fund System

All insurance companies look forward to the relaxation of regulation as one of the most important changes in last few years. The desire to increase the number and diversity of investment channels and the willingness to accept stronger competition for new domestic companies both present a big opportunity and incentive for foreign insurance partners.

6.3.3. Changes in the financial market

Some regulations were changed or suppose to be changed in the not so far future, such as the acceptance of more diversity in investment channels, the percentage of preparation fund,(which means the capital saving to China people's bank, it is obligation for china insurance companies for reducing the risk), consolidation of the financial industry and so on. CIRC is concerned about these problems and their potential adverse impact on the industry and is trying to improve the situation by:

- *allowing insurance companies to invest in AA-rated (or better rated) corporate bonds and increasing the acceptable limit to 20% of the company's assets*
- *proposing that the State Council (China's governing body) allows insurance companies to invest in major infrastructure projects*
- *Studying the feasibility of allowing insurance companies to invest in the overseas market, despite the foreign exchange risk. There is also concern about funds being drained out of the domestic market and the impact off foreign exchange controls.*

- *Allowing the list of insurance companies to invest in the stock market, so that they can draw funds from the stock market.*⁶⁵

The pace of development is remarkable. A major change occurred when three big domestic insurance companies (PICC, Ping An and China Pacific), were listed on the Chinese, Hong Kong and New York Stock exchange. It is the beginning of the financing of domestic insurance by other financial resources from both China and the global financial market. Moreover, there are a few companies waiting for further approval.

These regulatory changes will relax restrictions considerably and permit life insurance companies to actively use more investment opportunities. They enhance the ability of life insurance companies to earn more money and will have a positive impact on investment performance. Insurance companies will also be capable of focusing more on long-term investment methods and opportunities.

6.4 Product innovation and growth of insurance companies

Both factors are specific and influence growth on the Chinese life insurance market.

6.4.1. Product innovation

With the development of the life insurance products, currently, beside of his protection function, life insurance also can harness savings, facilitate efficient use of capital funds, and therefore act as a new kind of financial tool.⁶⁶

Currently, the life insurance industry in Beijing offers a wide variety of products which range from basic protection to investment tools. Besides got protection from the traditional

⁶⁵ Mark V.T. Saunders, Eric Lu, China's insurance market- The giant awakens—restate CIRC's policies

⁶⁶ Anthony Lau, Universal Life Insurance - A Tool For Wealth Management

insurance, the customers share the profit of insurance company and gain much more flexibility, such as to increase or decrease coverage, to choose premium payment, or to achieve high economic return when insurance company gain in investment and operation. So the Investment-Linked Insurance and Equity-linked Insurance is good tool for both protection and investment. Meantime, the insurance industry also changes his position from “product seller” to “financial planner”. Moreover, the income from insurance is tax free in China, which gives incentive for customer to buy this new product.⁶⁷

From the aspect of social development, this new product also caters for the need of people. With the enhancement of living level and health science, the predict life is longer. At this situation, people need to prepare for his agedness, and insurance industry also need to provide the protection for people’s wealth after retirement. The new product satisfies both insurance companies and customers, which both gives survival return and mortality charge⁶⁸

6.4.2. The increase of the number of insurance companies in Beijing

Due to its the huge population and rapid economic and social development, China has already become one of the most attractive markets in the world, also for life insurance. Beijing takes a particular place in this market and as we have previously mentioned the number of insurance companies and the volume of insurance premium have dramatically increased. Growth prospects are immense and stand an estimated 20 % over the next couple of years. Many domestic and foreign insurance companies are already present on the market and many more wait approval of their entry. With more players on the market, the market will also become more dynamic as new products will be developed and thus new customers interested. The structure of a more open market always creates growth opportunities by the openness itself.⁶⁹

⁶⁷ Anthony Lau, Universal Life Insurance - A Tool For Wealth Management

⁶⁸ Lawrence J, Variable Universal Life (VUL)

⁶⁹ Angelo Unson, liu yufeng, China insurance market review

6.5 Beijing 2008 Olympic Games

Finally, one very important factor temporarily has great influence on the prospects of the insurance market in the Beijing area. As host city of the Olympic Games, many new projects in building and renovation of the city have been undertaken and a lot of workers temporarily reside in the area. They will not all leave the city later and thus present potential customers. Moreover the Games will increase the GDP of the area substantially in 2008 and probably later as well although at a lower level. In this section the influence of this specific factor on the insurance market is described in following aspects:

1. The budget for 2008 Olympics games is 20 million dollars⁷⁰, it will directly increase insurance companies' margin income.
2. Based on the research of Liu Jinsheng⁷¹, Olympic game can directly promote local insurance market long-term development through increasing insurance awareness and enhance economic development.
3. Olympic game promotes international communication and brings more open international environment and more foreign investment, and then promotes insurance development.
4. Olympic game promotes the perfection of regulation and policies, provides good opportunity for insurance industry regulation system.

6.6 Natural disaster

On 12,May ,2008, eight-magnitudes earthquake happened in Sichuan province, China, and caused serious people casualty and property damage, nearly half of China all perceived the earthquake in different magnitude at the same time, including Beijing city.

⁷⁰ China Olympic Committee

⁷¹ Olympic economic and Olympic insurance

This serious natural disaster and results awaked people's insurance awareness. Based on the information provided by my original colleagues, the sales status of life insurance increased largely in last 10 days, was nearly 2.5 times ⁷²than average level.

⁷² primary data from consultant

Chapter 7 Medium Term Growth Potential of the Beijing Life Insurance Industry and Sector

From the previous chapters we can conclude that the insurance business in Beijing is booming and has bright future growth prospects because of many different factors. But how fast will this market grow? A quantitative research model will be applied in this chapter to predict the growth of the life insurance sector in Beijing in the next five years. A few statistical models for prediction can be constructed to achieve this goal: they will be presented and an evaluation of previous equivalent research will also be performed.

When constructing a statistical method to predict the life insurance industry growth in Beijing in the next five years, many influencing factors must be taken into account.

These factors can be subdivided into three categories:

- economic factors, including GDP, average income, interest rate, CPI index and so on;
- social factors, including insurance awareness, educational level, government policies and the social security system and so on; and
- Supply in the insurance business, including the number of insurance companies, the types of products and services offered, the pricing system and competitive situation of the market.

The influence of insurance supply will not be discussed in this chapter. I will try to predict the future development of the industry mainly from the point of view of premium volume.

Normally, two approaches can be used to analyze the potential development of premium volume in the insurance: a method using a statistical regression model⁷³ and the key index method⁷⁴. I will implement both of them to analyze the potential of the Beijing life insurance industry.

7.1. The method using Statistical regression analysis

⁷³ Liu wei ,China insurance industry development status and premium development prediction

⁷⁴ Qiu xiaohua , Chinese insurance development perspective analysis, yu ziyou, the change of insurance depth and insurance density and the prediction of China insurance market

In this section I first develop a regression model in two consecutive stages and then try to implement it in predicting future growth of the life insurance sector in Beijing.

7.1.1. Construction of the statistical regression model

For this analysis, I use data published by the Beijing Insurance Regulatory Committee and Bureau of Statistics of Beijing as shown in *table 7-1*. The unit of measurement used for GDP and life premium volume is hundred million Yuan, the unit used for income is Yuan, for population it is 1000 people, and for the CPI index and interest it is %.

Table7-1 Relevant statistical index from 1994 to 2007 in Beijing

Year	GDP	Life premium	population	income	index	interest
1988	410.22	0.55	1001.2	1436.9	120.4	7.56
1989	455.96	0.85	1021.2	1597.1	117.2	10.89
1990	500.82	1.13	1032.2	1787.1	105.4	10.02
1991	598.89	1.37	1039.5	2040.4	111.9	7.92
1992	709.1	2.64	1044.9	2363.7	109.9	7.56
1993	863.53	3.41	1051.2	3296	119	9.26
1994	1084.03	4.57	1061.8	4731.2	124	10.98
1995	1394.89	8.66	1070.3	5868.4	117.3	10.98
1996	1615.73	21.23	1077.7	6885.5	111.6	9.36
1997	1810.09	61.56	1085.5	7813.1	105.3	7.17
1998	2011.31	60.19	1091.5	8472	102.9	5.15
1999	2169.7	60.9	1099.8	9183	100.6	3.02
2000	2460	60.1	1363.6	10349	103.5	2.25
2001	2817.6	102.7	1383.3	11578	103.1	2.25
2002	3130	182.6	1423.2	12464	98.2	2.03
2003	3612	230.6	1456.4	13883	100.2	1.98
2004	4283.3	213	1492.7	15637.8	103	2.25
2005	6814.5	230.6	1538	17653	104.2	2.25
2006	7720.3	327.1	1581	19978	105.9	2.52
2007	9006.2	386.4	1633	21989	108.6	3.46

For the reason of difference source, the big difference in population between 1999 and 2000.

Source: Beijing Insurance Regulatory Committee and Bureau of Statistics of Beijing

In order to improve the stability of samples, the natural logarithm of each of the data variables was used to construct the regression model. The software used in constructing the model is SPSS 13.

The structure of the model we wanted to test is as follows:

Lm (formula) =

Life insurance premium income ~ Gdp + Pop + Inc + Ind + Int + ε

In which:

Pop is population (1000 people),

GDP is gross domestic production (hundred million Yuan),

Inc is personal income (Yuan),

Ind is CPI Index (%),

Int is interest rate (%),

Life insurance premium income (hundred million Yuan)

First, get natural logarithm of each of the data, and then construct regression model

The results of the SPSS analysis using the table above are as follows:

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	12.127	8.836		1.372	0.192
	INDEX	-5.677	1.432	-0.173	-3.963	0.001
	INCOME	1.950	0.411	0.780	4.745	0.000
	POP	-0.211	1.226	-0.017	-0.172	0.866
	GDP	0.267	0.472	0.113	0.565	0.581
	INTEREST	-0.008	0.245	-0.002	-0.031	0.976

a. Dependent Variable: PRE

The result shows that only income and CPI index are significant variables in the regression, so I constructed a simpler model using these two variables only in a second stage. The structure of the regression model thus becomes:

Lm (formula = Life insurance premium income ~ Inc + Ind + ϵ) (the same units and same definition as above equation)

The results of the SPSS 13 analysis are as follows:

Table 7-3 Coefficients(a) of model						
Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	9.820	4.745		2.070	0.054
	INDEX	-5.554	0.925	-0.169	-6.006	0.000
	INCOME	2.203	0.070	0.881	31.355	0.000

a. Dependent Variable: PRE

Table 7.4 Model Summary					
Model	R	R Square	Adjusted R Square	F Change	Sig. F Change
				1	.996(a)

a. Predictors: (Constant), INCOME, INDEX

From above statistical result, I got the following regression model:

Ln (life premium) = 9.82 -5.554 Ln(index)+2.203 Ln(income)

This formula shows that the life insurance premium volume is positively correlated with income and negatively correlated with the CPI- index.

7.1.2. Prediction of the premium volume growth according to the regression model

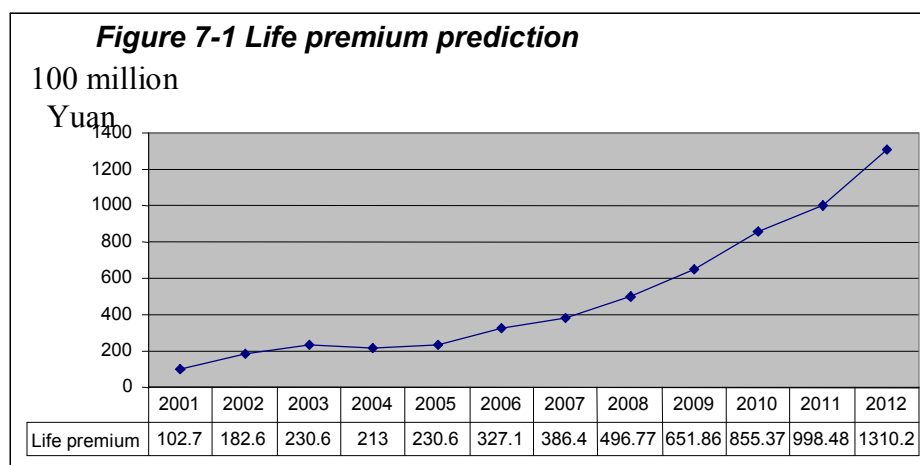
At first, we should investigate the CPI index and income more closely. CPI index increased very fast in last three years and caused instability in society because it leads to a substantial reduction in real term living standards of the people. The central government is consecrating more attention to it and strives to control the increase. The objective is to attain a reasonable level of 4% in this year. However, taking other factors such as enforcement problem, economic transition, and nearly natural disaster and so on into account, we suppose the index will stay around 5% in next five years.

With regard to the income level, through research about it over the last five years, I can state that the average annual growth rate stand at 12%. It is reasonable to assume that this figure will be representative for the annual growth rate in next five years as well because based on the previous data, the average growth rate in last ten year is 12.1%, at the same time, and it is undoubtedly that people’s income will increase with the economic development, as mention in above chapter.

Using these figures as input for the equation obtained by the regression analysis, leads to the following results (see table 7-5 and figure 7-1) .

Table 7-5 predict result of premium income

<i>Year</i>	<i>Income</i>	<i>CPI Index</i>	<i>Life premium</i>
2008	24187.90	105.00	496.77
2009	28057.96	106.05	651.86
2010	32547.24	107.11	855.37
2011	35801.96	108.18	998.48
2012	41530.28	109.26	1310.21



The average growth rate is predicted to be around 27.8 %, which is a little less than the average growth rate over the last 10 years, which was 30%. But this figure is probably more realistic and will be easier to be realized in the future. It also shows that the overheating of the Chinese economy will somewhat be alleviated after 2008.

This result can be compared to several macro-economic research studies performed in China and using statistical regression as well.⁷⁵ Their results are somewhat higher as mine. The Beijing insurance Regulatory Committee for instance concluded in 2005 that the premium volume in 2005, 2006 and 2007 should be respectively 40.1, 45.9, and 52.7 billion Yuan⁷⁶ on the basis of these models. These data are much higher than the real figures.

The origin of the deviations between the macro-economic models and our regression model stems from the selection of different variables for the regression model. Most researchers suppose that GDP is the most important factor to the Beijing life insurance industry, and did not consider income as a factor. This creates a huge difference since millions of Yuan have been invested over the last years in huge city construction projects as a preparation of the 2008 Olympics. The growth of GDP is thus probably overvalued for future years. In our model the income is used as a variable, which is more logical: there is no direct or dramatic impact of the one-off Olympic project on it. On the contrary, increase income did not increase as fast as GDP in the pre-Olympic period so that in spite of the huge GDP growth, people still cannot easily afford insurance. Other researchers have built a model based on world average insurance curves like the ones mentioned by Liuwei⁷⁷, but the problem of this method, is that it does not take differences between Beijing and other areas of the world into account. This also causes an overestimate in premium volume prediction. For these reasons we believe that our results, though lower than others, are more realistic and predict future development somewhat better.

Undoubtedly , there are also some shortages in the regression model I constructed, such as the use of natural logarithms, which is based on the assumption that the growth rate between income, index and life premium follows a linear regression. This is certainly suitable for short and medium-term predictions and in some special period, but it is not always consistent with the development over a longer-term period. But it can at least be used to give a more realistic idea of future development of the life insurance industry in Beijing.

⁷⁵ Qiu xiaohua , Chinese insurance development perspective analysis,
china insurance development research

⁷⁶ Beijing insurance industry development research

⁷⁷ Liu wei ,China insurance industry development status and premium development prediction

7.2. Key Index Method

This method tries to predict the growth rate of premium volume through the utilization of two key indexes, insurance depth and insurance density, along with the forecasted value of future GDP and population growth.

The calculation mechanism is the following:

$$\text{Insurance depth} = \text{Life Insurance Premium Volume} / \text{GDP};$$

Thus it should be that:

$$\text{Forecasted Life Insurance Premium Volume} = \text{Insurance depth} * \text{Forecasted GDP}$$

$$\text{Insurance density} = \text{Life Insurance Premium Volume} / \text{Population};$$

Thus it should be that:

$$\text{Forecasted Life Insurance Premium Volume} = \text{Insurance density} * \text{Forecasted Population}$$

7.2.1. Collection of basic data

Table 7-6 shows the development of the different variables used in those equations in Beijing since 2000.

Table 7-6 Relevant data from 2000 to 2007								
Year	2000	2001	2002	2003	2004	2005	2006	2007
GDP in 100 million Yuan	2460.00	2817.60	3130.00	3612.00	4283.30	6814.50	7720.30	9006.20
Life premium in 100 million Yuan	60.10	102.70	182.60	230.60	213.00	230.60	327.10	386.40
population in 1000	1363.60	1383.30	1423.20	1456.40	1492.70	1538.00	1581.00	1633.00
insurance depth	2.44%	3.64%	5.83%	6.38%	4.97%	6.32%	4.24%	4.29%
insurance density	440.75	742.43	1283.02	1583.36	1426.94	1499.35	2068.94	2366.20
Growth rate of these two indexes								
growth rate of insurance depth		49.19%	60.05%	9.43%	-22.11%	27.07%	-32.95%	1.26%
growth rate insurance density		68.45%	72.81%	23.41%	-9.88%	5.07%	37.99%	14.37%
average growth rate of insurance depth	13.14%							
average growth	30.32%							

rate insurance density	
---------------------------	--

Source: Beijing Insurance Regulatory Committee and Bureau of Statistics of Beijing

According to the average growth rate in insurance depth and insurance density since 2000, we can easily predict the future values of these two indexes. (See table 7-7)

	2008	2009	2010	2011	2012
insurance depth	4.85%	5.49%	6.21%	7.03%	7.95%
insurance density	3083.57	4018.44	5236.74	6824.39	8893.39

7.2.2. Forecasting GDP and population in the future

The average GDP growth rate was nearly 20% over the last seven years. Since this is extremely fast and the organization of the Olympics with all its construction projects in infrastructure and logistics contributed largely to it, I do not think this growth will continue in the near future at the same level.

When focus on the data from 1995 to 2004, on the purpose of reducing the influence by Olympic game, the average growth rate in that period was 12.49%, on the other hand, the average GDP growth in whole China is nearly 8% in last twenty years. As the capital and the central of economics, 10% looks like a more realistic and achievable objective for growth in GDP the next five years in Beijing. Maybe it has deviation in prediction, but it try to provide some useful guidance for the life insurance industry development in Beijing.

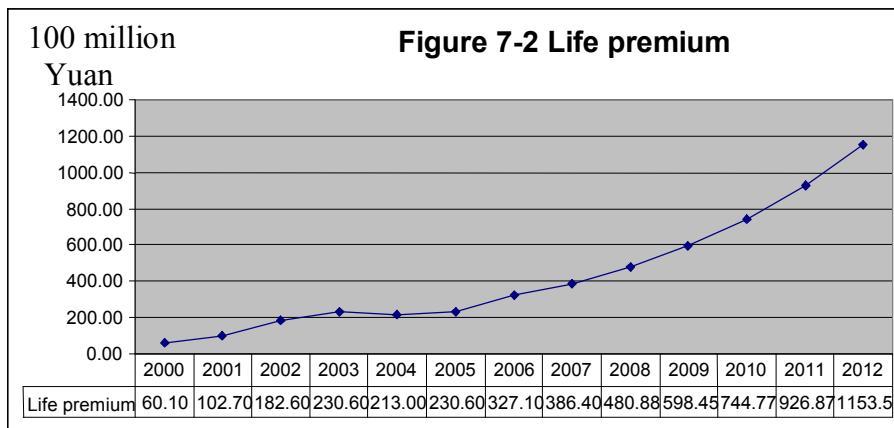
Over the last 7 years, population in Beijing grew with 384.9 thousand. Since population regulation (one child policy) is not likely to change in the next couple of years, I assume that the increase in population will continue at the same level in the next five years.

Integrating these data into the formulas mentioned in the previous paragraph, results in the following tables (see table 7-8, 7-9 and figure 7-2,7-3), using life insurance depth and life insurance density respectively:

Using life insurance depth the table looks as follows:

Table 7-8 using insurance depth to predict premium income

Year	GDP	Insurance depth	Life premium
2008	9906.82	4.85%	480.88
2009	10897.50	5.49%	598.45
2010	11987.25	6.21%	744.77
2011	13185.98	7.03%	926.87
2012	14504.58	7.95%	1153.50

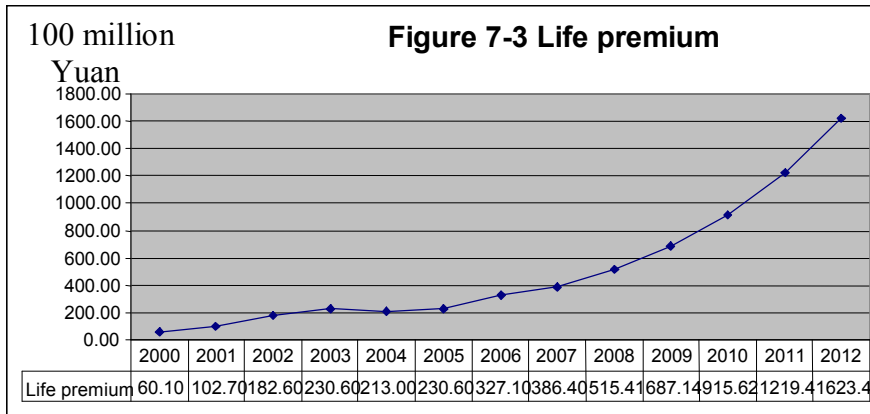


The average predicted growth rate of life insurance premium volume is 24% following this key index.

Using life insurance density the table looks as follows:

Table 7-9 using insurance density to predict premium income

Year	Population	Insurance density	Life premium
2008	1671.49	3083.57	515.41
2009	1709.97	4018.44	687.14
2010	1748.46	5236.74	915.62
2011	1786.94	6824.39	1219.48
2012	1825.43	8893.39	1623.42



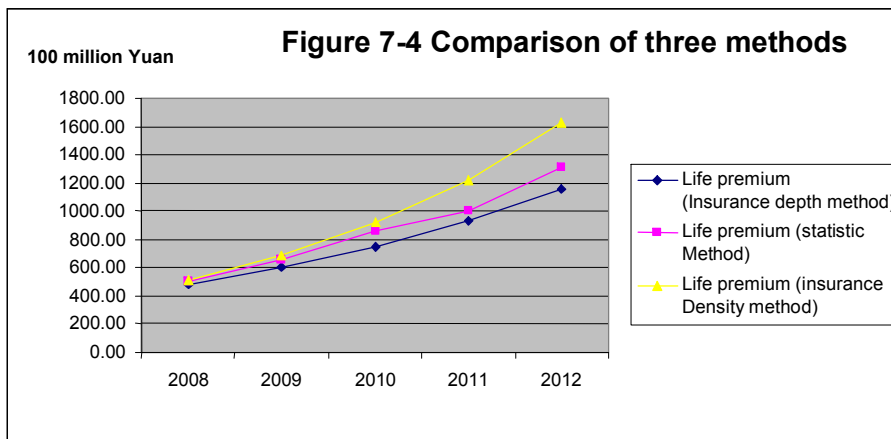
The predicted average growth rate is then 33 %.

7.3. Summary of our predictions

In Summary, we have forecasted growth of life insurance premium volume in three different ways. The different results we obtained are listed below in *table 7-10 and Figure 7-4* .

Table 7-10 summaries of prediction results

Year	<i>Life premium volume according to the insurance depth method</i>	<i>Life premium volume according to the statistic regression method</i>	<i>Life premium volume according to the insurance density method</i>
2008	<i>480.88</i>	<i>496.77</i>	<i>515.41</i>
2009	<i>598.45</i>	<i>651.86</i>	<i>687.14</i>
2010	<i>744.77</i>	<i>855.37</i>	<i>915.62</i>
2011	<i>926.87</i>	<i>998.48</i>	<i>1219.48</i>
2012	<i>1153.50</i>	<i>1310.21</i>	<i>1623.42</i>



Thus the forecasted growth rates of life insurance premium in Beijing range from 24 % to 33 %, with 28 % as the result of the third method. All three methods, using both linear regression and linear equation, lead to rather similar results depicting the future growth of life insurance premium volume in Beijing. Although the results are clearly differing from other economic predictions mentioned before, their similarity renders more confidence to the results we have obtained. Thus we think these predictions are fairly reliable and trustworthy, in spite of the limitations of the methods used, which mentioned in paragraph 7.1.2. And of which the assumption that economic growth follows a linear path is probably the most difficult one to defend.

Chapter 8 Conclusion and recommendations

Based on all data and criteria mentioned before, we can fairly accurately state that the Beijing life insurance market is growing fast but only plays a limited role on macro-economic development level. It improves economic welfare, the financial system of China and the social security system to a limited extent due to a number of limiting internal and external factors. At the same time, it has a rather low efficiency and shows a weak profit margin.

We try to enumerate all these factors in a SWOT-table below. A SWOT-table lists factors influencing the future development of a company, a product or an industry by subdividing them in both external opportunities and threats and internal weaknesses and strengths.⁷⁸ The SWOT-analysis in this case is mentioned in *table8-1*.

Table 8-1 SWOT analysis of the Beijing life insurance market

Opportunities	Threats
<ul style="list-style-type: none"> • Continuous high annual growth of GDP • Large and growing population in the Beijing area • Insurance depth and density are still lower than in comparable developed regions of the world • Gradual opening up of the market in line with the transition to a more market oriented economy • Hosting city of 2008 Olympic Game • Natural disaster increase people's 	<ul style="list-style-type: none"> • Imbalanced income structure (large difference between poor and rich people) • Unawareness of people of the advantages of life insurance savings and investments • Imbalanced structure of the financial market (limited possibilities to invest in different financial products, at home in China as well as abroad) • Stringent regulation for the entrance of foreign insurance companies (capital requirements, limitation of

⁷⁸ Bradford, Robert W ,simplified strategic planning : A No-nonsense guide for busy people who want results fast

<p>insurance awareness</p> <ul style="list-style-type: none"> • New products development, in health, pension and other sectors • High educational people continually go to Beijing • Middle-class people increase • Society translation to aging society • With the SOA and CFA exams hold in China, more people get actuarial and financial knowledge • High salary offered for some technical position encourage more people enter life insurance industry • 	<p>simultaneous opening of different branches...)</p> <ul style="list-style-type: none"> • Unclear role of CIRC • Unfavorable taxation system • China communist party's orientation • Shanghai and Tianjin become the central of economics • fierce competition from foreign insurance companies and more underground insurance contacts • high financial risk in outside investment • same category participant product from bank industrial
<p>Strengths</p>	<p>Weaknesses</p>
<ul style="list-style-type: none"> • Industry is 30 years after partial liberalization of the market embedded in social and economic life • People have become gradually aware of the necessity to complement social security and health care systems with private life insurance • Some Insurances has become obligation for employees and employers • A large amount of experienced staff • More than 40,000 sales personnel's can direct sale life insurance products to their families and friends 	<ul style="list-style-type: none"> • Focus on scale • Price competition • Most products are standard products and little sophisticated • Little focus on the development of more sophisticated products and services • Incomplete asset management • Lack of trained, staff Without systematic training and professional knowledge, sometimes fraud happen • Insufficient salaries for sale personnel , thus high turn-over of staff

<ul style="list-style-type: none"> • Some China insurance companies has already get experience and practical skill from last 20 years • New foreign insurance companies all have long history in this field and have developed marketing, financial, and actuary knowledge , the communication and competition among insurance companies can increase insurance industry wholly competence • Recently, rapidly development in the countryside area • some big insurance companies have development to financial group, including life insurance, property insurance , banking ,financial investment sectors, some of them listed in stock market 	<ul style="list-style-type: none"> • Low solvency rates • Lack of very developed information systems • Small scale of intermediate agency and unperfected intermediate system • Sells personal still contain more than 80%, and the broking and agencies development relative slowly • Market begin to saturation, the old customers do not want to buy again on the conditions of without new products enter market • Lack of financial channels and can not satisfying margin profit • The interest rate continually decrease and deduce marginal profit • The limitation of investment for foreign bond
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In view of this analysis, it is high time for the participants on the Beijing life insurance market to finally respond to the threats mentioned and to correct some of the weaknesses enumerated in order to take advantage of the enormous potential the market presents. Basically this signifies that the direction future should take should be guided more by efficiency than by scale. The objective of a more modern life insurance industry in Beijing should indeed be the realizing of a healthier interaction between the developments of the industry on the one hand and the development of economy as well as society on the other hand. Further opening up of the market and stimulation of competition, next to the fully exploitation of the industry's function in complementing social security, optimizing economic development and enhancing social harmony, are the cornerstones of this strategy.

This represents a huge turnaround which will take years to implement. Among the major steps to be taken, we can list the following recommendations for both insurance companies and regulators.

For insurance companies guidelines are:

- Improving solvency and overall risk management;
- Implementing actuarial technology and information technology;
- Asset management, implement a modern accounting system to control and monitor company cash flow, cost and benefits, thus making sure that the companies enjoy sustainable development;
- Increasing the effectiveness of underwriting and claim settlement;
- Insisting on more rigorous and objective criteria for collecting information, finding out problematic insurance contracts, thus deducing the business risks for insurance companies and increasing economic efficiency;
- Encouraging innovation and sophistication of products and services;
- Improving the training and professionalism of agents and other distribution channels;
- Building a healthier interaction between insurance companies and other related industries, specifically the financial industry; and
- Realization a better balance between supply and demand.

For regulatory bodies the majors steps to be taken are:

- Installing economic incentive mechanisms to replace administrative power, more specially using the stimulating effect of preferred taxation treatment on the insurance industry;
- Reducing taxation to a level, that can encourage insurance company to invest more in research, development and innovation, while also encouraging agents to work harder and more efficiently;
- Creating more transparency in rulemaking and regulatory procedures;
- Increasing communication between CIRC, domestic insurance companies, foreign insurance companies, brokers and agents to stimulate an open discussion on many issues,

such as performance, exchanging experience, potential solutions to problems and enhancement of the economic and social function of the life insurance industry in Beijing;

- Encouraging the development of foreign insurance companies by liberalizing current unfair limitations and providing a fair competitive environment to them, such as reducing capital requirements and allowing the simultaneous establishment of different branches.

All these changes when implemented will certainly give a new and enormous boost to the life insurance industry in Beijing and thus improve social and economic welfare in China as a whole.

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Appendix 1 Questionnaire used in the thesis

1. What is your opinion on the current situation of the Beijing life insurance industry and its further development?
2. What are the main barriers for current life insurance industry in Beijing?
3. What are the most important changes in Beijing life insurance market?
4. What are the most pressing issues you face?
5. What changes did happen in distribution channels? What is the results? Advantages and shortcomings?
6. What is the staff turnover rate in your companies?
7. How many kinds of insurance products do your company sale? Which one is the best?
8. What kind of working strategy does your company use?
9. What is your estimation about premium annual growth in next five years? Both for your company and for all life insurance industry in Beijing?
10. Do you have enough capable staff?

Appendix 2 :Data used in the thesis

Year	2000	2001	2002	2003	2004	2005	2006	2007
GDP(100 million Yuan)	2460.00	2817.60	3130.00	3612.00	4283.30	6814.50	7720.30	9006.20
Life premium(100 million Yuan)	60.10	102.70	182.60	230.60	213.00	430.60	327.10	386.40
total premium (100 million Yuan)	93.40	141.30	233.00	282.50	278.90	298.20	411.50	498.10
casualty(100 million Yuan)	33.30	38.60	50.40	51.90	65.90	-132.40	84.40	111.70
life insurance compensation(100 million Yuan)	13.70	15.70	22.80	20.80	21.10	40.20	45.10	85.70
total compensation (100 million Yuan)	23.70	32.00	47.20	48.00	54.30	75.40	84.00	135.40
% in life insurance premium	0.23	0.15	0.12	0.09	0.10	0.09	0.14	0.22
% in premium	0.25	0.23	0.20	0.17	0.19	0.25	0.20	0.27
registered population (10000)	1107.50	1120.50	1136.30	1148.80	1162.90	1180.70	1197.60	1213.30
lived population (10000)	1363.60	1383.30	1423.20	1456.40	1492.70	1538.00	1581.00	1633.00
GDP/population	2.22	2.51	2.75	3.14	3.68	5.77	6.45	7.42
enjoy pension insurance population(10000)	391.60	312.30		448.00	460.00	520.00	604.10	671.70
enjoy health insurance population(10000)	306.00	315.00	325.00	436.00	484.00	574.80	679.50	783.00
income (Yuan)	10349.00	11578.00	12464.00	13883.00	15637.80	17653.00	19978.00	21989.00
average salary (Yuan)	15600.00	18640.00	19865.00	20012.00				
cost (Yuan)	8493.50	8923.00	10286.00	11124.00	12200.40			

GINI index	0.36	0.36	0.34	0.32	0.32	0.32	0.31	0.32
insurance intermediate amount	6.00	10.00	24.00	100.00	184.00	227.00	255.00	281.00
agency property premium(ten thousand Yuan)		15826.87	12869.87	16358.55	26834.98	64648.33		
intermediate life premium(ten thousand Yuan)		6556.22	5867.16	14164.02	16180.50	27701.19	46783.00	67432.00
total	1929.00	22383.09	18737.03	30522.57	43015.48	92349.52		
Insurance Brokering Companies			41420.19	125678.00	176596.56	468625.56		
life premium from brokering (ten thousand Yuan)			11278.00	26547.00	39240.43	121645.00	187984.00	213076.00
<i>total</i>			60157.22	156200.57	219612.04	560975.08	660788.00	1073475.00
total life premium from intermediate(ten thousand Yuan)		6556.22	17145.16	40711.02	55420.93	149346.19	234767.00	280508.00
concurrent-business insurance agents amounts	3196.00	4190.00	4235.00	5111.00	5036.00	5867.00	7021.00	8416.00
premium from concurrent-business insurance agents(ten thousand Yuan)	31.22	45.78	60.72	106.96	98.76	92.99	109.46	120.78
sells personnel amount	24500.00	28354.00	43762.00	59081.00	46330.00	41513.00	51243.00	43270.00
sells personnel 's average salary (Yuan)	2100.00	2255.00	1478.00	1497.00	1562.00	2265.00	2348.00	2567.00
bank deposit (100 million Yuan)	9705.00	12223.40	15392.70	18321.90	21625.90	28970.00	33793.30	37700.30

Appendix 3 : Responsibilities and Internal Setup of the CIRC

Source : CIRC, HTTP:// WWW.CIRC.GOV.CN

The China Insurance Regulatory Commission (the “CIRC”), established on November 18, 1998, is authorized by the State Council to conduct administration, supervision and regulation of the Chinese insurance market, and to ensure that the insurance industry operates stably in compliance with law. In 2003, the State Council upgraded the CIRC from a semi-ministerial institution to a ministerial institution directly under the State Council, and to expand the size of the CIRC in terms of staff, internal setup, and local offices.

I. Major Responsibilities

(1) The CIRC formulates policies, strategies and plans regarding the development of the insurance industry, drafts relevant laws and regulations regarding insurance supervision and regulation, and makes relevant rules for the insurance industry.

(2) It examines and approves the establishment of insurance companies and their branches, insurance groups and insurance holding companies; approves in conjunction with relevant authorities the establishment of insurance asset management companies; examines and approves the establishment of representative offices by overseas insurance organizations within the territory of the People’s Republic of China; examines and approves the establishment of insurance intermediaries such as agencies, brokerages, loss-adjusting companies and their branches; examines and approves the establishment of overseas insurance organizations by domestic insurance and non-insurance organizations; examines and approves the merge, split, alteration and dissolution of insurance organizations; decides whether or not to take over an insurance company or designates an organization to take it over; organizes or participates in the bankruptcy and liquidation process of insurance companies.

(3) It examines and confirms the qualifications of the senior managerial personnel in all insurance-related organizations; establishes the basic qualification standards for

insurance practitioners.

(4) It examines and approves the clauses and premium rates of insurance lines related to the public interests, statutory insurance lines and newly developed life insurance lines; files the insurance clauses and premium rates of the other insurance lines.

(5) It supervises the solvency and market conduct of insurance companies according to law; manages the insurance security fund, and monitors the insurance guarantee deposits; formulates rules and regulations on insurance fund management on the basis of laws and relevant policies of the State, and supervises insurance fund management according to law.

(6) It supervises the business operation of public-policy-oriented insurance and statutory insurance; supervises organizational forms and operations such as captive insurance and mutual insurance; conducts administration of societies and organizations such as China Insurance Association and China Insurance Society.

(7) It conducts investigation into the following irregularities and imposes penalties accordingly: unfair competition and other irregularities by insurance organizations and practitioners, direct engagement or disguised engagement in insurance business by non-insurance organizations.

(8) It supervises overseas insurance organizations established by domestic insurance and non-insurance organizations according to law.

(9) It lays down standards for the information system of the insurance industry; establishes insurance risk-assessment, risk-warning and risk-monitoring systems; follows, analyzes and predicts the operation of the insurance market; compiles the statistics and report forms of the insurance industry and discloses them in accordance with relevant regulations of the State.

(10) Other duties commissioned by the State Council.

II. Internal Setup

(1) General Office

(2) Development and Reform Department

- (3) Finance and Accounting Department
- (4) Property Insurance Regulatory Department
- (5) Personal Insurance Regulatory Department
- (6) Insurance Intermediaries Regulatory Department
- (7) Insurance Fund Management Regulatory Department
- (8) International Department
- (9) Legal Affairs Department
- (10) Statistics and IT Department
- (11) Local Offices Administration Department
- (12) Personnel and Education Department
- (13) Disciplinary Inspection Department

III. Local Offices

After the CIRC was upgraded by the State Council from a semi-ministerial institution to a ministerial institution in 2003, the number of the CIRC's local offices has been increased accordingly. In addition to the 31 local offices in each province (except Taiwan), autonomous region (except Tibet), municipality directly under the Central Government and Shenzhen Economic Special Zone, another 4 offices are being set up in the cities of Dalian, Qingdao, Ningbo and Xiamen. The local offices are under the direct leadership of the CIRC.

Appendix 4 .Regulatory Measures of the CIRC Since 2004

Source : CIRC, HTTP:// WWW.CIRC.GOV.CN

As the administrative and regulatory authority of China's commercial insurance, which is still in the primary stage of development, the CIRC considers the development of insurance industry as its most important task and strives to make China insurance industry big and strong. The CIRC's major regulatory measures since 2004 are as follows:

I. Measures to Boost the Industry

Adhering to the market-oriented principle, the CIRC has adopted a series of policies and measures to accelerate development and has made breakthroughs in tackling problems and removing shackles that hampered the development of insurance industry.

(1) Improving the Market Access Mechanism

With the approvals to the establishment of the first agricultural insurance company, the first health insurance company, the first pension insurance company and the first agricultural insurance mutual company, insurance companies in China are becoming more and more specialized and the organizational forms for insurance operation are more varied. In 2004, 8 Chinese-invested insurance companies and 4 foreign-invested insurance companies entered the market. At the same time, the CIRC has improved the market access mechanism for insurance branches to encourage law-abiding insurance companies with sound internal control system and adequate solvency to establish branches so as to increase market competition.

(2) Broadening Insurance Fund Management Channels

To implement *Several Opinions of the State Council on Promoting Opening-up and Stable Development of Capital Market*, the CIRC has permitted direct investment of

insurance funds in the stock market, allowed foreign-exchange insurance funds to be invested overseas, allowed insurance companies to invest in subordinated debts issued by banks and convertible corporate bonds, and permitted foreign-invested insurance companies to enter into deposit agreement with banks. The broadening of insurance fund management channels helps insurance companies to improve the matching of assets and liabilities, to spread investment risks and to raise investment returns.

(3) Increasing Financing Channels of Insurance Companies

The CIRC has permitted insurance companies to issue subordinated debts, which provided a new financing channel for the fast-developing insurance industry and helped the insurance companies to improve their solvency status.

(4) Pushing forward Reform of Administrative Examination and Approval System

The CIRC promulgated *Implementation Measures on Administrative Licensing of the CIRC* in 2004, which specified standardized and transparent insurance administrative licensing procedures. The CIRC has cancelled three batches of items for administrative examination and approval. Altogether, 108 items have been cancelled including the 22 items in the third batch. Besides, CIRC has reformed the management system of insurance clauses and premium rates. The clauses and premium rates of some products now only need to be filed with the CIRC instead of being approved by the CIRC. Insurance companies can adjust their auto insurance premium rates in the light of different risk elements and establish a market-oriented pricing mechanism. Simplification of life insurance clauses has also been pushed forward to make insurance products easier to understand by the public.

II. Measures to Strengthen Risk Prevention

The CIRC considers risk prevention as a project of systematic engineering and tries to build 5 lines of defense against risks, namely, internal control as the basis, supervision of solvency adequacy as the core, on-site inspection as an important means, fund management regulation as a key link and insurance security fund as a protective

screen.

(1) Strengthening Internal Management

The CIRC has promulgated *Guidance on Informationalization Inspection of Insurance Organizations Before Business Commencement* and specified requirements for the Informationalization of insurance companies. The CIRC has also promulgated *Provisional Regulations on Management of Insurance Statistics*, launched China Insurance Statistics Information System, and realized the network connection between the regulatory authority and insurance companies. These measures have strengthened the risk control and internal management of insurance companies.

(2) Strengthening Supervision of Solvency Adequacy

After the promulgation of *Measures on Administration of Reserves for Non-life Insurance Business of Insurance Companies (Tentative)*, more prudential and standardized requirements for liabilities reserving have been implemented. The promulgation of *Rules of Solvency Reporting of Insurance Companies* made the solvency assessment of insurance companies more scientific and accurate. A quarterly solvency report system and a specialized financial analysis system have been established. Besides, the *Regulatory Opinions* issued to insolvent companies, asking them to rectify by the prescribed time made the supervision of solvency adequacy stronger and more effective.

(3) Reinforcing On-site Inspection

CIRC is more rigorous in punishing insurance companies and intermediaries that violate laws and regulations and has eliminated some of the risks that endanger the stability of the insurance market. “Underground policies” has been dealt with severely and stopped spreading. The liability insurance business for car loans has been standardized and relevant risks mitigated.

(4) Strengthening Supervision of Fund Management

A custody system for insurance funds has been adopted since the promulgation of *Provisional Regulations on Administration of Insurance Asset Management Companies* and *Guidance on Risk Control in Insurance Fund Management*. The CIRC has been guiding insurance companies to improve their fund management risk control systems to

deal with the latent risks after the opening up of insurance fund management channels. It has organized special inspections and many activities to warn insurance companies of relevant risks.

(5) Establishing and Improving Insurance Security Fund System

Measures on Administration of Insurance Security Fund was promulgated in 2004 to reinforce the central management of the insurance security fund, to establish a self protection mechanism for the insurance industry and to enhance the industry's ability of preventing and mitigating risks on the strengthen of its own.