

Insurance set to stir up mainland capital markets

Arun Sudhaman

China's capital markets stand to receive a substantial boost from the deregulation of the insurance industry that should occur once Beijing joins the World Trade Organisation.

The impact of WTO entry on relatively open industries such as consumer goods is expected to be limited but the insurance sector, largely shielded from foreign competition, is likely to face a fundamental revolution.

The head of economic research and consulting at global reinsurance giants Swiss Re, Kai-Uwe Schanz, believes a number of crucial measures have the potential to transform the mainland's capital markets, making them far more attractive for potential investors.

The mainland's insurance market is worth about US\$20 billion (HK\$155 billion) at present and Mr Schanz expected it would double by 2010.

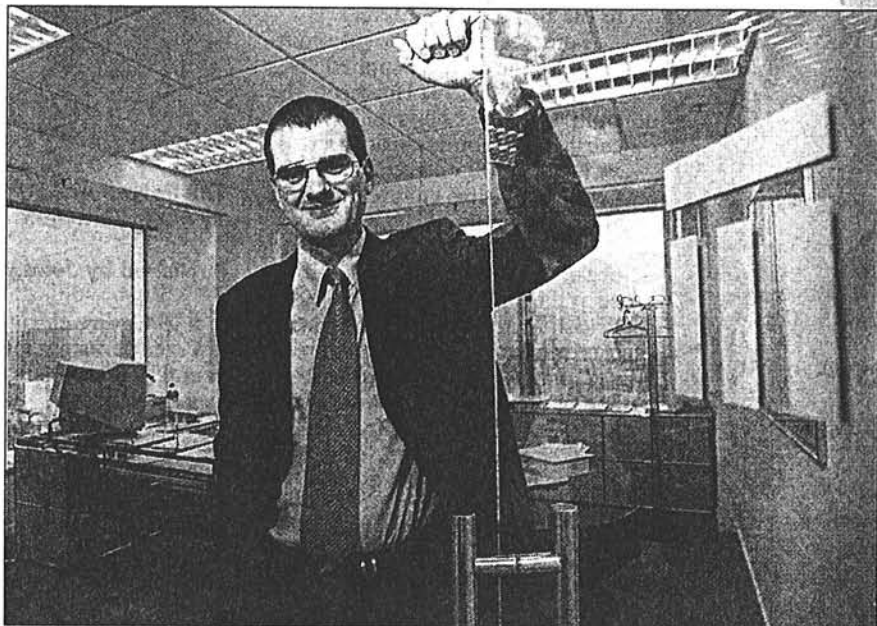
Foreign insurance companies face strict restrictions and have a market share of less than 2 per cent. Foreign insurers are allowed in a few cities, Shanghai being one, but operations are tightly controlled.

The WTO agreement, however, stands to change all that.

Under the terms of the deal, Beijing has agreed to allow foreign non-life insurers to operate wholly owned subsidiaries two years after accession.

Furthermore, foreign life insurers will be able to hold a maximum 50 per cent stake in joint ventures with domestic life insurers.

The geographical restrictions will vanish within three years of accession



WTO storm

Martin Chan

Swiss Re economic research and consulting head Kai-Uwe Schanz foresees the freeing up of China's insurance industry as Beijing rewrites regulations for World Trade Organisation membership and the drawing in of foreign players.

and, to Mr Schanz's delight, insurance licences will be issued based on relevant economic criteria.

"China has agreed, in future, that business licences will be granted based on strictly prudential criteria, so no longer according to political or other considerations," he said.

Mr Schanz is also happy that the measures allow for gradual liberalisation of the insurance industry rather than, in his

words, "a shock-like increase in competition".

Sudden relaxations in regulations could, according to Mr Schanz, lead to more insurance company insolvencies, as is the situation in Japan.

Aetna International vice-president for pension business in the Greater China region David Hatton agrees that Chinese insurance companies are not

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very likely to face the insolvency problems of their Japanese counterparts.

"Chinese insurance companies are simply not as bankrupt as Japanese insurance companies," Mr Hatton said. "The [Chinese] Government has concerns about solvency."

However, it is clear domestic Chinese insurers must gear themselves up to meet the demands of foreign competition. In this respect, Beijing has been implementing reforms aimed at making their insurance industry better prepared for the foreign influx.

To begin with, the investment channels open to insurers are being broadened, so life insurers are now allowed to invest, in some cases, up to 15 per cent of their total assets in mutual funds. However, for an industry used to the meagre returns of bank deposits and treasury bonds, the readiness to invest in mutual funds must be questioned.

Mr Schanz said: "It is interesting to note that Chinese domestic insurers have not used the leeway that they have for investing in these funds." Often, less than 5 per cent of assets were invested, with companies concerned about fund management and performance.

"Part of the reason is they [domestic insurers] don't know what performance will be," Mr Hatton said on the low percentages invested in funds.

Dr Schanz also believed Chinese insurers should be allowed to invest directly in primary and secondary markets, by underwriting share offers and, as recently allowed, in open-ended mutual funds.

"What we see right now is relatively strict," Mr Schanz said. "It would be more attractive if opportunities in open-end investment funds were opened up - then I think we would see more investment from the insurance side."

The recent moves to allow open-ended mutual funds are a step in the right direction, although there are still concerns over

fund management. At present, only domestic companies are allowed to manage funds - although three Chinese fund houses do have high profile "alliances" with international fund houses.

Beijing also encourages domestic insurers to seek a stock market listing in order to strengthen their capital base.

China Pacific Insurance, the country's third-largest insurer, is planning to list its property insurance arm on the market.

Additionally, the two largest Chinese companies, China Life and the People's Insurance Company of China, are mooting the idea of listing.

Mr Schanz was confident measures implemented by Beijing would be effective, but did have fears about the quality of insurance workers in the mainland.

"I foresee a lot of competition for insurance experts in China - this is probably the biggest problem the incumbent firms face, to offer similar terms and conditions as the foreign firms."