Institutional Design of Catastrophe Insurance in China:
Progress and Challenge

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Integrated Disaster Reduction Strategy

- Capacity Building: National Development and Reform Commission
- Disaster Relief
- Integrated Disaster Reduction Strategy
- Emergency Management: Office of Emergency Response, State Council
- Risk Transfer: China Insurance Regulatory Commission? Ministry of Finance?
- Ministry of Civil Affairs
History of Agriculture Insurance in China

1950-1958
1982
2007

1982-2008 Agriculture Insurance in PICC

- Premium Collected
- Indemnity
Understanding of the Four Principles

- “Guided by government”
  - Initiated and launched under fiscal support
  - Not policy-based insurance: limited liability and support; subsidize premium for policy-holders
  - Risk is undertaken by insurance industry only
- “Market operation”
  - Should not establish policy-based institution/company specifically for agriculture insurance
  - Rely on existing commercial insurers
- “Voluntary participation”
- “Carried forward under joint forces”
  - Central and local government
  - Government and insurance industry
  - Supporting institutions: meterological, water, agriculture..
Operational Model

Step(1): Farmers’ payment
Step(2): Local government subsidy
Step(3): Central government subsidy
Step(4): Provincial government subsidy
Step(5): Reserve 25% of premium
## Details in Crops Insurance Policy (2007)

<table>
<thead>
<tr>
<th>Provinces</th>
<th>Hunan</th>
<th>Jilin</th>
<th>Inner Mongolia</th>
<th>Xinjiang</th>
<th>Sichuan</th>
<th>Jiangsu</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Insured crops</strong></td>
<td>Paddy rice and cotton</td>
<td>Corn, rice, soybean, tobacco, etc.</td>
<td>Corn, wheat, and soybean</td>
<td>Cotton, corn, paddy rice, soybean, wheat, etc.</td>
<td>Paddy rice and corn</td>
<td>Paddy rice, wheat, cotton, rapeseed and corn</td>
</tr>
<tr>
<td><strong>Perils</strong></td>
<td>rainstorm, flood, inundation, wind, hail, frost, and drought</td>
<td></td>
<td></td>
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<td></td>
</tr>
<tr>
<td><strong>Insured amount (CNY/mu/season) and premium rate (%)</strong></td>
<td>Rice: 240 (basic 5%, drought 3%, all 7%)</td>
<td>Corn: 200 (10%) Rice: 266.7 (8%) Soybean: 166.7 (8%)</td>
<td>Corn: 230 (10%) Wheat: 300(8%) Soybean: 170 (8%)</td>
<td>Cotton: 400(7%) Wheat: 300(5%) Corn: 300(5%)</td>
<td>Rice: 300 (basic 5%, With drought 10%) Corn: 292 (5%)</td>
<td>300~500 (5% for all)</td>
</tr>
<tr>
<td><strong>Subsidy rate</strong></td>
<td>Central: 50%</td>
<td>25%</td>
<td>25%</td>
<td>25%</td>
<td>25%</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td>Provincial: 50%</td>
<td>25%</td>
<td>25%</td>
<td>25%</td>
<td>25%</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Local: &gt;=10%</td>
<td>30%</td>
<td>10%</td>
<td>-</td>
<td>20%</td>
<td></td>
</tr>
<tr>
<td></td>
<td>In total: &gt;=60%</td>
<td>80%</td>
<td>85%</td>
<td>&gt;=50%</td>
<td>70%</td>
<td>&gt;= 60%</td>
</tr>
<tr>
<td><strong>Summary of 2007</strong></td>
<td>Premium (CNY): 750 million</td>
<td>689 million</td>
<td>-</td>
<td>760 million</td>
<td>74 million</td>
<td>450 million</td>
</tr>
<tr>
<td></td>
<td>Indemnity (CNY): 440 million</td>
<td>-</td>
<td>-</td>
<td>200 million</td>
<td>19 million</td>
<td>150 million</td>
</tr>
</tbody>
</table>

Source: Peijun Shi et al.
Farmers knew the program?

- 2007: 15%
- 2008: 30%
- 2009: 65%
How they knew it?

- Public medias (TV, newspapers, broadcast)
- Village officials and official docs.
- Insurance companies
- Friends and relatives
Quick Summary

- Too much government act
- Against market operation principle
- However, government helped to educate the market and subsidies are driving force for both insurers and farmers.
- Business grows rapidly.
Crops and livestock loss v.s. Insured Amount

Economic Loss (100 million RMB Yuan)

- < 30 billion (before 2007)
- 240 billion (end of 2008)
New progress in 2009

- Experimentation of “market operation” on pig, forest and hybrid rice: insurers determine coverage, premium rate and limit.
- Establishing catastrophic disaster fund: government provide matching fund to the reserved premium, and set up an independent account managed by city government.
- In Hunan, subsidy for operating cost is approved at provincial government.
Legal Basis for Catastrophe Insurance

- Flood Control Law of The People’s Republic of China (promulgated on August 29, 1997)
  - “Article 47 ...The state encourages and supports flood insurance”

- Law of the People’s Republic of China on Protecting Against and Mitigating Earthquake Disasters (promulgated on December 29, 1997)
  - “Article 25 The state encourages units and individuals to participate earthquake disaster insurance”
  - Modified in 2008, ““Article 45 The state develops the earthquake insurance system under the national fiscal support, and encourage ....”

- Emergency Response Law of the People's Republic of China (promulgated on August 30, 2007)
  - Article 35 ...The country is to establish a insurance system for large-scale disasters under the national fiscal support, and encourage units and individual citizens to participate the insurance program.
Proposal from Financial Committee of NPC

- Market operation with government support (subsidy and tax benefit)
- Focus on residential houses and all-in-one policy
- Consider regional difference
- Start with experimentation
- Catastrophe insurance fund operated independently
Proposal Submitted to NCDR

- Led by government with fiscal support
- Compensation mechanism with clearly defined responsibility
- Meet fundamental need and consider regional difference
- Encourage international cooperation and risk sharing
- Start with experimentation with centralized budget (EQ)
Social Basis: National Survey

84% have insurance experience
16% have no insurance experience
Importance of Disaster Insurance

- Very important: 37%
- Relatively important: 23%
- Neutral: 36%
- Not needed: 4%

Responsibility for Disaster Loss

- Government: 70%
- Insurance Company: 23%
- Community: 3%
- Family: 4%
Why are people reluctant to participate?

- Lack of insurance knowledge: 28%
- Discredit insurance company: 27%
- Cannot afford insurance premium: 11%
- Refuse to accept hazard risk: 5%
- Expect government disaster relief: 3%
- Other: 5%
Earthquake premium rate at county level

There is a gap between people’s WTP and cost of risk financing, therefore subsidy is necessary.
### Suggested Government Subsidy Percentages according to the Classification of Cities and Counties

<table>
<thead>
<tr>
<th>Classes</th>
<th>Description</th>
<th>Suggested Government Subsidy Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Poverty stricken counties in need of annual fiscal support from the central government</td>
<td>95%</td>
</tr>
<tr>
<td>2</td>
<td>Average counties other than poverty stricken counties</td>
<td>70%</td>
</tr>
<tr>
<td>3</td>
<td>County-level cities</td>
<td>50%</td>
</tr>
<tr>
<td>4</td>
<td>Average cities other than 36 large cities</td>
<td>30%</td>
</tr>
<tr>
<td>5</td>
<td>36 medium and large cities such as Beijing, Tianjin and Shijiazhuang</td>
<td>0%</td>
</tr>
</tbody>
</table>
Internal Project Conducted by Ministry of Finance

- Project title: Research on Institutional Design of Catastrophe Insurance.
- Framework of establishing catastrophe insurance system was completed.
- A symposium was held in November of 2009 (feedback collected).
Challenges Identified

- Lack of a government authority whose role is clearly defined to deal with disaster risk financing
- Lack of risk sharing mechanism and government faces financial pressure
- Lack of clear definition of catastrophic disaster (or large-scale disaster)
- Most rural areas have limited capacity against disasters
Suggested Institutional Design from MOF

- Government, Insurers, Reinsurers and policy-holders adopt a risk sharing mechanism
- Establish a coordinating commission for catastrophe risk management
- Emphasize that catastrophe insurance is one of the components in integrated risk management.
- Start with one peril as experimentation
Thank you!

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