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Insurance in the Land of the Thunder Dragon

By Michael Cohen

Bhutan, a small Himalayan kingdom, tucked in between Tibet to the north and the Indian states of West Bengal and Assam to the south, is famous for mountains, monasteries and a monarch who has recently bestowed democracy on his people. But even in Shangri-La people need insurance.

Ngultrum, which is pegged to the Indian rupee. RICBL's establishment predated the arrival of the airport at Paro by eight years; this is why the head office is on the border with India. Now that the capital Thimphu is a good deal more accessible than a 10 hour drive over treacherous roads from the nearest Indian airport, moves are afoot to relocate the head office to the capital city. Not only will this make it easier for RICBL personnel to get to work, it will also make life a lot easier for consultants, reinsurers and others who wish to visit the head office.

Last year I made three memorable trips to this isolated kingdom to help bring RICBL into the 21st Century. Even getting there is a challenge—a three day trip from Ottawa, Canada, via Delhi (and yes, I flew by airplane). Twice I landed and took off from Paro Airport, the trickiest airport in the world. The pilots have to thread their way through the Paro valley to a tiny airstrip. And Paro was chosen for the site of the airport because it was the easiest place to land! Thimphu is now a short 45 minute drive away—before the new road was built, the 45 km trip took two hours. On my second trip I spent most of my time in Phuentsholing, on the border with India, where RICBL's head office is situated. This involved a flight to a regional airport in West Bengal and a two and half hour trip by road. I've also been driven between Thimphu and Phuentsholing, a seven hour trip for a 170 km journey on mountain roads that are prone to landslides, travelling mostly in the clouds—hence the need for frequent Buddhist monasteries and prayer-wheels (including ingenious hydraulically operated ones by the side of the road).



Flying from Kathmandu to Paro, a glimpse of Everest.

Until about 40 years ago, the country was essentially closed to outsiders (you needed an invitation from the king to visit!). There was no national currency, no financial institutions, and no links to the outside world. Royal Insurance Corporation of Bhutan Limited (RICBL) was established in 1975, shortly after the kingdom's central bank, the Royal Monetary Authority and the national currency, the



RICBL Building in Thimphu, with picture of HRH the fifth Druk Gyalpo, Jigme Wangchuk.

Visiting Bhutan is like stepping backwards in time. Men are required to wear their national costumes in public, the *gho*, which resembles a knee-length dressing gown, with an immense kangaroo pouch at the front, to be worn with oxfords and long argyle socks. Women wear the *kira*, a tight ankle length dress, on ceremonial occasions, but they wear a tight long skirt and short jacket on a daily basis. Foreigners are exempt, but some long-term residents wear the Bhutanese costume, especially for formal occasions. Wearing a suit to meetings with Bhutanese officials makes one feel distinctly over-dressed! There are no skyscrapers, only traditional two or three story buildings decorated with good luck symbols (including the ultimate good luck symbol, a phallus, to be seen on a number of official buildings!). And no need for smoker and non-smoker rates, this is the world's first non-smoking country (the sale and importation of tobacco products are prohibited). Unfortunately, this is made up for by the national habit of chewing *doma* (known in India as *paan*), the so-called betel nut concoction that makes teeth and gums go red and accounts for the red blotches all over the side-walks (although spitting is prohibited). *Doma* is also carcinogenic, of the mouth rather than the lungs. We have not yet recommended chewing and non-chewing rates!

Given the time-warp look of Bhutan, it's not surprising that the insurance line-up has an old-fashioned look to it. Being the only insurance company in the kingdom, it is naturally a composite. Draft legislation, in accordance with best international practice was about to prohibit composite insurance companies, but fortunately this was

changed to permit existing companies to remain composite, provided the accounts were carefully separated. This was an example of taking "best international practice," misapplying it and nearly messing up a perfectly good company for no good reason. Unfortunately, there was a further legacy from the past which was not quite so easy to fix. Since RICBL was one of the first financial institutions in the kingdom it tended to be "all things to all people." As a result a considerable portion of the assets consists of personal and business loans. While this might not seem to be all that bad for a "financial conglomerate," RICBL is not structured in this way. Given the limited investment opportunities in the kingdom, rearranging RICBL to look more like a financial conglomerate is proving very challenging, but hopefully will be achieved without too much dislocation.

On the property and casualty side, naturally the vast bulk of the premiums are for compulsory motor vehicles insurance, and most of that is third party. Also fire insurance is a significant line. All lines are very heavily reinsured. The project examined the retention from a variety of stand-points and concluded that retentions could be increased very considerably—RICBL was simply ceding away most of its profits. This is probably the case with many insurance companies in emerging markets. It follows the Indian tariffs, which of course have very little to do with experience in Bhutan. Also India is "de-tariffing," in other words, the Indian market is being liberalized, so Bhutan risks using tariffs taken from another jurisdiction which no longer uses them! At some point Bhutanese experience will have to be examined and applied to rate

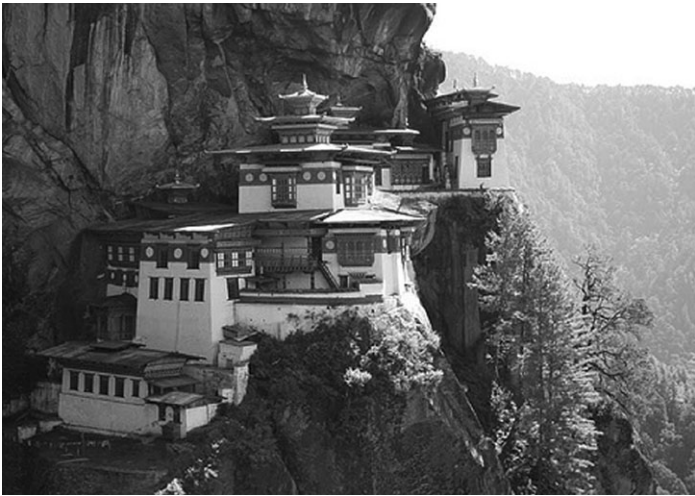
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making and reserving. Reserving is completely arbitrary, based on government fiat of 60 percent of premiums. Earned or written? Who knows? Probably written, although the accounts say earned. In fact, one line showed very anomalous results that were quickly straightened out by switching from written to earned (at least on an approximate basis, given the data in the annual reports), which was a text book case of distortions introduced by using written premiums for loss ratios. Claims? Probably mostly paid, but given that these are quickly developing lines, the distortion is probably not too bad, but I did include “Insurance 101” in my training course, an eye-opener for most of the staff.

One challenge in fire insurance is to insure Buddhist monasteries, of which there are a great deal and many very historic. In fact these are *fortified* monasteries (*dzongs*) going back to the days when the monks were armed and fought pitched battles with each other and various invaders (the image of peaceful Buddhist monks is strictly late 20th Century). Monasteries burn hundreds of votive candles, which are permanently lit, in small

wooden structures next to the monastery and of course no sprinkler systems—fire insurance quote anyone? Mostly they are rebuilt by the state when they burn down (including tragically Takhsang, or the Tiger’s Nest, which is a four hour hike from the parking lot but is magnificent. Though, not as magnificent as the original which burned down in 1999).



The new Takhsang, a national treasure but also a fire hazard.

On the life side, most of the policies are traditional U.K. style reversionary bonus with profits. Most are very savings-heavy and in fact the most popular policies are the ones that give cash back relatively quickly, begging the question as to why people save at all. Rather picturesquely, the valuation is done by an Indian actuary on an old manual Remington, complete with corrections in liquid ink, but on a policy premium method. The draft legislation wanted to mandate the net premium valuation method (with zillmerization). I also suggested that they require it to be hand-written with a quill pen. Again, my recommendation was a more modern approach to life insurance valuation (preferably by computer, but if they want to type the report on an old Remington, that’s okay by me). Of course, the reversionary bonus was calculated in shall we say a “non-transparent” method and people (including senior officials of the company) tended to equate the bonus rate to the rate of interest earned on bank deposits. People wanted to compare the “investment return” from the life policy to returns on other investments, a challenge for actuaries, let alone the lay-person. My suggestion was to junk all this stuff (including a quaint policy aimed at “the ladies”—politically correct hasn’t reached Bhutan yet) and replace it with universal life, which can be compared more easily to other investments.

I also suggested a guaranteed issue policy for those seeking pure life insurance. In fact there is a case for “death insurance”—funeral rites, the *puja*, can run to over \$1000, a fortune in Bhutan, especially for rural dwellers (80 percent of the population). Often families go into debt for this. The government provides some subsidized insurance, but not enough.

“It does not measure progress by means of the increase in Gross National Product, but in GNH—Gross National Happiness”

Bhutan is famous for inventing “stochastic analysis”—in fact “stochastic” comes from a Greek root meaning “ability to shoot an arrow straight” and this is exactly what happens in Bhutan—archery is the national sport, as this picture shows (it also illustrates the *gho*).



A straight-shooter, stochastically speaking.

It is also famous for inventing the six-sided form of statistical analysis, as illustrated below:



No need for insurance—divination by a throw of the dice

But change is coming to the kingdom. Not only did they hold their first democratic elections recently, but the Royal Monetary Authority (the financial regulator) is examining applications for licenses for new insurance companies, so competition is coming to the cozy world of the RICBL. Also, a more rigorous regulatory regime is in the works. When this happens, RICBL will need to move proactively to protect its position by offering more competitive rates and a better range of products. It has recently created a customer relations unit, which has undertaken a customer satisfaction survey, so the company is clearly moving in the right direction.

Bhutan is in the forefront of the environmental movement—while it desires development it will not sacrifice its fragile environment in the process. In fact it does not measure progress by means of the increase in Gross National Product, but in GNH—Gross National Happiness. Forests, rivers and mountains are sacred, so although it has abundant hydro-electric resources it plans to exploit them mostly by flow-of-the-river turbines rather than by building dams and reservoirs. Tourism is encouraged, but only in limited numbers. Climbing Bhutan’s highest peak, Jhomulhari is off-limits. This cautious approach to development will present the insurance industry with challenges (currently the “industry” is only one company, but that will change in the not-too-distant future). Direct writers can only retain very small percentages of mega projects and other hazards (for example Druk Air, the only airline to fly in and out of Paro, only a few basis points are retained). As tourism grows there is scope for enhanced insurance, at least of the tour operators (most of the visitors would hopefully have their own insurance), especially if more hazardous sports, such as sky-diving and white-water rafting are permitted. More in-

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novative life products will expand coverage and give consumers more choice and of course greater retention will keep more Ngultrum in Bhutan and give the insurance industry more opportunity to practise a wider range of risk management.

This was my second project in Bhutan (the first was a pension project) and my wife and I fell in love with the country (as do most visitors). I am hoping to return to help Bhutan's financial sector (both pensions and insurance) progress into the 21st Century. While much will change in Bhutan, and for the better, it is the fervent hope of many of us who visit Bhutan that much will remain the same. This is one of the most unusual places in the world and surely the model for Shangri-La. It is the last Himalayan Buddhist kingdom and contains many treasures from the past. I am privileged to be able to work and live there, and to get to know the people (who all speak impeccable English, as well as Dzongka, the national language and often their own local languages as well) and partake of the customs (for example, chilli peppers are eaten as a *vegetable*, bring your fire-extinguisher to every meal). I have only seen a small part of the country, and hope to see more on further visits. I also wish to monitor their progress in increasing GNH and developing their country in an ecologically sound manner. While Bhutan has much to learn from

the West, we could do no worse than looking for wisdom in an ancient land that still reveres nature and develops its economy by working with nature and not destroying it. Insurance has its part to play in both preserving what is good and guarding against hazards that could damage the natural order. I hope to be able to continue to help the Bhutanese to achieve this.



Michael has been involved in consulting in developing countries in projects mostly funded by international donors for the last eight years. He has undertaken insurance, pension and regulatory strengthening projects in East and Central Asia, Eastern Europe, Africa, the Caribbean and Latin America. □

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