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An Example of the New Silk Road: The Creation of a New Private Insurance Industry in Post-Mao China

By Charles Bentzin

For thousands of years the Silk Road stretched by land and water routes from the central plain of the Yellow River in China eastward to Japan and Korea, westward through the Eurasian land mass as far as Turkey and the Eastern Mediterranean and to North Africa and south to Southeast Asia and the Indian Sub-continent. During several times in the Silk Road's history Chang'an (now called Xi'an) was considered the beginning of the Historic Silk Road.

The Silk Road encouraged trade and the transfer of things, ideas, and technology. Today trade and the transfer of ideas and technology between different peoples and countries, by whatever the means, is the successor to the historic Silk Road. To illustrate the operation of the New Silk Road, this article will outline some of the steps involving the transfer of ideas and technology which enabled the creation of a new private insurance industry in post-Mao China.

During Mao's reign the government owned or controlled most or all of the means of production, distribution, and allocation of all of China's goods and services. This included the government providing economic security which was said to be from the "cradle to the grave." Consequently, most or almost all of the risks that might arise to any firm, institution or individual during Mao's reign were assumed by the Chinese government and the Chinese government did not see any need for any insurance to help them deal with these numerous risks. This pooling of all risks in China was similar to the practices of many other countries. In China only a few demands for insurance arose because any losses arising from most risks were paid for by the government. In the few circumstances where risks needed to be insured, the Chinese government required that all insurance on any lives or goods within China be provided by a Chinese government owned insurance company.

The small amount of insurance used in China was usually related to the importing or exporting of goods while the goods were in transit within China. This Chinese insurance usually did not apply when the imported goods were still waiting to be unloaded from the delivering ship or when the exported goods had been loaded onto the outgoing ship. At these times these goods were usually insured by commercial insurance companies not owned by a government. Consequently this Chinese insurance usually involved policies of very short durations; sometimes as short as a few days or weeks. To fulfill these limited insurance needs for goods in transit within China the Chinese government created the Peoples Insurance Company of China (PIC). Because of the limited nature of the PIC's activities, PIC personnel had a much narrower and limited insurance experience than similar persons employed by a typical private insurance company in the west.

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After the end of Mao's reign, the Chinese government decided to adopt a modified and controlled market economy model. This meant that the government, over time, would no longer own or control most or all of the means of production, distribution, and allocation of all of China's goods and services and that the government would no longer provide security for its citizens from the cradle to the grave. Consequently, a large number of risks arose which individuals, institutions, and corporations needed to address while they were managing their lives and companies. However, the government had determined that these new insurance needs should be filled by private Chinese domiciled insurance companies. This lead to the creation of a new private Chinese insurance industry.

Several press reports stated that it is likely that the Chinese government had determined that the cost to the Chinese government of the previously promised cradle to the grave economic security was going to be too much for the government to bear and that the government should encourage individual Chinese citizens to pay for the cost of their own economic security through insurance purchased from private insurance companies. There has been no official confirmation of the Chinese government's intention that each citizen would pay for that citizen's own economic security. But it is not surprising that such an intent could exist since in numerous countries, it is likely that benefits that the government has promised to its citizens will, over time, cost more than the country will be able to afford.

To verify that these new private Chinese insurance companies would be able to properly provide for the insurance needs of Chinese citizens and organizations the Chinese government adopted rules and regulations covering the formation and operation of the privately owned Chinese insurance companies. The new private insurance companies included Chinese-owned companies, companies partially owned by Chinese firms and partially owned by non-Chinese (such as Ping An that was partially funded through Goldman Sachs), and insurance companies entirely owed by foreigners such as the American Insurance Group (AIG), which was formed in Shanghai in the 1920s by C. V. Starr.

As previously noted, insurance involves promises that have been created by people and that need to be administered by people. The proper management of an insurance company requires a dedicated management and staff with many different skills. Employing qualified persons with the requisite skills, integrity, and experience was extremely important to these new private Chinese insurance companies.

Some of the different types of skilled staff required for the effective operation of private insurance companies include:

1. Governmental regulators who are capable of determining whether a new private insurance company is sufficiently well capitalized and managed to be permitted to provide insurance and who can continually monitor each company's continuing operations.
2. Boards of directors and senior officers to establish and maintain appropriate company policies and to make certain the companies operate in an appropriate manner.
3. Marketing and sales personnel to identify possible risks that could be insured and determine the most efficient ways to reach these insurance markets.
4. Underwriters to classify and evaluate the risks that are being considered.
5. Actuaries to determine the premiums to be charged, the reserves to be established, and cash flow requirements.

6. Investment professionals to invest the insurance company's funds to provide a sufficient rate of return, liquidity, and safety and to provide for the cash flow needs of the companies.

7. Claims personnel to effectively and properly determine the amounts to be paid under the policies.

8. Attorneys to draft the policy forms, deal with legal matters, assist with the payment of claims, and assist with the preparation of documents to be filed with the regulatory authorities and other stakeholders.

9. Accountants to properly record and present the company's financial results, possibly on both Statutory (according to applicable laws and regulations) and GAAP (Generally Accepted Accounting Principles) bases, assist in the preparation of any forms required to be filed with regulatory authorities and with any stakeholders, calculate the company's tax liabilities, and prepare any required tax forms and returns.

10. Information technology specialists to develop systems that accurately provide information to all company personnel to that they can quickly and effectively do their work.

All of these persons would need to work efficiently and well together for the insurance company to achieve satisfactory results.

For companies, like AIG, that already had large overseas operations, transferring personnel and systems to China was relatively easy and rapid. For most other companies it was more difficult and time consuming. There were few, if any, thoroughly trained and experienced insurance people already living in China. As previously noted, the PIC personnel's experience was limited. In addition, there had been no private insurance companies in China from when Mao took over China in 1949 until after his death in 1976. Earlier, after the Japanese attacked China in 1937, the then existing insurance industry severely restricted their operations. As a result, there were few, if any, experienced insurance personnel available in China. For the few that remained, their knowledge was extremely out of date.

Companies tried to recruit Chinese living in Taiwan or overseas who were working in insurance companies and also recruited the relatively small number of professional insurance personnel living in Hong Kong. To the extent possible they also outsourced certain operations. Perhaps most importantly, they instituted aggressive training programs which included the methods, information, and techniques already being used in other countries. All of these efforts were influenced by the realization that it takes a long time to train insurance personnel. For example, to become a fellow of the Society of Actuaries has taken candidates, on the average, eight years. The Society of Actuaries assisted in establishing actuarial programs in universities in Beijing and Hong Kong to facilitate the training of Chinese actuaries.

All of these efforts to recruit and train qualified insurance personnel who would enable the creation of an effective and viable new private Chinese insurance industry in China represent the transfer of ideas and technology-which was the essence of the activity along the Silk Road. This is why the creation of a new private insurance industry in post-Mao China is a worthy example of exchange along a New Silk Road. □