China market opportunities for foreign insurance companies under the new opening-up policies

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This report only covers insurance products and institutions for general consumers

1. Foreign insurers continue to embrace new opportunities as China accelerates the opening-up of its financial sector

Since the 1990s, close to 50 foreign insurers have entered the China market, predominantly in the form of joint ventures (JVs). However, the scale of these ventures has been relatively small due to regulatory restrictions, which limit the percentage of foreign ownership and the rate of branch expansion. By the end of 2018, the top 10 life- and non-life insurance companies in China were all Chinese controlled, with combined market shares of 73.5% and 85.2% respectively (Table 1). No single foreign or Sino-foreign joint venture insurer (in both life and non-life insurance) accounted for more than 2% market share.

Table 1: China life and non-life insurers ranked by 2018 primary premiums

Life Insurers

Type	Rank	Company	Mkt Share
Chinese Enterprise	1	China Life	20.4%
	2	Ping An	17.0%
	3	CPIC	7.7%
	4	Huaxia	6.0%
	5	Taiping	4.7%
	6	New China	4.7%
	7	Taikang	4.5%
	8	PICC	3.6%
	9	Funde Sino Life	2.7%
	10	Tian An	2.2%
Sino-foreign JV	16	ICBC-AXA	1.3%

Non-life Insurers

Type	Rank	Company	Mkt Share
Chinese Enterprise	1	PICC	33.0%
	2	Ping An	21.0%
	3	CPIC	10.0%
	4	China Life	5.9%
	5	China Continent	3.6%
	6	China Insurance	3.6%
	7	Sunshine	3.1%
	8	Taiping	2.1%
	9	China Export & Credit	1.7%
	10	Tian An	1.3%
Sino-foreign JV	16	AXA Tianping	0.5%

Note: life insurers refer to the companies whose business scope cover life insurance, health insurance and/or pension insurance. Non-life insurers refer to those covering property and casualty (P&C) insurance.
Source: China Banking and Insurance Regulatory Commission (CBIRC)

However, since 2019, the competitive dynamics in the insurance market have been changing, as China continues to ease market access restrictions on foreign insurance companies.

There are three key changes in the new opening-up measures:

- First, removing the requirement that the foreign insurers must have operated for at least 30 years before entering the China market;
- Second, removing any ownership caps on foreign insurance companies in a Sino-foreign JV, allowing for 100% foreign-owned entities;
- Third, abolishing any rules on branch establishment and management that specifically apply to foreign insurers. This means the rules and regulations for foreign owned insurance companies are the same as the ones for domestic owned companies[1].

Since the new measures were rolled out, a number of foreign insurance companies have sought to increase their shareholding percentages in their existing joint ventures in order to become the majority shareholders. Other foreign insurers are setting up new wholly- or majority-owned insurance institutions in China through acquisitions, new joint ventures or new strategic partnerships (Figure 1). In 2019, Allianz announced that it had been approved for setting up the first wholly foreign-owned insurance holding company[2] since China joined WTO. AXA completed the acquisition of the remaining 50% stake in AXA-Tianping which has become the largest wholly foreign-owned property and casualty insurance company in China[3]. HSBC has reached an agreement with its partners in China to acquire the remaining 50% stake in HSBC Life[4]. Chubb Limited is seeking majority control of its investment, having already gained approval to increase its shareholding in Huatai Insurance Group from 25% to 30%[5]. Insurers such as Prudential plc, Generali and Manulife have their eyes on China's large pension market and have already started preliminary negotiations with relevant authorities to enter the market[6].

According to Sina.com, in 2019, the premium income from foreign or Sino-foreign JV insurance companies in China increased by 29.9% year-on-year (YoY), more than doubling the 12.2% growth experienced by domestic owned insurers. The total market share of foreign/joint venture insurers increased by 1% to 7.2%. With the full implementation of the less restrictive market access policies, the market share of foreign insurance companies is expected to further increase[7].

In addition to the aforementioned policy reform, the China Banking and Insurance Regulatory Commission (CBIRC) has issued a series of new policies which will allow foreign insurers to more easily enter the asset management sector[8]:

- Foreign ownership caps have been removed, and the same standards now apply to both domestic and foreign owned companies. The restriction that "domestic insurance companies shall hold no less than 75% of the total shares of insurance assets management companies" has been abolished, allowing foreign investors to hold more than 25% of the shares with no upper limit. Overseas financial institutions can now directly establish or invest in a pension fund management company.
- Furthermore, the Interim Measures for Insurance Assets Management Products became effective on May 1, 2020, allowing insurance asset management products to be sold to eligible natural persons. This aligns the insurance asset management business scope and model with other asset management companies. Insurance asset management companies can appoint other financial institutions to sell their products, or sell the products by themselves. These policies have paved the way for foreign insurers to develop their asset management business in China.

Figure 1: Important policies and key milestones for foreign insurance companies in China (1992~2020)

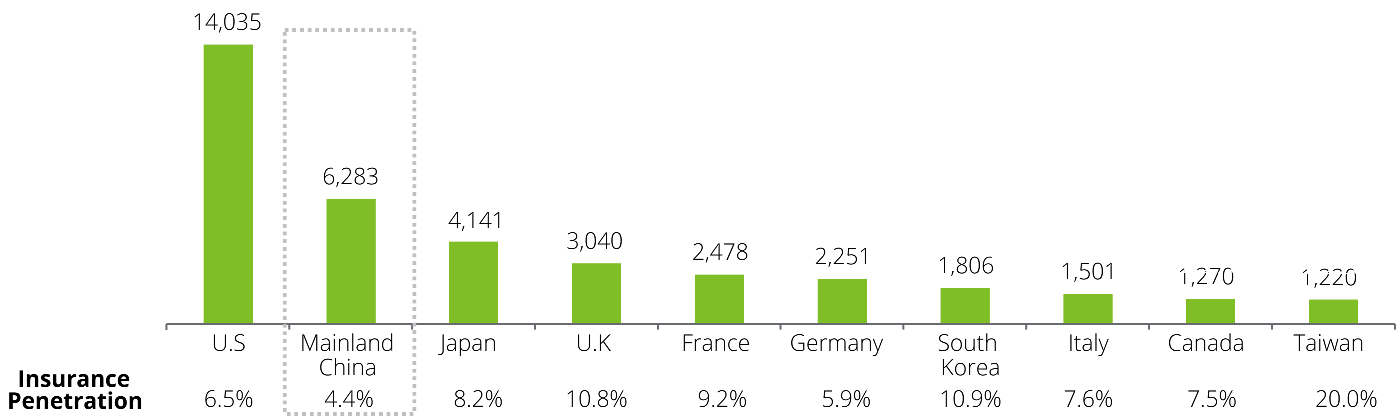
Phase	Year	Opening-up Policies	Key Milestones: Foreign Insurance Companies In China
Starting-up	1992	***Interim Administrative Measures of Foreign Insurance Companies in Shanghai*** • People's Bank of China publishes relevant regulations to supervise AIA	***The People's Bank of China grants approval for AIA to establish a branch in Shanghai*** • Types of insurance: life • The first wholly foreign-owned life insurance branch
Growing	2002	***Regulations on Foreign Insurance Companies - the first formal regulation*** • Allows foreign ownership for life insurance JVs up to 50% ownership • Limits business scope and regions for non-life insurance JVs	***China joins the WTO. New York Life (USA), Metropolitan (USA), and Nippon Life (Japan) obtain Chinese insurance license*** • Type of insurance: life
	2004	***Detailed Implementing Rules on Administration of Foreign Insurers in China*** • Requires that applicants must have more than 30 years of insurance experience, with a representative office set up in China at least 2 years ago prior to the submission of the application • Allows foreign-invested non-life insurance branches to be converted to WOFE • Cancels regional restrictions	***14 foreign insurance companies account for 2.3% of total premium income***
	2018	***April, 2018 - Notice on Expanding the Business Scope for Foreign Insurance Brokers and Agents*** • Allows foreign insurance brokers and agents to cover the same business scope as their Chinese peers	***November, 2018 - Allianz receives CBIRC approval for establishment of a wholly foreign-owned insurance company*** • Types of insurance: life, non-life
		May, 2018 – Administrative Measures on Foreign Insurance Companies (draft) • Allows foreign ownership of life insurance JVs up to 51%	***November, 2018 - AXA announces it will acquire the remaining 50% stake in AXA-Tianping, becoming the largest wholly foreign-owned P&C insurer in China*** • Type of insurance: non-life
Developing	2019	***May-July, 2019 – CBIRC announced its plan to release 19 policies to further open up the market*** • Advances the transition period for removing foreign ownership caps in foreign-invested life insurance companies to 2020	***March, 2019 – Heng An Standard Life is granted approval to develop pensions insurance*** • Type of insurance: life
		October, 2019 – Amendment of the Regulations on Administration of Foreign Funded Insurers • Eases the entry conditions for foreign insurance companies by removing the requirement that "they must have more than 30 years' experience in insurance business, with a representative office set up in China at least 2 years ago prior to the submission of the application"	***August, 2019 – CBIRC approves AXA to take full ownership of AXA-Tianping*** • Type of insurance: non-life
	2020	***December, 2019 – Notice on Clarification of the Timeframe for the Cancellation of Foreign Ownership Restrictions on JV Life Insurers*** • Foreign ownership restrictions on life insurance JVs is relaxed, allowing 100% foreign ownership, starting from 1 January 2020	***October, 2019 – ERGO (Germany) and Great Wall Motors (China) sign a JV for auto mobility insurance*** • Type of insurance: non-life
			November, 2019 – Chubb purchases an additional 15.3% stake in Huatai, increasing shareholding to 46.2% • Types of insurance: life, non-life
		December, 2019 – Amendment on Administrative Measures on Foreign Insurance Companies • The terms for local insurance companies are now equally applicable to foreign companies	***January, 2020 – Allianz (China) Insurance Holding Co. Ltd launches in Shanghai*** • Types of insurance: life, non-life
			January, 2020 – AIA announces its intention to convert its Shanghai branch into a wholly foreign-owned life insurance subsidiary • Type of insurance: life

Source: CBIRC

2. The China insurance market has significant growth potential, compared to more developed markets

In terms of market size, China has grown into the world's second-largest insurance market after the United States. In 2019, China's annual premium income reached 0.63 trillion dollars[9], surpassing other major insurance markets, including Japan, Britain, France and Germany. However, in terms of insurance penetration, China's total insurance premium income represented only 4.4% of GDP in 2019, still far behind those of developed markets (Figure 2).

Figure 2: Total premiums by country/region in 2019 (unit: $100 million)



Source: CBIRC, Fitch Solutions, Deloitte Internal database

The gaps between China and developed insurance markets could be broadly attributed to three aspects:

Insurance awareness has historically been low, resulting in lower levels of coverage. There are 4.2 insurance policies per capita in the United States and 6.5 insurance policies per capita in Japan. However, the per capita insurance policy rate in China is only about 0.6, which translated to far less than 1 policy per capita[10].

Less product choice compared to developed markets. In developed markets, consumers have a wide range of insurance products available to them, covering all aspects of their daily live. For example, when purchasing a property, in addition to the basic

housing insurance, customers can also buy personal property insurance, personal umbrella insurance[11], flood insurance and home loan insurance. There are also insurance products covering home appliances and furniture purchases, pet insurance and an array of other products. Many of these products are becoming increasingly available but in concept are still new to Chinese consumers.

Sales channels and customer services are not well developed.
Most domestic insurers heavily rely on agent based distribution systems, and do not provide base salaries to their agents, meaning their compensation is derived purely by commissions. In order to maximize their sales, sales practices may potentially produce higher insurance coverage than customers' risks may actually need, resulting in significant gap between the actual, viable claims and customers' expectations. In developed markets, insurers provide more comprehensive training and implement a stricter protocol on sales and distribution teams. As a result, sales agents are not only able to provide professional services, but can also customize services based on customer's protection and saving needs such as offering family protection, medical care, annuity, pension and investment. In recent years, CBIRC has issued stricter quality regulations for the insurance workforce, leading to some visible improvements; however, there is still significant room for improvement.

With a growing middle class and rising awareness of the need and purpose of insurance, Chinese consumers' demand for better insurance products and services will increase further.
The accelerated opening-up of the financial sector has further energized the insurance sector in China. Competition from foreign insurers will push domestic insurers to learn from global best practices, and better shape China's insurance industry in terms of corporate governance, risk pricing and investment management. This will help bridge the gap between China and more developed insurance markets.

3. Key constraints for foreign insurance companies' market development in China

There have been two long-standing barriers for foreign insurance companies doing business in China:

First, obtaining the required insurance licenses. In China, all insurers are required to apply for an insurance license from CBIRC before starting their operations. Companies need to meet certain qualification criteria before their applications are accepted. The different types of insurance licences in China include: life, health, pension/annuity, P&C (property insurance, liability insurance, credit insurance, etc.), reinsurance and internet insurance (internet insurance's scope is limited to P&C and short-term health insurance) licenses. For a foreign firm, the more types of licenses obtained, the wider the business scope can be, but the longer it takes to apply. Currently, the entire process can take at least two years from license application submission to regulatory review, to license approval and finally approval for opening the business (Figure 3)[12].

Figure 3: Insurance license application and business opening approval processes for foreign insurance companies in China

1 Insurance license application

Application	Establishment requirements: Year-end total assets must exceed US$5 billion prior to the application. The country of the applicant has a mature supervision system. The applicant has been effectively supervised and meets solvency standards. The applicant should obtain approval from their country. They may be required to fulfill other prerequisites.
Approval	CBIRC will review and approve/reject within 6 months from the date of receiving the application. The applicant will receive formal application forms if approved.
Preparing	The applicant must complete the preparatory work (for Business Opening Approval) within one year of receiving the formal application forms (they can apply for a 3 month extension if needed).

2 Business opening approval

Application	The applicant should submit documents with detailed company information.
On-site Inspections	CBIRC will undertake on-site inspections to ensure insurers have put in place effective internal controls. The applicant must report the status of their preparation work and demonstrates underwriting and claims process.
Approval	CBIRC will review and approve/reject within 60 days from the date of receiving the application.

Source: CBIRC

The new opening-up measures have not yet fully gone into effect, so it is too early to fully assess their impact on the insurance license application and approval process. Already, though, of the 36 approvals granted by the CBIRC in 2019 (including license issuance, ownership changes, and registered capital changes), 15 cases were related to foreign insurance companies. A local Chinese media source, Securities China, recently commented that foreign insurers have been enjoying "super-national treatment" when it comes to application approvals. There is speculation that applications and approvals may be further expedited for qualified foreign insurers in the next few years. After obtaining the insurance licenses, insurers need to meet regional regulatory requirements when opening business in different regions of China. If an insurance company wishes to establish a business in a province, autonomous region or municipality other than their initial regulatory domicile, they must first apply to the CBIRC for a provincial-level business check, and then apply to the provincial Banking and Insurance Regulatory Commission to set up local branches and sales offices[13]. Past cases suggested that the process could require at least 3-5 years' preparation time if the insurers plans to open business in more than 10 provinces.

Second, building nationwide sales channels. For foreign insurers with no existing presence/partnership in China, it would take at least 3-5 years and significant investment to build a direct sales/agent network that covers multiple provinces.

The first group of foreign market entrants in China tried to overcome these long-standing barriers by setting up JVs with large state-owned enterprises (SOE). By taking advantage of their SOE partner's existing network and resources, they could quickly obtain licenses and build nationwide sales channels through banks and postal services.

However, as of today, these joint ventures have only generated few successful cases. The main reason behind these difficulties has been the ownership caps. Restricted to no more than 50% shareholding in joint ventures, foreign insurers have faced significant challenges managing the JVs. Often, the foreign shareholder appoints the CEO or general manager while the Chinese shareholder appoints the chairman, and in some cases the two shareholders rotate the leadership and management every few years. This has made it difficult for the joint ventures to formulate a consistent and sustained business strategy. Under these conditions, any disparity in business vision, risk management, resource allocation, and culture is amplified. Consequently, internal friction has hindered many joint ventures from fully achieving their goals. The new opening-up measures will give foreign insurers a new opportunity to rethink their business models in China.

4. Possible paths for foreign insurers to enter or re-enter the China market

At the moment, foreign insurance companies will be considering how to best capitalize on the opportunities the new opening-up policies present. There are a number of possible options:

Option 1: Buying out existing JV partners
Some foreign insurers already have an existing joint venture in China. The new policies will allow these firms to consider buying out their Chinese partner and become the controlling shareholder of the venture. As of 2020, a number of foreign insurance companies are already in negotiations with their Chinese JV partners, aiming to increase their shareholding from 50% to full control[14]. However, there are many challenges to the buyout. For one thing, the majority of the JV partners are Chinese SOEs; due to strategic considerations, they may not be particularly willing to sell their shares. Even if they are willing to sell, they may often demand a high purchase premium.

Option 2: Set up Wholly Foreign-Owned Enterprises (WFOE)
For foreign insurers entering the China market for the first time (or planning to develop new businesses in China) setting up a WFOE has become an alternative pathway under the new opening-up measures. To do so, a series of regulatory requirements need to be met. First, they must obtain the relevant insurance licenses from CBIRC. Second, they need to obtain approval from local authorities to set up branches and sales network in every province they plan to carry out business. As discussed in Section 3, it can take several years from first applying to finally obtaining a license. In addition, establishing a multi-province sales network will require substantial investment, and an even longer and complicated ramp-up process. The new opening-up measures will take time to roll out, and it has not yet seen its impact on expediting this process.

Option 3: Acquire existing insurance companies in China
Acquiring a company that already has insurance licenses can be a shortcut for foreign insurers to quickly obtain the licenses they need. If the target already has businesses in multiple provinces and cities, the foreign firm will also benefit from the target's established sales channels and scale of business.

At present, the 129[15] Chinese insurance companies disclosed by CBIRC can be segmented into three tiers based on their market share (Table 2).

Table 2: Number of Chinese insurers and representative enterprises in 2018

Life Insurers

	Number	Representative
1st Tier	2	China Life, Ping An
2nd Tier	14	CPIC, Hua Xia
3rd Tier	47	CCB Life, Ping An Annuity
Total	**63**	

Non-life Insurers

	Number	Representative
1st Tier	2	PICC, Ping An
2nd Tier	9	CPIC, China Life
3rd Tier	55	Zhong An, Zking
Total	**66**	

Source: CBIRC

Most tier 1 and tier 2 companies are large SOEs with low willingness to sell their business and any potential sale would trigger very high expectations on their valuation. Tier 3 companies with business coverage in more than 10 provinces would be ideal acquisition targets.

Nevertheless, buyers will need to be prepared to face the reality of complex shareholding structures of most domestic insurance companies. Shareholding structures are mostly fragmented, and shareholders often include financial service institutions, real estate companies and other local enterprises. This creates challenges surrounding acquisitions, since it requires early negotiations and due diligence with a number of different shareholders. Take Yong An property insurance[16] (3rd tier) for example: the firm has business coverages in 32 provinces as well as 7 major shareholders including six manufacturing firms and one financial institution. Some of these shareholders are SOEs, and others are local private companies. Another example is the AXA-Tianping joint venture: even with a relatively simple shareholding structure, AXA still needed to negotiate with the five Chinese shareholders to buy out the remaining 50% stake. The transaction took almost a year to complete.

Option 4: Joint venture / partnership with InsurTech companies to acquire customers and channels

In recent years, a large number of technology companies focusing on the insurance sector have emerged in China. Their business is no longer limited to selling insurance online. They have reshaped the entire insurance value chain with disruptive innovations from product development to sales to claims and customer services.
By building an information platform and creating "contexts" (e.g. bicycle sharing, food delivery, hotel booking, crowd funding, etc.) that attract user traffic, InsurTech companies have been able to identify potential customers' insurance needs based on big data analysis. This big data analysis enables InsurTech firms to develop customized products, improve customer interaction frequency and service quality, and transform the customer acquisition process from the traditional mass promotion model to precision marketing. The application of new technologies such as AI, block chain, and cloud computing will enable automation and smarter solutions for processes such as underwriting, claims and customer support, significantly improving operational efficiency (Figure 4)[17].

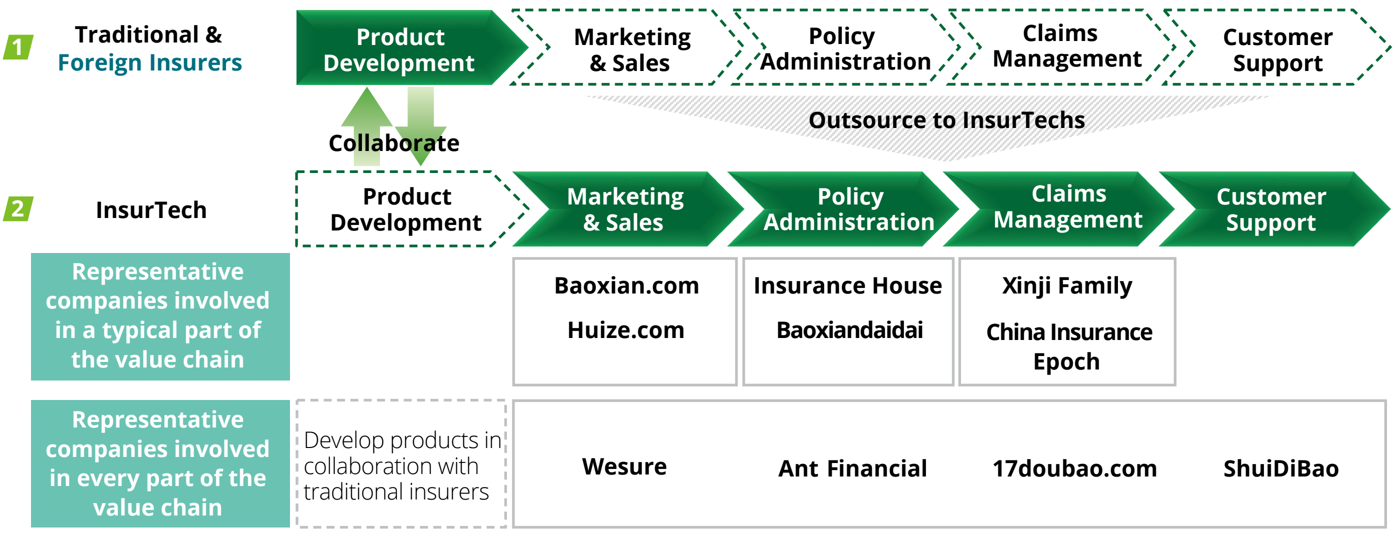
More and more traditional insurers have outsourced, or are outsourcing, their non-core operating processes, such as sales, policy administration, claims management and customer support, to InsurTech companies, with some even partnering with them for product development (Figure 5).

Figure 4: Technologies enabling China insurance value chain

	Product Development	Marketing & Sales	Policy Administration	Claims Management	Customer Support
Insurance Business	Market Research Product Design Risk Assessment & pricing	Precise Marketing Sales Channels CRM	Policy Administration Underwriting Billing & Collection	Damage Claim Fraud Detection Payment	AI Customer Reps Online Transaction 24/7 Service
AI		• Assist in online customer acquisition	• Electronic policy management	• Streamlined claim management process • Fraud detection in insurance claims	• Reduce costs
Big Data	• Personalized products • Accurate risk assessment and pricing	• Customer segmentation • Tailored marketing • Prevent customer loss	• Efficient underwriting process	• Better fraud detection through biometrics' risk scene identification	
Cloud Computing		• Integrated customer portals	• Automated systems and workflow for policy administration, underwriting and claims		
Block Chain	• Innovative products • Low-cost products	• Improved transparency and security		• Automated execution of claims • Reliable billing & payment process	
IoT	• Automated demand analysis • Generate new product offerings				

Source: Deloitte Analysis and Research, Insurance Association of China

Figure 5: Business models of InsurTech companies in China



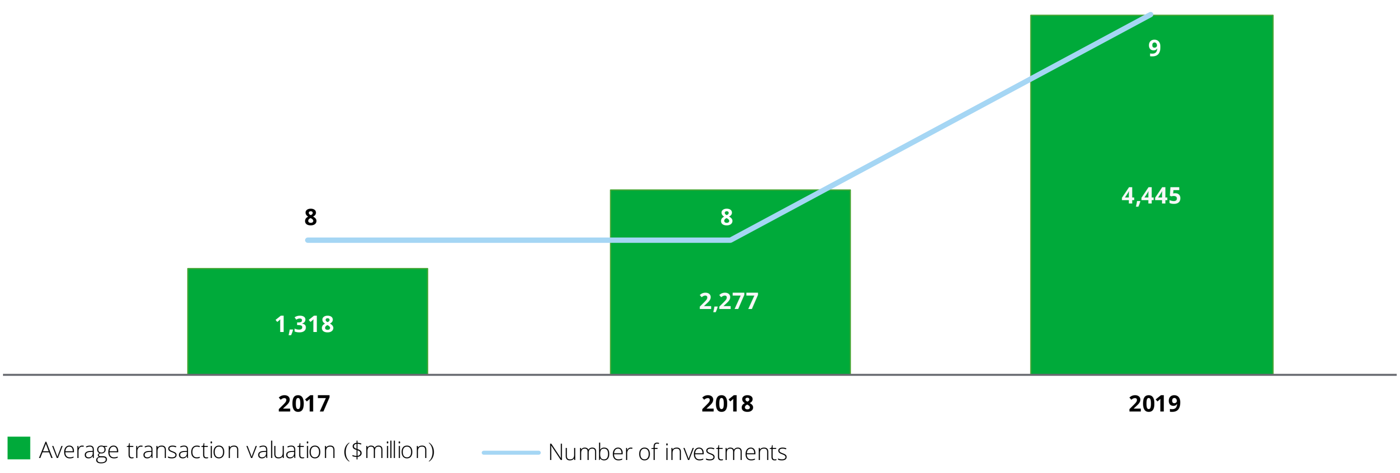
Source: Deloitte Analysis and Research

Through joint ventures or strategic partnerships with leading Chinese InsurTech companies, foreign insurers can quickly have access to multiple millions of user/customer data points, better understand customer needs, develop customized products, and conduct precision marketing. Outsourcing non-core processes can also help reduce labor cost and enable the foreign insurers to quickly scale up their business. By selling a 30% stake to China's leading e-commerce platform JD.com and leveraging the platform's digital resources, Allianz P&C insurance rapidly expanded its online business, with premium income increasing by 104% from 2018 to 2019[18]. The insurance firm also enjoyed significant growth in other performance indicators, such as profitability and the total number of customers served. In November 2019, AXA and ShuiDiBao, a leading online insurance sales platform in China, agreed to an in-depth collaboration around online sale, product development and operation[19]. The scale of online insurance sales has grown significantly in particular during the COVID-19 crisis. In 2020 Q1, the total premium income of online insurers Zhongan and Taikang Online increased 82% YoY[20]. The impact of COVID-19 is proving to be a powerful accelerator in the transformation of business models of traditional insurers and facilitate more partnerships between foreign insurers and technology companies.

5. The next three to five years will be the critical period for foreign insurers to develop their foothold in the China market

The new opening-up policies have brought unprecedented opportunities for foreign insurers in the China market. Local authorities are expected to facilitate the implementation of these new measures to enable easier market access for foreign insurers. At the same time, the next three to five years will provide a solid window of opportunity for mergers and acquisitions (M&A). A number of Tier 3 insurers have been facing operational challenges, with low profitability and slow business growth. This may lead some existing shareholders to seek potential exit opportunities. Given the impact of COVID-19 and any resultant economic downturn, we expect the M&A transaction valuation premium in the insurance sector to return to a more reasonable level, down from a record high in 2019 (Figure 6).

Figure 6: The number of investments and average transaction valuation in the Chinese insurance sector from 2017 to 2019



Note: The average transaction valuation has been calculated based on 100% stake; the number of investments only includes the deals that disclose the deal size.
Source: Mergermarket, Deloitte Analysis and Research

In addition, regulatory authorities have prohibited the asset-driven[21] liability model, pushing some tier 1 and tier 2 insurers to look for new business growth opportunities. There is significant disruption in the market, with nearly one third of domestic insurers changing management in the past two years. InsurTechs with an established user base and online channels are actively seeking traditional insurer partners. All these developments will lead to market expansion opportunities for foreign insurers. The impact of the COVID-19 may make the needs of local insurers more pressing and the opportunities for foreign firms easier to materialize.

"...The next three to five years will be critical for foreign insurers with respect to their China market development, amid new opening-up measures. Additionally, many small- and medium-sized local insurers are facing operational challenges and seeking new investors and business growth, creating more opportunities for foreign insurers..."

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Endnotes

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