ag insurance covers new ground

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assessing ag insurance claims is costly and labour-intensive

domestic ag market intervention impacts farmers worldwide, contributing to politicisation of trade

'green box' ag insurance subsidies give policymakers direct intervention alternative

Ag insurance protects crop producers, safeguards against poverty and creates non-farm employment—all top policy priorities for 2019. Policymakers hope a tie-up with futures markets will get insurers on board.

Direct state intervention in the farming sector aimed at self-sufficiency in grain production warped markets and left farmers dependent on payments, rather than profits, as they made planting decisions. Responding to new commitments following WTO accession, Beijing began opening agricultural markets in the early 2000s. In 2015, efforts began to remove domestic price floors and decouple subsidy payments from the market. Coupled with rising imports, this has resulted in a market access tug-of-war, as fears of dependence are weighed against huge domestic demand for crops that are unprofitable or too risky for China's small-scale farmers. Further, as intervention in the domestic market now exerts a huge impact on farmers across the world, China's agri-food market has become intensely politicised on a global scale.

Enter agricultural insurance—a WTO-friendly 'green box' alternative to direct subsidies. It allows policymakers to subsidise potentially costly coverage, weaning farmers off price floors and direct payments while guaranteeing their financial well-being. Heavy state involvement guarantees insurance products are aligned with state goals, including production of relatively unprofitable staple crops, guaranteeing low-income farmers stay above the poverty line, and encouraging investment into promoted sectors like seed companies.

how it works

Since Beijing first included ag insurance premium subsidies in the 2007 central budget, agricultural insurance has rapidly expanded both in terms of total premiums, and coverage of crop varieties and geographic areas. According to China Banking and Insurance Regulatory Commission (CBIRC) ag insurance premiums totalled C¥47.9 billion in 2017. Cost insurance is the most popular by far, although pilots are ongoing for price, income, and yield insurance as well as weather-based and disaster index insurance.

The 2016 no 1 document first linked agricultural insurance products with futures markets. In the 2017 no 1 document, pilots sought to support agricultural insurance products with hedging tools based on futures markets. These would support agricultural marketisation reform, allowing participants to hedge risk and providing an important reference for price-setting. To date, three insurance giants, People's Insurance Company of China (PICC), China Pacific Insurance Company and Ping An Insurance have been approved to offer 'insurance + futures'.

local governments have great deal of power in determining which companies may participate and are experimenting with ag insurance models

While ag insurance itself is centrally regulated, access for ag insurance agencies is determined by local governments, and business models vary widely across the country. Tuo Guozhu 庹国柱 Capital University of Economics professor describes four major modes of operation

- 'free competition' model
    - all ag insurance agencies approved by CBIRC can operate and develop business within the province or municipality
    - example: Beijing
- 'limited competition' model
    - only one ag insurance agency gets access to the market. Usually, the agency with access has a major state shareholder
    - example: Shanghai, where Anxin Ag Insurance Co., Ltd holds a monopoly
- 'government-company partnership' model
    - local government selects a small number of ag insurance companies to cooperate with. Insurers and local governments each take half of the premiums, profits, and risks
    - example: Jiangsu province

'collective insuring' model

around 10 insurance companies form an alliance, led by one company, and conduct ag insurance business as a collective. Premium subsidies are given directly to the alliance and allocated internally

example: Zhejiang province, where People's Insurance Company of China (PICC) leads the alliance

a turning point

2019 poised to be turning point for insurance + futures model

Following three years of rapid development in pilots linking ag insurance with futures, 2019 is poised to be a turning point, said Zhu Lihong 朱丽红 Dalian Commodities Exchange (DCE) vice general manager at a 20 Dec 2018 insurance industry summit. Fiscal commitment, in the form of premium subsidies, has grown rapidly—from C¥20 million in 2016, to C¥70 million in 2017, to an estimated C¥300 million in 2018. Pilots have expanded from roughly ten insurance products in 2016 to nearly a hundred by end 2018. In Q4 2018, pilots were promoted from county to province level for the first time with premium subsidies for full income and cost insurance to farmers growing corn, wheat and rice in six provinces.

Policymakers' enthusiasm for ag insurance flows from its political and economic convenience, allowing them to provide subsidies in direct alignment with state goals without breaking WTO commitments. The primary goals in question are threefold: poverty alleviation, staple crop production, and economic transition.

poverty alleviation

ag insurance facilitates poverty alleviation, protecting farmers from sliding into debt after a bad year

New pilot efforts have been carefully focused in regions earmarked for rural revitalisation and poverty alleviation, a time-sensitive task with just one year remaining to win Xi's siege on poverty (see cp.signal). Zhengzhou Commodity Exchange (ZCE) recently approved roughly 40 new ag insurance + futures pilots in Xinjiang, Yunnan, Gansu, Guangxi, and Anhui after two years of successful operation at smaller scale. Compared with previous initiatives, the new pilots

- cover new crops like sugar, cotton, and apples
- introduce new fundraising methods
- give farmers more choice on what to grow

By involving private sector players in poverty reduction and rural revitalisation, the state can diversify resources for these agendas away from direct subsidies and payments, while remaining compliant with WTO rules.

staple crop production

Most ag insurance premium subsidy funds, and the bulk of pilot efforts, have been focused on staple crop production—wheat, corn, rice and soybeans in particular. Early forays into ag insurance focused heavily on grain farmers in key counties—Dec 2016 management measures from Ministry of Finance (MoF) guaranteed central financing for a minimum 40 percent of premiums to grain farmers in these counties. MoF further extended subsidies to staple grain growers in Aug 2018. Ag insurance + futures efforts have also focused heavily on staple grains as well as oilseeds.

grain and oilseed farmers face high risks and contribute substantially to food security, giving them priority for insurance

A number of factors drive policymakers' focus on staple crop categories when designing ag insurance. These crops are seen as critical to food security, but are also areas where domestic farmers face strong competition from trade partners. As grain and oilseed growers are pushed to scale up and mechanise, they incur substantial financial risk that policymakers hope to defray. More practically, the ag insurance + futures model requires an active futures market for related crops or commodities to be covered—putting grain and oilseed categories at the front of the queue.

rural financial services

expanding ag insurance industry supports broader rural development agendas

Policymakers are keen to improve rural financial services, and view ag insurance as a critical aspect of that agenda. Basic financial tools and institutions like credit and insurance are needed to attract private capital into the sector. Development of banks and insurance services at the county and village level also creates non-farm jobs, raises local incomes, improves commercial data collection and supports 'balanced growth' targets. As rural insurance inevitably develops beyond subsidised ag coverage, agencies will already have infrastructure to serve clients there. To date, MoF estimates around 400,000 ag insurance service stations are in operation. With over 600,000 administrative villages domestically, and multiple insurers providing coverage, there is still room for expansion.

but will it work?

insurers wary of ag volatility and high cost of set-up in rural areas

Insurers, thus far, do not share policymakers' enthusiasm for ag insurance. It has long been considered a challenge due to relatively low incomes and technology adoption rates among clients, as well as high costs and low margins at the village level. Now, insiders at major insurers say they are struggling to build sustainable ag insurance business models due to immature derivatives market conditions and high levels of volatility in agriculture. A long-term subsidy plan is needed to provide clear incentives for companies to set up and staff offices, design products and invest in technology to make ag insurance profitable, argues Wei Bolin 魏柏林 PICC Poverty Alleviation division deputy general manager. Better collaboration and information sharing between futures, insurance and banking industries is also needed, but remains lower on CBIRC's priority list than support to the village-level banking sector.

note: Our mid-2017 signal 'Insurers at the gate' offers a reflection on how quickly the insurance industry has been harnessed to serve the state.

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profiles

Tuo Guozhu 庹国柱

Capital University of Economics and Business professor, China Social Security Institute council member

Well-designed ag insurance can underpin food security, advance marketisation of agricultural commodities, and lower food prices, argues Tuo. He proposes promoting income insurance to encourage new ag operators—particularly family farms—to expand their operations. Tuo hailed the 2018 merger of China Banking Regulatory Commission and China Insurance Regulatory Commission as critical to closing loopholes and preventing risks, later calling for further consolidation of ag insurance management under one agency responsible for planning, data collection and information sharing, and allocating premium subsidies to farmers. A trusted advisor to top policymakers on ag insurance institutional arrangements and business models, Tuo plays an active role in pilot design.

Zhang Qiao 张峭

Chinese Academy of Agricultural Science Agricultural Risks Management Research

Agricultural risk management and rural finance expert Zhang sees ag insurance at a crossroads. The industry has expanded from offering a single type of state-mandated coverage, to a diverse product mix serving a broad range of farm types. Zhang sees the next step as a shift from 'one size fits all' premium subsidies to broad liberalisation of banking and futures in support of ag insurance. Broadening pilot efforts linking it with futures are a better alternative to the old state-set minimum price system, he argues. Ag insurance is more capable of reassuring farmers, stabilising production, guaranteeing incomes and facilitating product price formation. However, domestic futures markets are not yet robust enough to effectively hedge risks for insurers and may experience extreme volatility if ag insurance + futures pilots are rolled out too quickly.

He Hao 何浩

China Insurance Regulatory Commission (CIRC) Asset Insurance Regulation Department former vice director

Prior to March 2018 institutional reforms, He was a vocal advocate of state-supported ag insurance and regularly appeared in domestic media interpreting ag insurance regulatory moves. Agricultural insurance will evolve beyond a natural disaster response tool, he argues, to provide comprehensive risk management as part of improving rural financial services. State fiscal support will continue to play a substantial role, but regulators need to clarify whether government is leading or facilitating development of ag insurance markets. He criticises current models as lacking 'service mindset and capacity' and failing to keep pace with supply-side structural reforms in farming. He suggests shifting focus away from controlling insurance market access, and toward ensuring products are robust and appropriate.

context

15 oct 2018	ZCE expanding insurance + future pilots to national targeted areas with poverty alleviation or rural development goals
aug 2018	two moves by MoF expand ag insurance pilots, establish a small leading group including MARA and CBIRC, and include seed companies among entities eligible for premium subsidies
16 jul 2018	MoF lists expanding ag insurance among top near-term priorities to support poverty alleviation (2020) and rural revitalisation (2022) goals
feb 2017	No. 1 Document again calls for expanding ag products and derivatives markets to facilitate further expansion of ag insurance + futures
19 dec 2016	MoF issued 'Management measures for fiscal subsidies of ag insurance premiums'
22 nov 2016	Insurance Association of China issues 'Agricultural insurance service general rules', the first industry standard for ag insurance
17 nov 2016	NDRC rural development 5-year plan includes substantial commitment to ag insurance set-up
8 oct 2016	State Council adopts national ag modernisation plan including commitments to revamp subsidy and insurance systems to facilitate a professionalised ag sector
27 jan 2016	No.1 Document first proposes linking ag insurance to future market
25 mar 2015	CIRC released 'Management measures for ag insurance underwriting and claiming'
12 nov 2012	State Council passed and released Ag Insurance Articles, which came into effect in March 2013
13 apr 2007	MoF first includes ag insurance premium subsidies into the central fiscal budget
feb 2006	No. 1 Document calls for ag insurance pilots
2003	ag insurance is prioritised at the third plenum of the CPC 16th Central Committee. China Insurance Regulatory Commission (CIRC) proposes five development models
2001	total ag insurance coverage value has fallen over half a billion RMB in a decade, to just C¥236 million. Policymakers again turn attention to ag insurance during WTO accession as coverage is considered a 'green box' subsidy
1992	market reforms include unprecedented liberalisation, insurance companies turn away from ag insurance and develop more profitable insurance types
1987	total ag insurance coverage reaches C¥100 million; it will grow to C¥817 million by 1992