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**RUSSIAN INSURANCE INDUSTRY AND ITS FUTURE  
CHALLENGES**

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### Selected abbreviations:

CMTPL = Compulsory Motor Third Party Liability

FSSN = Federal Service of Insurance Supervision (Federalnaya Sluzhba Strahovogo Nadzora)

CMI = Compulsory Medical Insurance

MRUR = Millions of Russian Roubles

BRUR = Billions of Russian Roubles

MUSD = Millions of US-dollars

BUSD = Billions of US-dollars

## Foreword

The Northern Dimension Research Centre (NORDI) is a research institute run by Lappeenranta University of Technology (LUT). NORDI was established in the spring 2003 in order to co-ordinate research into Russia.

NORDI's mission is to conduct research into Russia and issues related to Russia's relations with EU with the aim of providing up-to-date information on different fields of technology and economics. NORDI's core research areas are Russian business and economy, energy and environment, the forest cluster, the ICT sector, as well as logistics and transport infrastructure. The most outstanding characteristic of NORDI's research activities is the way in which it integrates technology and economics.

This volume “Russian Insurance Industry currently and it’s future challenges” tells about Russia – one of the largest potential insurance market in the world, which surprisingly is relatively unknown. This study aims to provide readers with overview of the contemporary Russian insurance industry and its comparison to other insurance markets.

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Lappeenranta, December 2004

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## **Executive Summary**

Russian insurance industry's history can be divided in three periods: before the year 1917, between 1917 and 1988 and after the year 1988. During the first historical period Russian insurance industry reached the position among the leading insurance countries. On the eve of World War I, Russia had 19 active joint stock insurance companies with an aggregate capital of MRUR 48 and total assets about MRUR 300 (the amount is comparable to 1/10 of the entire national budget). In the early 20<sup>th</sup> century, Russia held the second place in the world by total value of fire insurance premiums collected, while its position by total volume of insurance business (5) was consistent with its share in the global industrial production.

The second period was dominated by the experiment with central planning. In the year 1918 the Soviet Government nationalized all the Russian private insurance companies and created a state monopoly for insurance industry. This period continued for the next 70 years. During the years 1918–1990, the Insurance legislation in Russia was limited by the needs of state monopolists. There was no basic law on insurance. Only a few regulations concerning relations of insurers and certain categories of the policyholders existed. The only professional insurance people in the country were in Rossgostrakh and Ingostrakh which were the only “insurance companies” in Russia.

It is often maintained that the state insurance monopoly in Russia was abolished not earlier than in 1988 by the Law on Co-operatives. As a matter of fact, already in 1958 the new bylaw on State insurance cut out the paragraph about such a monopoly. This paragraph can be found in its previous edition from the year 1948. No other laws contained clauses about state monopoly. In spite of this information, in practise this monopoly existed.

Even today it can be said that transition to competitive Russian insurance market was not supported by adequate legal base, as insurance legislation was not a system of laws but merely a set of different regulations. Such regulations mostly contained norms for state insurance but not for private insurance business.

The third period started in 1988 when privately owned insurance company ASKO was introduced. When it became possible to establish privately owned insurance companies, there were suddenly more than two thousand of them. Many of the new companies were not established for the insurance business purposes but for personal purposes; e.g. tax avoidance,

quick wins (losses in insurance are always realised with a certain delay) and captives (insurers, which are daughter companies of a big firm active in other branches).

Due to missing real supervision and legislation, the business field was rather wild. Also the instability in the Russian economy and the political situation made it difficult for insurance companies to operate. The institutional framework was very confusing. The insurance business climate improved essentially when in January 2004 a new edition of the Law on Insurance was introduced.

A further reform step was taken when the system of the Russian Insurance Supervision was introduced in March 2004. The president of Russia established the new administration structure of the Insurance Supervision. One of the key ideas of the reform from insurance control point of view was to separate regulatory function (i.e. providing governmental policy by means of regulatory acts), from supervisory function (i.e. controlling of compliance of regulations and law by the companies). To fulfil the new idea of the Supervision, the function was transformed from the Department of Insurance Supervision of the Ministry of Finance to Federal Service of Insurance Supervision (Federalnaya Sluzhba Strahovogo Nadzora – FSSN). At the same time, regulatory functions remained within the Ministry of Finance and were transferred to the Department of Financial Policy.

Current investment regulations for insurance companies are valid since February 22, 1999, amended March 16, 2000 and August 18, 2003. Previous regulations were changed as a result of 1998 crisis, during which the Rouble exchange rate collapsed and the state defaulted her internal debt.

Investment regulations are valid only in respect of reserves (provisions). No regulations concerning capital investments do exist. Anyhow, the new version of the Law on Insurance gives the Supervisor the right to establish regulations in respect of capital.

Until January 2004, life and non-life insurance business in Russia could be run in one legal entity. Now the new Law of insurance established the needed requirement that life and non-life insurance business cannot be run within one legal entity. For companies possessing both licenses on January 17, 2004, the established law allows transitional period until July 1, 2007.

A new established insurance company faces new capital requirements, different for life and non-life companies. Any newly established life-insurance company must have MRUR 60 (1 USD  $\approx$  29 RUR) charter capital to get a license. Non-life insurance companies can start with

MRUR 30. Reinsurance companies or companies combining direct business with inward reinsurance should have MRUR 120 capital. For those companies that are already present in the market, the law allows gradual increase of capital.

On January 1, 2003 there were over 1200 registered insurance companies in Russia and over 30 reinsurance companies. According to the information of Ministry of Finance of Russia (Minfin) the total premium income was BRUR 432,4. Comparing to 2002 the growth was 44%. In 2002 the growth was only 8%. The share of the Top 20 insurance companies was about 50% of the total figure in 2003. The share of the Top 100 exceeded 77% in 2003.

The top 10 insurers have following features:

1. Five (5) of the top 10 are specialized in tax optimisation and are not involved in real insurance (life premiums over 80% and low marketing activities). Another two of the 10 have over 50% share of life business, which is also a sign of tax optimisation.
2. One company has the share of compulsory (medical) insurance in its portfolio of over 99%.
3. Only two companies (Reso-Garant and Ingostrakh) reached high figures due to real business success.
4. There are no captive companies in the Top 10 (Uralsib should be considered like a captive of Uralsib Financial group as this company has been already on the top 10 before Uralsib purchased it).
5. There are no foreign related companies in the Top 10.

In 2003 the share of Moscow-registered companies dropped down to 55% from 65% in 2002. The share of Moscow Area (Moskovskaya oblast) also decreased from 5,8% to 5,4%. So far foreign related insurance companies in Russia are not playing any significant role on the market. The biggest six companies (12 altogether) can be divided so that AIG Russ and ROSNO are the big ones and the remaining four (4) are middle-sized Russian insurance companies.

Despite of high growth rates of capital of the Russian insurance companies during several previous years, Russian insurers remain comparatively small financial institutions. For example, aggregate assets of the Top 100 Russian banks exceeded aggregate assets of the Top 100 insurers by 14,7 times. Aggregate assets of the Top 100 Russian insurers reached BRUR 288,4 (BUSD 9,4) and net assets BRUR 281,1 (BUSD 9,16). The largest companies by assets are SSO with BRUR 30,6 (growth 29,3%), Rossgostrakh (Group) with BRUR 30,5 (growth 440%), Ingostrakh with BRUR 19,1, Capital-Strakhovaniye with BRUR 16,4 and RESO-Garantiya with BRUR 13,1. Net assets of the Top 10 insurers reached BRUR 153,7.

According to an Interfax study, 135 largest insurers' share of equity capital in total assets of insurance companies increased from 21,1% in 2002 to 22,7% in 2003 and reached BRUR 2,16 (generally the growth of equity capital of insurers decelerated in 2003).

In 2003 the changes in the Russian insurance market continued. Captives actively came to the open market. Major Russian insurers continued to decrease their shares of tax avoidance life insurance and to increase the share of real insurance including real classic life insurance.

The share of voluntary insurance continued to decrease – 79,4% in 2002, 76,2% in 2003. The share of the personal insurance lines also decreased from 10,7% in 2002 to 9,6% in 2003, property insurance from 30% in 2002 to 29,1% in 2003, and liability insurance lines from 4,1% in 2002 to 3% in 2003. The share of life insurance decreased insignificantly from 34,6% in 2002 to 34,5% in 2003.

The share of compulsory insurance lines increased from 20,6% to 23,8%. It is important to notice that the share of compulsory medical insurance decreased from 19,6% in 2002 to only 17% in 2003.

The post-Soviet Russia is an emerging market with a living standard of about one third of the level in the western Europe calculated on the basis of GDP per capita in Euros, purchasing power parity (PPP) adjusted. Insurance business is, therefore, on an entirely different level in Russia in comparison to West-European countries. In Finland, for example, insurance premiums per annum and per capita are about thirty times higher than in Russia. United Kingdom is even further ahead of Russia in the same calculation.

Income is very unevenly distributed in the transitional Russia. In the framework of rapid privatisation, a new class of extremely wealthy persons, called oligarchs, came into being. This group dominates basic industries, including extractive activities. On the other side of the scale, about 25–30% of the population lives below the calculated subsistence level. Obviously, this part of population has no discretionary income to spend on insurance policies.

Geographical distribution of income is also very uneven. People living in Moscow earn about four times per capita compared with national average. Thus, it is not surprising that Moscow is an undisputed centre of the insurance business in Russia. The second metropolis, St. Petersburg, has also over average living standard, but on per capita terms it is clearly lower than in the capital city.

In Western system, insurance industry is monitored strictly by authorities, which take both policyholders and insurers interest into account. In Russia, this system of supervision is still developing, but not yet perfect.

One of the essential features of the recent insurance branch reforms is enhanced capital requirement level introduced in 2004. It is not yet clear whether Russian insurance companies will be able to bear the risks they take with the required higher capital base.

Reinsurance schemes and support of international reinsurance companies is essential to Russian insurance industry. Reinsurance arrangements between Russian direct insurers are not always very reliable. Reinvestment business is under reconstruction.

In the industrial revolutions of the Western countries, insurance companies have been an essential tool in capital formation. Obviously, this role is reserved to these financial institutions also in transitional Russia. About 60% of investment done by insurance companies goes to enterprise sector: enterprise bonds and shares can be found in insurers portfolios. In this context it is worth underlining that securities markets in Russia have a very limited scope. However, local markets are supposed to be favoured. There are rules concerning investment activity. Profits cannot be maximized by international operations when Russian insurers make their investment decisions.

The state defaulted her internal debt amid the 1998 crisis, which caused substantial losses to insurers. In the post-crisis era, government bond are finding their way to insurers portfolios again.

The involvement of foreign companies in the Russian insurance market has so far been very thin. The overall share in this branch's total assets in foreign hand is limited, first to 10%, and later on, to 20%. These ceilings have no practical importance, because the stakes of foreign capital remain permanently on a low level.

In this context it is appropriate to remark that many Russian citizens are not familiar with the insurance philosophy of the Western world. Thus, the private household sector is hardly regarded as part of the insurance clientele. However, introduction of compulsory insurance schemes is changing the scene.

The new Compulsory Motor Third Party Liability (CMTPL) Insurance, introduced in 2003, is one of the biggest and most important events in Russian insurance industry. The private

persons are in a way “forced” to learn insurance and its philosophy. A big file of personal particulars will be put together due to this compulsory insurance line. This data is now available to exploit marketing purposes for other insurance products targeting.

Insurance product development has been very exciting during the past years and now the situation is such that almost all needed insurance products are available (this is of course related to Russian business environment) to finance business risks in Russia if decided to have insurance for risk financing.

Insurance companies’ personnel and company management level is good standard in Russia. The past fifteen years has educated in theory and practise a new generation into Russian insurance industry. Very often education of the people has even been completed in foreign countries’ insurance companies and universities.

Big Western companies are interested mainly in big industrial risks and reinsurance arrangements. Obviously, the Russian state is reluctant to allow monetary outflow in the reinsurance business. Too strict rules may cause critical situations in which risks taken cannot be covered. Thus, a constructive compromise is optimal solution.

It is expected that at least half of insurance companies existing on January 1, 2004 will not cope with new capital requirements and gradually disappear during the period July 2004–July 2007. Expansion of foreign insurers in Russia is not clearly in sight. The main reason is that they are able and eager to concentrate only on huge industrial risks.

Russia is a huge country and insurance is a mass product. Russian insurance companies’ challenge is to create functioning distribution channels to reach potential clients cost effectively. Thus, a consolidation of the branch is needed. It can be assumed that in the near future an acquisition wave will take place.

Reinsurance requirements in Russian insurance industry continue to stay in a very important role in the nearest future. Local primary insurers are not able to carry big risks without rather massive reinsurance support from abroad. Therefore, no isolation of Russia from the international network can be expected.

## 1. Introduction

The economic development in the 20<sup>th</sup> century Russia was extremely colourful. In the early period of that century, Russia experienced a boom, which was interrupted by the World War One. Amid this conflict Russian monarchy was dismantled and replaced by the communist rule in 1917. After the Bolshevik revolution a bloody civil war broke out.

During the Russian civil war strict control in the economy with tight rationing of everything was introduced. This period is called war communism in the economic history.

After the communist victory in this conflict, the Soviet State was established. In the early period of soviet power, a rather liberal mixed economic system called NEP (New Economic Policy) was launched.

This highly interesting NEP-system with many market elements was replaced with a highly controlled management system in the late 1920's. Private property and personal initiative were prohibited with the aim to industrialise the huge country in shortest possible timeframe by the state. An investment boom based on forced savings took place in the era of Stalinism. Millions of people were executed and others perished. However, remarkable structural changes were achieved.

The strict control of planning introduced by Josef Stalin relied heavily on coercion and terror. The controlled allocation of resources favoured production of inputs (especially machines and factory buildings). Production of foodstuffs and consumer goods had a secondary importance only.

After the death of Stalin (1953) several economic reform models were created and some experiments took place. However, the system was incapable to prepare itself for a post-industrial era of intensive economic growth based on innovation and productivity increase. Amid conservative political atmosphere of one-party rule, period of stagnation took place. This term is used when the 1970's is scrutinized in Soviet economic history.

In the mid-1980's, a relatively young person, Mikhail Gorbachev, was selected to top of the communist superpower. Very soon this new type of leader launched an open discussion on socio-economic affairs. The intellectual climate in the Soviet Union and in her satellite states changed radically. Suddenly, discussion on mixed economy with market elements was

allowed. Thus, the second half of 1980's was extremely interesting period of reform thinking and experiments.

In the hindsight, it can be stated that economic reforms and the Soviet Union came too late and too slowly. The traditional system of central planning contained terrible waste impeding further development of general living standard. A system, in which the central authorities are responsible for resource allocation without any incentive in the enterprise sector to save inputs, cannot be optimal from the point of view of value creation.

In the last years of Soviet power, the aggravation of the so-called monetary overhang problem took place. Monetary income of the population increased continuously, while the supply of consumer goods and services stagnated or even decreased. As a result, more and more people were forced to save a big part of the earned income. The accumulated amount of forced savings (money one could not use for anything) is called monetary overhang.

The reform of Gorbachev era aimed at increasing productivity. This aim was supposed to be achieved by improving material incentives (higher pay). From the point of view of average consumer, it made very little sense to earn supplementary money without any options to use it for purchases of needed goods and services.

The Soviet economic history teaches us that amid permanent supply bottlenecks virtually everything was available. This economic miracle was achieved via a double system: the official (planned) economy with fixed prices was not able to satisfy the overall demand, but plenty of supplies were available in the black market. In the latter, prices were formed on the basis of supply and demand.

Under those circumstances of late communism, profiteering and corruption were rampant. Both of them were supposed to be eliminated by definition in the communist system.

It is not possible to cover all details of the communist central planning and its consequences here. It suffices to say that general dissatisfaction concerning difficulties in everyday life was the main cause of collapse of the communist system. This historical event took place in two waves: in 1989, countries of the Eastern bloc abandoned the system of central planning combined with the undemocratic system of one-party rule; the same occurred in the Soviet Union in 1991.

The collapse of the Soviet Union had enormous political consequences. All 15 republics of the former Union became independent states. Twelve of these states joined The Commonwealth of the Independent States (CIS), which was established in 1991 with no supranational powers.

Russia is far the largest former Soviet republic with a population of about 145 million people and a territory of over 17 million square kilometres. Thus, the Russian Federation is the largest country in the world (in area) with a vast resource base containing almost all minerals and a huge magnitude of forests and agricultural soil.

Thus, Russia has excellent preconditions for economic success in her transitional period. Especially important natural resource is oil that is exported in large quantities. Natural gas deposits are also plentiful in Russia.

The early period of Russian transition was extremely difficult. The quantity of economic activity (measured in gross domestic product or GDP figures) decreased by about 40% in the 1990s.

The systemic change caused a strong inflationary wave when the centrally fixed price system was abandoned. Capital flight took place in massive scale. Rapid privatisation of state owned assets created huge differences in wealth and income.

In 1997, it was anticipated that the post-Soviet wave of price increases was over. A new system of exchange rate policy was established in which a central rouble-dollar rate was fixed with +/- 15% borderlines (around the central rate) giving leeway for market fluctuations. This system of managed floating came into force at the beginning of 1998.

In that time, the state borrowed heavily on the national and also international bond market paying very high real interest. Therefore, inflationary expectations were high. In August, the same year, a run against rouble started. The Central Bank of Russia was unable to defend the set borderline of 15% depreciation (of rouble). The market demanded more and more dollars against the local currency. The monetary authorities with rather low currency reserves were unable to defend the fixed borderline (-15%). Rouble depreciated strongly when the managed floating system was abandoned.

This rouble crisis caused a strong inflationary wave in 1999. Average income calculated in dollars / euros declined considerably (for details, see: T. Tiusanen: Development of the

Russian Rouble – The Crisis of 1998 and its aftermath, Northern Dimension Research Centre publication 3, 2003).

In the turn of the century, the price of oil, the main exportable of Russia, increased essentially. At the same time, the new (realistic) rouble-dollar exchange rate gave a remarkable incentive for import substituting activities. These two factors started a boom in investment, which had declined during the early transitional period.

In the post-crisis (of 1998) period, the overall economy and real investment have grown rapidly in Russia. Amid this positive development, average income of the population has recovered remarkably rapidly. Growth prospects have improved fundamentally in comparison to the 1990s.

Obviously, there are winners and losers in the Russian transitional process. Poverty is a serious problem. There are some extremely rich individuals but some 25% of the population live under the poverty line. Moscow is about four times better off than Russia in average. Life expectancy, especially for male persons, is low in international comparison.

In the Soviet period, the state (via the monopoly power of the communist party) ran the entire economy. Under these circumstances, there was hardly any need for traditional insurance business. However, certain activities in this sphere were in existence in the communist era. A short overview on this era is included in this study.

In the first half of the 1990s, the number of insurance companies exploded. Rules governing the insurance business in Russia were rather unclear. Tax avoidance seemed to be an important background factor in the insurance boom of the early period of Russian post-communism.

This short study of the Russian insurance market in the 21<sup>st</sup> century shows how a clear consolidation process with participation of Western companies is under way. The legal framework shows improvement. The insurance branch development reflects the positive trend in the overall economy. Evidence provided here indicates that the Russian insurance market is far away from saturation. Thus, the long-term prospects in the branch under review are excellent in the large market of post-communist Russia.

## 2. General aspects of Insurance Industry

There are certain basic properties in insurance industry, which are valid everywhere in the world like risk carriers (premiums written, premiums earned, claims incurred, operating expenses, investment income, solvency, solvency margin, solvency capital).

Insurance companies can be classified in two main categories, non-life and life insurance companies due to the different character of their business.

### 2.1. Insurance market generally

Insurance is a rather obscure article. Insurance premium is paid before the product (insurance coverage) is delivered to a client. Basically the price of insurance is always a prediction and the final price will take shape during the years.

Insurance industry is closely connected to the general economic situation. When the economy is growing, the insurance industry is developing well due to e.g. industrial investments, new jobs, and increased salaries. General welfare of a country is feeding the need of new insurances in all fields: property and casualty insurances, life insurances as well as deposit insurances.

The development of the insurance branch is cyclical: in a booming economy insurance business goes up and in a slump it goes down. Insurance industry follows the general business cycle with one or two year's delay.

Long-term effects to the insurance industry are changes in population and risks. When insurance industry's growth prospects are assessed, the method to calculate insurance premium income as a percentage of GDP is often used internationally.

Insurance companies operate as risk carriers. When we assess and analyse an insurance company according to its loss and profit account as a risk carrier, the following principles are considered.

#### *Premiums written*

This figure shows how much a company has written insurance premiums during the period (~ turnover).

*Premiums earned*

The real premium earnings from insurance policies sold in the previous period.

*Claims incurred*

This is a sum how much claims an insurance company has paid during the period under consideration.

*Loss ratio*

The proportion of claims paid or payable to premiums earned

*Operating expenses*

Cover running and fixed costs.

*Expense ratio*

The ratio between premiums earned and expenses to run the business (in per cent).

*Combined ratio*

The ratio between premiums earned and overall expenditure. This is the figure that shows the effectiveness of the insurance company to run their pure insurance business. Very often this figure in insurance companies is above 100%. That means that more money is going out than coming in.

*Investment income*

Insurance companies collect premiums from the market and invest the money to different profit or interest bringing investment instruments. This makes it possible that insurance companies may make a profit, even if the combined ratio is above 100%.

*Reinsurance structure of a company*

A Reinsurance program is a risk portfolio that a company transfers to other risk carriers by paying a fee for this service. Reinsurance structure of a company provides important information in assessing it as a risk carrier (who are the reinsurers, what size of the treaties the company has, how do they manage in facultative reinsurance)

*Solvency – solvency margin, solvency capital*

The extent, to which the realisable assets of an insurance company exceed its liabilities. Solvency is the capital from where losses will be covered. It consists of the following parts:

own capital, reserves, under valuation of assets and equalization reserve. Solvency capital and solvency ratio of the insurance company are decisive indicators in ranking the company and to evaluate its capability to carry the risks.

#### *Capital and reserves / share*

Every insurance company has her own capital. Reserves are for the open claims during the period that have not been completed. In analysing a non-life insurance company's result and financial position it is appropriate to concentrate to loss and profit account's details, which explain how actual business is conducted.

In case of a life insurance company, the situation is more complicated due to the lack of international methods to analyse the results and company's financial position. Differences in practise between countries are bigger than in non-life companies.

## **2.2. Distribution channels**

Insurance is a mass product especially when we deal with the private household business segment. This statement is valid for all insurance lines: non-life and life insurance as well as deposit products.

In many ways it is critical for an insurance company's success to organize and manage its sales effectively. Premiums written, operating expenses, combined ratio and other key figures of a company relate to its sales and distribution channels and how effectively they work.

Widely used distribution channels in insurance industry are own personnel, sales offices, insurance agents, and insurance brokers, direct marketing and cooperation partners, call centres and Internet. As far as the private household segment is concerned, the most used channels are direct marketing, agents, telesales and insurance brokers. In the corporate insurance segment own personnel and insurance brokers are the most popular marketing channels. Especially insurance brokers' importance increases annually.

### **3. General Features of the Russian Insurance Industry**

#### **3.1. Historical Background of Russian Insurance Market**

Insurance appeared in the Russian market later than in major West-European countries. Russian insurance (with respect to both joint stock insurance companies and mutual insurance companies) is peculiar in the sense that, unlike in Western Europe where it was initiated by trade and industrial circles, in Russia it grew from bottom to top frequently under pressure from the government. This is true first and foremost for fire insurance, one of the most important types of insurance in Russia.

The first Russian insurance company was so-called Insurance Expedition established in 1786 under the State Loan Bank “for insurance of stone mansions, plants and factories”. The bank’s prior objective was to extend to noblemen and city residents long-term mortgage loans secured by real estate purchased with the proceeds of such loans. The Edict On Establishment of the State Loan Bank issued by the Empress Catharine II on June 28, 1786. The Edict demanded that prior to extending loans the bank should insure the buildings used as security. To attain this objective, a subsequent edict dated December 23, 1786, ordered that the Insurance Expedition to be established. According to the edict the insured value of the building was legislatively set at the same level as its collateral value. This amounted to  $\frac{3}{4}$  of the assessed value, so that owners, “without being tempted with being paid for the properties, even reduced to ashes, would take greater care to preserve their buildings”.

The 1786 edicts also introduced state monopoly on insurance operations, as it was prohibited “to have dwelling houses and factories insured by foreign countries, thus inflicting monetary losses upon the Russian State”. At the same time, this monopoly was not an absolute one. According to the Edict of December 24, 1786 those persons who dared to use foreign insurers could be deprived of the protection and pay a fine of 1,5% of the insured amount – which was the amount of the insurance premium paid when property was insured by the Insurance Expedition. In fact already in 1798 Russian nobles were allowed to insure their property abroad.

For the next four decades the results of insurance development in Russia were not impressive: some mutual companies started operating in Riga, while several governmental projects failed (like insurance company for ships and cargos, declared but never really established) and Insurance Expedition (MRUR 1,2 premiums and RUR 170.000 claims paid within 1787–

1822, 95 insured valid policies in 1822). Foreign insurers met the noticed demand and need for fire insurance in Russia. One of the most active ones was representative office of British company Phoenix 9est from London. The representative office was opened in St.Petersburg in 1782.

The presence of foreign insurers caused massive outflow of cash, which forced the government to encourage development of domestic insurance companies. On June 22, 1827 Emperor Nicholas I approved the charter of the first joint stock insurance company – Russian Fire Insurance Society. The government granted significant privileges to the company – 20 years monopoly to insure risks in St.Petersburg, Moscow, the Baltic States and in Odessa where most of stone buildings were located. For the same period the company was exempted from all taxes except a small duty on written policies RUR 0,25 per each RUR 1.000 of the insured amount. The company issued the first policy on October 14, 1827. During the 20 years of monopoly the company issued over 500.000 policies. 70% of premiums were collected in St.Petersburg.

Commercial success of Russian Fire Insurance Society encouraged the establishment of more joint stock insurance companies. The Second Russian Fire Insurance Society commenced its operations in 1835, receiving 12-years privilege in 40 provinces lying outside of the area of operations of the Russian Fire Insurance Society. Several (not only fire) insurance companies were established in the 1840s.

In 1847 the privileges that were given to Russian Fire Insurance Society and Second Russian Fire Insurance Society expired and the age of free competition started. Dozens of new companies appeared in the 1850s and 1870s, mostly specializing in fire insurance.

A price war in insurance became the main method of competition. In 1875 eight major insurers created so-called insurance syndicate implementing an agreed tariff policy. Later on, all Russian joint stock fire insurers joined to the syndicate. In 1881 Russian insurance company with a huge chartered capital and aggressive policy was established.

After several bankruptcies of minor insurers, the government decided to set the first insurance supervisory – the Insurance Committee – in 1894. The supervisor had the right to approve charters of insurance companies, insurance policies' terms and conditions, life insurance plans as well as approval of reporting and balance sheets and auditing of insurers.

In the early 20<sup>th</sup> century the Russian Fire Insurance Society still maintained the leading position in the Russian insurance market. In 1896 it expanded the range of operations and became involved in vehicle and accident insurance. Amid this development, the name of the company was changed to First Russian Insurance Company.

On November 24, 1900 disastrous fire destroyed Moore and Marylise department store in Moscow. The fire continued 2 days and resulted in MRUR 1,7 losses. Nevertheless, this did not affect the strong financial position of the First Russian Insurance Company who indemnified the loss.

On the eve of World War I, Russia had 19 active joint stock insurance companies with an aggregate capital of MRUR 48 and total assets about MRUR 300 (amount is comparable to 1/10 of the entire national budget). In the early 20<sup>th</sup> century, Russia held the second place in the world by total value of fire insurance premiums collected, while its position by total volume of insurance business was consistent with its share in global industrial production.

In the year 1918 Soviet Government nationalized all Russian private insurance companies and created state monopoly for insurance industry. This period of communist rule lasted about 70 years.

Gosstrakh of USSR and Department of Gosstrakh for foreign operations were established in 1925. This department became a separate unit (Ingosstrakh Insurance Company) in 1947. Until 1988 Gosstrakh remained the only domestic insurance service provider and Ingosstrakh was the only Soviet insurance representative on international insurance market.

Not earlier than 1988 the first alternative insurance company ASKO was created and allowed in the form of a co-operative.

### **3.2. Insurance Companies Ingosstrakh and Gosstrakh**

Ingosstrakh was established as a department of foreign insurance of USSR November 16, 1947. It was created on the basis of relevant department of Gosstrakh. Ingosstrakh started operations in 1948. The first lines were marine cargo, marine hull, fire insurance, liability insurance and reinsurance. The first rep office was opened in Finland in 1952. Other rep offices: Pakistan (1953), Egypt (1954), Afghanistan (1955), Algeria (1963), Mali (1963), and Cuba (1971).

Ingosstrakh's British subsidiary, Black Sea Baltic Insurance Company, opened its offices in France, Egypt, Syria, Lebanon and Sudan. In 1958, Garant Company (in Austria) was created. In 1967, Soviet-Indian insurance bureau in Bombay was established. In 1972, Ingosstrakh's status changed. Remaining as a part of the state structure, it received the right to act as a joint stock company. In the 70s, Ingosstrakh extended its operations to marine liability, engineering and aviation and in the late 80s operations were further extended to aerospace, credit insurance and professional liability.

In the early period of Soviet power, following decrees were published: March 23 in 1918 Decree on State Control over Insurance (except social insurance) and November 28, 1918 Decree on Organization of Insurance in Russian Republic. As result of these Decrees, insurance became state monopoly. All private insurers were liquidated and their property ceded to government. Practically there were no insurance companies present at that time. Life insurance in the USSR was cancelled in 1919. State property insurance was cancelled in 1920 and replaced by direct governmental payments to persons who suffered from acts of nature. Policy changed from War Communism to NEP, New Economic Policy.

On October 6, 1921 Decree On State Property Insurance was issued. Russian state insurance organization was created. Insurance Administration of Russia (Gosstrakh) was formed within Narkomfin (Ministry of Finance). Regional network was created. State property insurance for private enterprises covered following risks: fire, agricultural and transport risks. In 1922 Gosstrakh was authorized to perform life and accident insurance, as well as fire insurance for peasants' property. In 1925, compulsory insurance of state property rented by individuals and co-operatives was introduced.

In the Soviet industrialization period's initial stage (late 1920s–1931), compulsory property insurance of state enterprises and co-operatives were introduced. Insurance of state enterprises was practically cancelled. Mutual co-operative insurance and voluntary insurance of peasants' property were cancelled. Long-term life insurance was prohibited. Insurance authorities were liquidated, and their functions transferred to financial authorities.

In 1933, the insurance system was restored. Life insurance, voluntary property insurance for individuals, co-operatives and other organizations were allowed. Compulsory insurance was extended to state residential buildings. In 1936, the network of insurance agents was created.

Personal lines insurance growth in the USSR was as follows: at the end of 1945 there were 1,8 million policyholders and in 1953 5,9 million.

Until 1990 there were 3 forms of property in the USSR: state, co-operative and individual. Compulsory insurance covered the following types of state property:

- Sovhoz (state agricultural enterprise) since 1979
- State property leased out (since 1925)

All other losses to state property were covered from governmental reserve funds. The reason for such limited application of insurance was that Gosstrakh was a governmental body, and thus, every insurance could actually be considered as self-insurance.

Compulsory insurance of state agricultural enterprises was introduced as such insurance showed its effectiveness in respect of co-operative farms (kolhoz). State enterprises did not have the right for voluntary property insurance until 1988. Total value of the property of such enterprises reached BRUR 2.000 (1990) but only 5.000 policies were issued in respect of this property (1990) resulting in only MRUR 28,6 premiums. In 1990, total insurance premium figure in USSR (except Lithuania) was BRUR 20. Insurance penetration was 2,2%. There were 205 million policies valid, including 85 million life insurance policies<sup>1</sup>.

### **3.3. Development of Insurance Legislation and Products**

During the years 1918–1990 the Insurance legislation in the USSR was extremely limited by the needs of state monopolists. There was no basic law on insurance. Only a few regulations concerning relations of insurers and certain categories of the policyholders existed.

In 1991 the Supreme Soviet of USSR adopted The Basics of Civil Law of USSR containing the following aspects of insurance: objects of insurance, subjects of insurance, general obligations of the insurer and the insured.

Compulsory and statutory insurance was exclusively granted to state-owned insurance companies. Only written form of insurance contract was allowed. Subrogation and right of recourse in insurance was introduced. Specific insurance law was substituted by acts of government exempting compulsory insurance that was regulated by acts of the Supreme Soviet.

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<sup>1</sup> All data V.A. Sukhov, Russian Insurance Market, 1992

According to the act of Soviet Government, adopted in 1958, State Insurance was submitted to Ministers of Finance of the republics (USSR contained 15 republics) and a standard bylaw of State Insurance Agency was approved. According to these regulations the system of state insurance was centralised within each republic. Central Board of State Insurance of the Ministry of Finance of the USSR was responsible for methodology and co-ordination of 15 republican Insurance bodies. The board was in charge of preparing of terms and conditions for each and every line of insurance.

In the year 1992, when The Soviet Union did not exist anymore and The Russian Federation had become an independent state, the Law on Insurance appeared. The law was supplemented with following acts: taxation of insurance operations (Law in 1991), on Insurance supervision (decree of president 1992 / related to controlling the insurance industry), on creation of Russian State Insurance Company “Rosgosstrakh” (decree of president, 1992 / related to definition of Rossgostrakh’s position).

Usually it is stated that the Law on Co-operatives abolished the Russian State insurance monopoly in 1988. As a matter of fact, in 1958 a new bylaw on State insurance dismantled the monopoly created in 1948. No other laws contained clauses about state monopoly.

Even today it can be said that transition to competitive Russian insurance market was not supported by adequate legal base, as insurance legislation was not a system of laws but just a set of different regulations. Such regulations mostly contained norms for state insurance but not for private insurance business.

During the years 1991–2003 Russian policyholders and insurers experienced severe difficulties partly due to very limited solvency demands set for insurance services.

Compulsory insurance of separate buildings was established in 1940. A law allowing voluntary insurance of buildings was published in 1956. In 1967, compulsory agricultural insurance was introduced for co-operative farms (kolhoz). In 1978, such insurance became compulsory also for state farms. The system was cancelled not earlier than in 1991 by adoption of the Law on Co-operatives. In the 1960–70s new products came into being: life insurance for legitimate children, new conditions for property and motor insurance. In 1972, new life insurance conditions were published. In 1977, marriage insurance was started. Compulsory insurance for certain types of property of individuals (private houses) was introduced in 1981. In 1982, regulations concerning voluntary insurance of individuals’ property were adopted. Agricultural insurance was reformed in 1979–1984.

Since 1982, the development of Russian Insurance Industry has been continuous: compulsory insurance of passengers of air, motor, sea and river transport appeared in 1982. Regulations for voluntary personal insurance were issued in 1982. children's accident insurance was introduced in 1986–87. In 1987, regulations for voluntary (additional) pension insurance were published. Before that there was no possibility to increase private person's pension accumulation. The Soviet system was not aware of pension funds or any other system. The one and only pension system was the state practise. Compulsory personal insurance for military personnel was put into force. In 1991, the Law on medical insurance was adopted.

### **3.4. Insurance Regulation and Supervision**

In 1992, the first post-Soviet specialized insurance regulatory body was established and named Gosstrakhnadzor. Later this body was renamed to Federal Inspection of Insurance Supervision. In 1993, after the introduction of the Law on Insurance, the name of the body was changed to Federal Service of Insurance Supervision (Rosstrakhnadzor). In 1996, Rosstrakhnadzor lost its independence. It started to operate as Department of Insurance Supervision of the Ministry of Finance, which performed the supervision until May 2004.

Initially Supervision authority was only able to issue licenses, regulations, collect reports and send prescriptions to insurance companies. The Supervision staff was neither experienced insurance professionals nor numerous enough to follow the real situation, in which a huge number of insurance companies operate across Russia.

Creation of Regional Supervision Offices started in 1993. For many years, their activities could hardly be observed on local districts and markets. In 2002, there were 11 local offices of Insurance Supervision (St.Petersburg, Khabarovsk, Rostov, Samara, Yekaterinburg, Novosibirsk, Krasnoyarsk, Vladivostok, Tatarstan Republic, Bashkortostan Republic, and Udmurt Republic). Total number of personnel in Supervision reached 189, including 99 employees in the headquarters and 90 in the regional offices. Competence of Russian Insurance Supervision was specified in The Civil Code of Russia, Law on Organization of Insurance Activities in Russia, decisions of Government and other legal acts.

The aim of Insurance Supervision was (still is) to take care of the enforcement of insurance legislation, protection of rights of policyholders, of insurers and of other parties involved in insurance (including state itself).

The major functions of Insurance Supervision are the following:

- Checking fulfilment of insurance legislation by means of current, planned and operative supervision on the territory of Russia;
- Licensing of insurance activities;
- Issuance of rules of creation and investments of insurance reserves, rules for creation reports;
- Checking solvency of insurance companies;
- Providing measures for elimination of violations of insurance legislation;
- Development of regulations in respect of insurance activities;
- Analysis of insurance activities and working out suggestions on improvement of insurance legislation ;
- Updating State Register of Insurers and State register of Insurance Brokers.

In practice, one of the most important tasks of the supervisor is to fight against tax optimisation schemes, money laundering and illegal export of capital from Russia via insurance companies.

Tax optimisation schemes in the insurance sector came into being as a result of progressive income tax and high social security payments as a part of the gross wage paid by employers helping them to evade compulsory payments. So-called life insurance deals per one month were concluded, which were nothing else but an indirect way of wage payment. Via this trick, the employee received his/her agreed upon net pay, by which the employers saved money in compulsory payments (part of the gross wage).

In the turn of the century, the state introduced a flat personal income tax rate of 13%. At the same time employers' social security payments were reduced, and thus, incentives to use tax optimisation schemes via insurers became less important.

Obviously, the insurance supervision in Russia has had and still has a vital interest in rooting out all methods of tax evasion schemes in the insurance sector. Furthermore, it is the interest of the state to supervise the insurance branch in the sphere of capital flight. The state is naturally aiming at improvement in these contexts by modifying the institutional framework.

### **3.5. Insurance Companies in Russia**

As mentioned above, the number of insurance companies rocketed sky-high in early 90's.

Many branches that previously were prohibited expanded rapidly, when the market was introduced. Very often the insurance business was started without real understanding of its principles. Anyhow, there was a strong belief that it is possible to make successful business in

banking, insurance or in trading. Entrance barriers to the market were almost missing: licensing procedures were mainly formal, supervision was absent or only formal, big competitors were often missing. The biggest competitors were former state companies, not flexible enough to be real competitors in a rapidly changing environment.

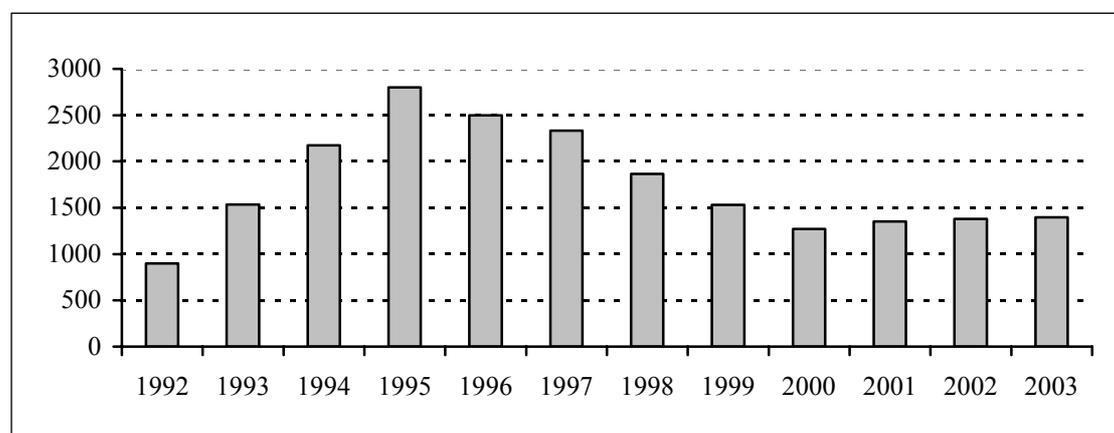
Because the capital requirements for insurance companies were extremely low, numerous insurance companies were established just for tax optimisation and money laundering purposes. A good reason for establishing an insurance company was the visible profitability of such business, as claims followed premiums with a certain delay.

All insurance companies can be divided into following groups:

1. Former State owned insurance companies – Rosgosstrakh and Ingosstrakh including their regional subsidiaries;
2. Newly established independent insurance companies;  
They can be divided into two subgroups: market oriented companies (minor group) and money laundering / tax optimisation companies;
3. Captive insurance companies of financial and industrial holdings (mostly banks and oil / gas industry);
4. Subsidiaries of foreign insurance companies (less than 10).

It is important to notice that tax avoidance schemes were crucially important for insurance companies, often giving them the only possibility to survive in the early period of transition. It was hardly possible to find any (even big and well-known) company in the 90s, which was not involved in such operations. Even now the distinction can be made between those who play this game as a supplementary activity for ordinary insurance business and those who were established only for money laundering and tax avoidance without any intention to provide real insurance services.

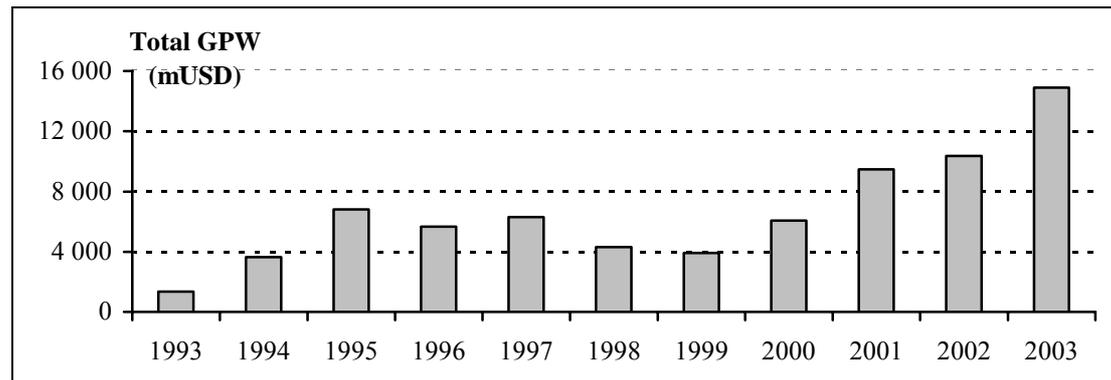
**Table 1**      **Number of insurance companies in Russia**



(Source: Ministry of Finance)

It can be seen from the table 1 that the number of insurance companies has stabilized in the last four years. The number of newcomers and companies leaving the industry was not as high as in previous years. In 2001, the Supervisor recalled only 38 licenses. In 1998–2000, the equivalent number was fluctuating between 350 and 500. In 2003, the Supervisor recalled 105 licenses and temporarily stopped the validity of 136 licenses.

**Table 2 Total insurance premiums (Gross Premium Written)**



(Source: Swiss Re Sigma 1993–2001, Ministry of Finance)

Insurance premium development has been positive, but uneven. As shown in table 2, the trend increased rapidly in the early period of transition. However, a decrease took place in 1996, but the following year showed growth again. In 1998, Russia established a new exchange rate regime of managed floating. In this system, the central rate was fixed on RUR 6,2 = USD 1. Market fluctuations were not supposed to exceed the borderlines from +15% to -15% around the fixed central rate. However, in the summer of the same year it became obvious that the central rate was not on the right level: Rouble was too strong. Thus, the market started a run for dollars. The Central Bank of Russia with rather low currency reserves was unable to defend the set borderline of -15% (about RUR 7 = USD 1). After giving up the managed floating system, the monetary authorities had to witness a rapid and strong devaluation of the RUR. Within 12 months, the price of one US dollar (in Rouble terms) increased about fourfold.

Decrease of premiums written in 1998–1999 reflects the devaluation crisis in August 1998. Russian Rouble's (RUR) exchange rate jumped from about 6 RUR/USD to 9,75 as an average for 1998 and 24,68 as an average for 1999.

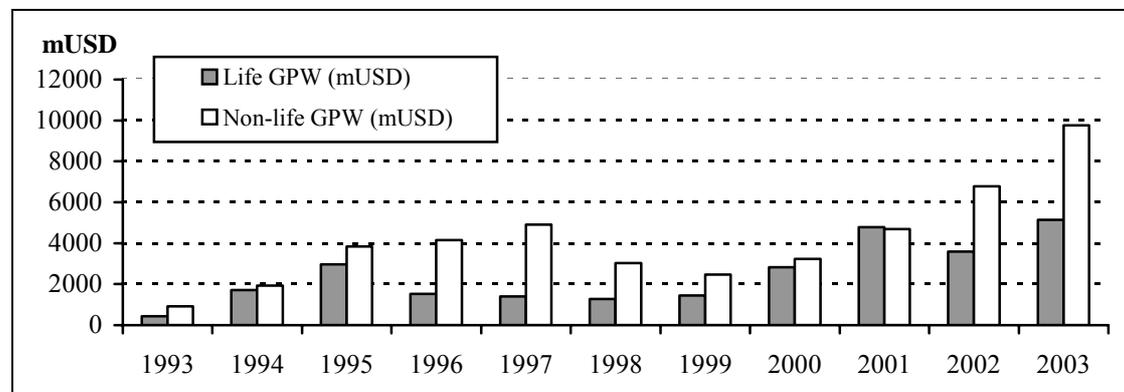
In addition, insurance companies suffered strongly due to regulations concerning the placement of insurance reserves issued by the Supervisor. According to these regulations,

insurance companies had to place not less than 10% of their insurance reserves to Governmental Bonds.

Amid the devaluation crises, the government defaulted her internal debt. Thus, all bondholders (natural and juridical persons) suffered considerable financial losses.

If the Russian economy in the late 1990s is analysed in the light of statistics, different results may come up. Different sources show different results in USD for 1998 as some companies used average rate and the other ones the rate at the end of the year for conversion of official statistics from RUR to USD.

**Table 3 Life and non-life insurance premiums 1993–2003 (MUSD)**



(Source: Swiss Re Sigma 1993–2001, Ministry of Finance)

Table 3 shows two trends in the insurance business: life and non-life. The life insurance development was very dynamic in the early years of the transition, but experienced a very clear drop in 1996. This business remained on a rather low level in 1996–1999. This trend obviously cannot be explained by the Rouble devaluation crisis alone.

As mentioned earlier, life insurance numbers are mostly representing activities in the field of tax avoidance. Thus, the decrease of life business in some years is mostly resulting from Russian Government's efforts in fighting such schemes or liberal changes in legislation making some of avoidance decisions obsolete. Before the year 1995, there was hardly any insurance company who seriously tried to concentrate on real life insurance business (pure life assurance, long-term investment insurance). Thus, the slump in the pre-crisis period has special background factors.

In 1995, European Bank of Reconstruction and Development (EBRD), Scottish Provident and some British investment funds established Insurance Company Principal. Their aim was to

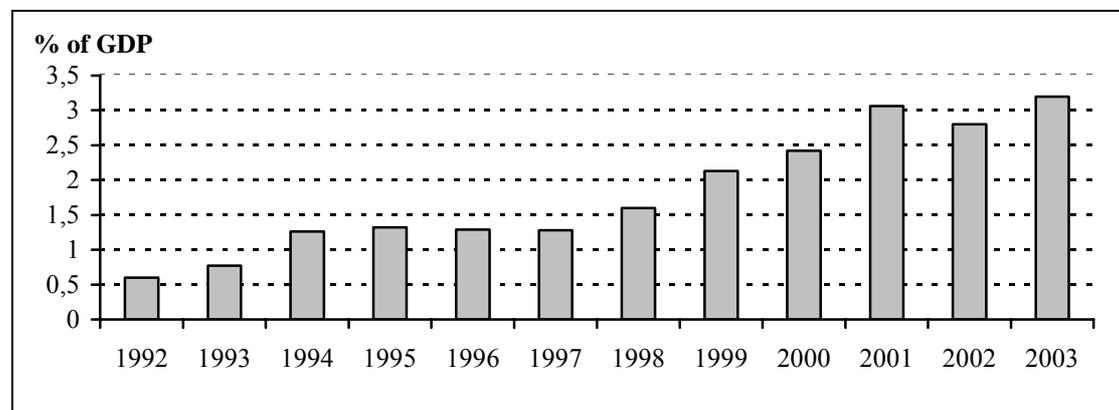
start and develop real life insurance business in Russia. Unfortunately, they failed (details below).

In the aftermath of the Rouble crisis, a very rapid recovery has taken place. The most important background factor has been the oil price that increased strongly in 2000. The devaluation of the Rouble created preconditions for investment in import-substituting branches. In the turn of the century, political stability has improved essentially.

Thus, the investment climate has become more favourable. It is not surprising that Western insurance companies (AIG<sup>2</sup> Russ, ROSNO) have shown increasing interest in the Russian market.

Obviously, the Russian market has enormous potential from the point of view of international insurance companies. This fact can be illustrated in the light of some comparative key figures. There are two parameters used for comparative analysis of insurance markets: insurance penetration (insurance premiums as % of GDP) and insurance density (insurance premiums per capita).

**Table 4 Russian insurance penetration 1992–2003 (insurance premiums, % of GDP)**



(Source: Swiss Re Sigma 1993–2001, Ministry of Finance)

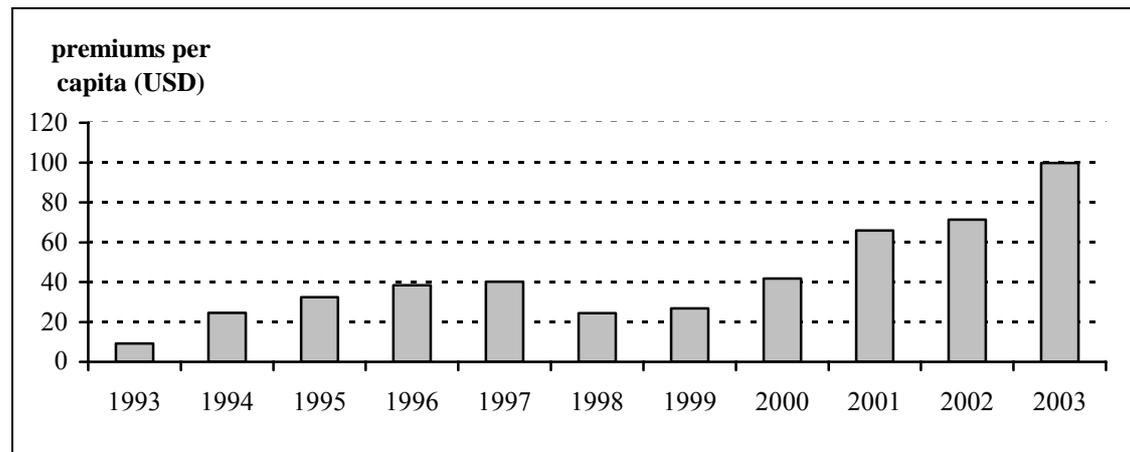
As the table above shows, the Russian insurance penetration has in the transitional period experienced clearly increasing trend. The GDP share of insurance premiums increased about sixfold between 1992 and 2001 reaching roughly 3% (of GDP).

<sup>2</sup> AIG = American Insurance Group

This very dramatic growth obviously has one decisive background factor: insurance business virtually started in the early post-Soviet period. The figure decreased slightly in 2002, but the insurance premiums as a percentage of GDP exceeded the 2001 mark in 2003.

In addition, the same table indicates, that the Rouble crisis did not affect the insurance scene. Premiums (as % of GDP) stagnated in the pre-crisis period (1995–1997), but increased clearly in the post-crisis period (1998–2001).

**Table 5 Russian insurance density 1993–2003 (Premiums per capita)**



(Source: Swiss Re Sigma 1993–2003, Ministry of Finance)

Russian insurance density trend (table 5) shows similar strongly increasing tendency, as the penetration development: premiums per capita in US-dollars grew from roughly USD 20 in 1994 to about USD 100 in 2003 – a fivefold increase. In the premiums per capita figures, the Rouble crisis of 1998 is clearly visible: a slump took place in 1998–1999, while a strong recovery occurred in 2000–2001. The latest figure (2003) indicates that a long-term boom is on the way.

**Table 6 Insurance density and penetration in Finland, Poland and Russia**

	1993		1996		2001	
	Insurance density	Insurance penetration	Insurance density	Insurance penetration	Insurance density	Insurance penetration
Finland	1132	6,8	1972	8,1	2098	8,9
Poland	44	2,0	79	2,3	140	3,1
Russia	9	0,8	38	1,3	66	3,1

The described positive trends in insurance penetration and density developments in the Russian insurance market are not surprising considering the low starting level in both cases.

The Russian insurance business is not yet on a mature level. This can be illustrated with some simple international comparisons.

In Table 6 three countries are involved: Finland, Poland and Russia. Finland is a small country with a high level of living standard. Poland is a transitional economy, like Russia. Poland, which joined the EU in 2004, has a living standard which is less than 50% of EU (15 countries) in average.

Not surprisingly, Finland has far higher figures in two accounts of Table 6, in density and penetration insurance premiums, than Poland and Russia. Premiums per capita were about USD 2.100 in Finland in 2001, while the equivalent figure in Russia was only USD 66: the Finnish result is about 32 times higher than the Russian one. In this comparison, Poland has an USD 140 marking, which is approximately twice the Russian equivalent, and far away from the Finnish result.

In the insurance penetration comparison, Finland has almost three times higher figure than Poland and Russia: the GDP share of insurance premiums in Finland (2001) was about nine per cent, while Russia and Poland are both a bit over the 3% mark.

The development of insurance density in the three selected countries is interesting. In the mature economy of Finland, the density figure almost doubled between 1993 and 2001 (85% growth). In the same period, the Polish economy in transition shows an increase in insurance density of over factor three. The equivalent growth in the transitional economy of Russia is no less than factor seven.

**Table 7 Insurance density and penetration in 2003 in Germany, UK and France**

	<b>Insurance density in 2003</b>	<b>Insurance penetration in 2003</b>
Germany	2.051	7,0
UK	4.058	13,4
France	2.698	9,2

It is a well-known fact, that insurance is a big business in all traditional market economies of the Western part of the world. The above table illustrates insurance density and penetration in Germany, the UK and France in 2003. All these three countries are so called large EU-countries.

Insurance density in Germany is virtually on the same level as in Finland (2001), but the penetration figure is about two percentage points lower. France is slightly ahead of Finland and Germany in both accounts, in insurance density and penetration.

The United Kingdom is clearly a special case in this small sample of countries. The British insurance density is about twice as high as in Finland and Germany exceeding also the French level considerably. Insurance penetration is with 13,4% essentially higher than in Germany and France.

The public sector involvement is essentially lower in the British economy in comparison to countries in the continental Europe. Thus, there are differences in the social safety net with EU. It can be assumed that this fact at least partially explains the high figures of British insurance density and penetration represented above: the UK state gives more leeway for individualism and personal insurance policies. The insurance density figure is no less than 62 times higher in the UK than in Russia.

It is impossible to predict what form the Russian economy will take with the development of market. There are two theoretical options: the Scandinavian type of welfare state now present in the most continental Europe of the EU-15, or the so called Anglo-Saxon model with less state tutelage. Obviously, the latter option provides more insurance business opportunities than the first one on the long run.

Presently, the living standard in Russia is about one third of the average level reached in Western countries mentioned in the above tables (Finland, Germany, UK and France). This statement is based on recent GDP per capita calculations purchasing power parity (PPP) adjusted. Therefore, it is understandable that Russia lags clearly behind advanced market economies in both insurance density and penetration, as the above comparison indicates.

It is a well-known fact that macro-economic indicators do not reflect reality completely accurately in transition economies, Russia included. In every post-communist society an unofficial market is in action, the extent of which cannot be properly estimated. It is not a secret that moonlighting takes place also in Western economies with high tax levels.

In the transitional economy of Russia, income distribution is extremely uneven. There are estimates according to which the best-off 20% of the population collects almost 50% of the available net income. This figure is in international comparison very high.

In addition, there are estimates that 25–30% of the Russian population lives below the subsistence level. The average life expectancy, especially for male persons is low (about 60 years for male persons).

Income distribution is not only low on the household level, but also in the regional comparison. People living in Moscow earn about four times more than the national average. In the second metropolitan area, in St. Petersburg, the living standard is twice as high as in Russia in general. Thus, the big bulk of discretionary income concentrates on these two urban centres. The rest of the huge country is often called province. Some regional centres have experienced dynamic development, which means that the geographical distribution of wealth and income cannot easily be described in simple terms. However, the predominance of the two metropolitan areas in transitional Russia is very evident: Moscow and St. Petersburg participate over proportionally to income creation, and thus, consume far above the national average.

Insurance figures used in this research report are mainly collected in Moscow, where about 80% of total insurance business takes place. The equivalent figure in St. Petersburg is only 5%, while the rest (15%) comes from the other regions. These figures may have some biases: the largest insurance companies have their headquarters in Moscow, but sell insurance policies throughout the country. Thus, the high share in Moscow is not necessarily reflecting correctly the distribution of insurance policies sold.

In international comparison, insurance business in Russia is still very modest. Life insurance branch has very peculiar features in Russia: obviously, the main bulk of agreements concluded originates from tax avoidance schemes with very little or no link to actual life insuring. It can be assumed that a certain part of insurance takes place in the unofficial economy. Moonlighting magnitude in this branch cannot be estimated.

There are certain trends in the Russian economy which will affect the insurance branch. Overall living standard is likely to increase rather rapidly because oil price is high at the moment, and in the immediate future, one result of the economic growth is the rapidly increasing car density, which in international comparison is still on a rather low level. This growing tendency on the car market is excellent news for insurance companies.

Private housing market is also booming. New dwellings and weekend houses represent valuable assets in private hands. Newly won properties obviously are worth to be secured

enhancing potentially insurance business. Probably, interest in actual life insurance policies will start to emerge.

### **3.6. Insurance Brokers in Russia**

The definition of insurance broker in Russian insurance law specifies a broker as an insurance intermediary, acting on behalf of policyholder, insurer or on its own. According to Russian insurance law before 1994, there were only two requirements for insurance brokers:

a) To be registered in the State Register of Insurance Brokers.

It was enough just to send notification to supervision to be included in the register. There were 1294 insurance broker companies in the register on January 1, 2004.

b) Not to distribute services of direct foreign insurers on the territory of Russia.

The importance of brokers was extremely low until 2002. Only local AON, Marsh, WFD, Heath and Lambert offices are worth mentioning. Activities of domestic insurance brokers have increased since 2002, but still there are no noticeable Russian-wide players.

There are several reasons for the low number of brokers:

1. Potential clients and investors are not well familiar with insurance to understand the role of a broker
2. For insurance professionals it is easier to work under a well-known label of an insurance company than under an unknown name of a broker
3. There are numerous so-called hidden brokers. Officially such individuals work like agents for several insurance companies choosing the best option for each and every client. Mostly such “hidden” brokers are specialized in private lines.

## **4. The present stage of Russian Insurance Industry (2004)**

### **4.1. Legislative aspects**

#### **4.1.1. Regulation and supervision**

In the early period of Russian transition, financial markets – including the insurance sector – had plenty of turmoil, which reached its culmination point in the Rouble crisis of 1998. This crisis caused extensive social and economic harm.

In the turbulence of the 1990s, it became evident that insurance schemes with the aim of tax avoidance and laundering money were not in the interest of the state. New rules in the insurance business were overdue.

A turnaround in the insurance legislation took place in January 2004 when the new edition of the Law on Insurance was issued.

This new law shows that Russian insurance legislation is on its way to the right direction: experience of the Western countries has been used in formulating the new rules. Even if the Russian insurance legislation is not just copied from other countries, the influence of the outside world is evident

Alongside with the new Law on Insurance, the system of Russian insurance supervision is reconstructed (on the basis of the Law passed in March 2004). One of the key ideas of the reform from insurance control point of view is to separate regulatory function (i.e. providing governmental policy by means of regulatory acts), from supervisory function (i.e. controlling the compliance of regulations and law by the companies). To fulfil the idea of the supervision, the function was transformed from Department of Insurance Supervision of the Ministry of Finance to Federal Service of Insurance Supervision (Federalnaya Sluzhba Strahovogo Nadzora – FSSN). At the same time, regulatory functions remained within the Ministry of Finance and were transferred to the Department of Financial Policy.

The supervisory reform was preceded by a public scandal, which is rather typical in Russia's current situation. A group of insurers blamed Mr. Konstantin Pylov (Head of Department of Insurance Supervision) and some other Governmental and parliament officials for creating a system of corruption by issuing licenses and using supervisory authority as a tool of competition favouring a few selected large companies.

Even if no action took place on the basis of this accusation, it is not a secret that some insurance companies were waiting for a reply on their application for a year or longer, getting neither yes nor no for an answer from the Supervisor. On the other hand, some companies were celebrating their new licenses in a couple of weeks after application although the law stipulates a two months period for making the decision about issuing the license.

This dispute lasted for some time. Thus, selecting the Head of the Federal Service of Insurance Supervision (FSSN) was not easy. Initially, the candidate number one was Mr. Pylov and another probable name was Mr. Motorin (former Deputy Minister of Finance and immediate boss of Mr. Pylov). Finally, the appointment was made and Ilya Lomakin-Rumyantsev, who had already been at the Head of Insurance Supervision in the late 90's, became the Head of FSSN. The majority of insurance companies commented this appointment positively.

Before the reform of 2004, the license obtaining process was not described in the Law in detail. This meant that the Supervision had the possibility to establish its own rules and change them whenever it wished. Now the procedure is fixed in the Law in detail and thus, there is less leeway for corruption.

However, it is too early to judge, whether the licensing procedure will change considerably under these new arrangements. When insurance companies' (big and small ones) license package applications will be considered under the new circumstances, it will be possible to assess, whether the situation will improve or not.

#### **4.1.2. Investment, capital and reserve regulations for companies**

Current investment regulations for insurance companies are valid since February 22, 1999, amended March 16, 2000 and August 18, 2003. Previous regulations were changed as a result of the 1998 crisis. Investment regulations are valid only in respect of reserves (provisions). No other regulations concerning capital investments do exist. Anyhow, the new version of the Law on Insurance gives to the Supervisor the right to establish regulations also in respect of capital.

The following assets are accepted:

1. Securities of federal government;
2. Securities of regional governments;
3. Municipal securities;
4. Bank promissory notes;

5. Shares (stock);
6. Bonds except for mentioned in items 1–3;
7. Building certificates except for mentioned in items 1–3;
8. Shares in investment funds;
9. Bank deposits including deposit certificates;
10. Shares in bank trust funds;
11. Shares in partnerships;
12. Real estate;
13. Reinsurers' shares in reserves;
14. Reinsurance premium deposits;
15. Payments receivable from policyholders, insurers, reinsurers, reinsurers and insurance intermediaries;
16. Cash;
17. Roubles on current accounts;
18. Foreign currency on current accounts;
19. Gold and silver in bars.

Real property: separate flats, vessels, aircrafts and space objects are excluded. Other assets can be accepted by special consent of the Supervisor. Assets cannot be in mortgage. Banks should be licensed in due order. Securities should be traded at registered / licensed stock exchanges. Investment funds should be registered according to Russian law. Payments receivable: only payments to be received within nearest three (3) months in case such payment receivables are related to insurance / reinsurance operations. Shares in partnerships are accepted only in case that there are no limitations on their sale. Investment in gold and silver can only be done in the territory of Russia.

A newly established insurance company faces new capital requirements, different for life and non-life companies. Any newly established life-insurance company must have MRUR 60 (1 USD  $\approx$  29 RUR) charter capital to get a license. Non-life insurance companies can start with MRUR 30. Reinsurance companies or companies combining direct business with inward reinsurance, should have MRUR 120 capital. For those companies, that are already present in the market, the law allows gradual increase of capital.

These requirements are applicable only for companies looking for a new license. Companies that obtained the license or applied for it before December 31, 1997, are not affected by these regulations. The requirements for reinsurance are applied only to companies requesting license for reinsurance. All direct insurers have the right to be reinsurers as well. It's commonly expected that at least half of insurance companies existing on January 1, 2004 will not cope with new capital requirements and gradually disappear during July 1, 2004–July 1, 2007.

**Table 8**      **Gradual increase of capital (deadlines and amounts, MRUR)**

<b>Company</b>	<b>July 1, 2004</b>	<b>July 1, 2006</b>	<b>July 1, 2007</b>
Non-Life	10	20	30
Life	20	40	60
Reinsurance or inward reinsurance combined with direct insurance	40	80	120

The new insurance legislation is likely to cause restructuring of insurance branch. First of all, many companies are eager to separate business immediately to minimise the expensive procedure of life portfolio transfer in the future. Secondly, if one buys an insurance company now, he does not have to pay MRUR 1–2 as a charter capital immediately. The price for a small existing insurance company could fluctuate, but most of the acquisitions (according to unofficial information) will cost something like USD 100.000–200.000 on top of the net assets of the company.

According to the information of Insurance Supervision Office, 437 (of 1397 insurance companies as registered on January 1, 2004) companies had to increase their capital within one month as their capital on June 1, 2004 was below the requirements for July 1, 2004. Russian authority made a comprehensive checking among the insurance companies and found out that that was the number of companies who must implement this capital injection just during one month to keep their licenses. That number included 23 reinsurance companies (of total 45) and almost all (251) health insurance companies. Another 367 insurers (combining life and non-life insurance) had capital less than needed for life business but enough to continue with non-life. About two thirds of all insurers had to increase their capital within one month.

Among medical insurance companies, there was clear confusion. Before the adoption of the new version of the Law, all medical insurers were sure that this new version wouldn't touch them.

In April 2004, some medical insurers were convinced that they did not have to take care about additional capital and only after special public notice of the Supervisor they started all necessary procedures.

For small companies there are severe problems arising from the new capital requirements. All the companies are not able to find resources to increase the capital. Issuing new shares and selling them to outside investors is not very attractive to current owners. They are normally managers and decision-makers in the companies. They are used to situations in which they

can make whatever decisions within the company and now they face a risk of finding themselves just as minor shareholders without any position in the company management.

It is likely that some insurance companies will use bookkeeping tricks to fulfil the new requirements. As there are no regulations concerning placement of charter capital, it is quite easy to inject some money into the company and later move the real assets from the company by purchasing some non-liquid securities of related companies. Often there is a chain of companies and the injected capital returns to the investor. Repeating this operation several times allows the company to increase the nominal charter capital in amount  $x$  times bigger than the real amount involved in operation.

This pumping of capital obviously is not such an attractive solution in the long-term, because the real ability of the company to carry risks does not increase and the ability to invest in development does not increase either. In the meanwhile, other companies are strengthening their competitive position.

Russian reinsurers must be duly licensed. Foreign reinsurers, which are licensed in their home countries, can get a permit in Russia, provided that their creditworthiness is noted by a reliable rating agency. In this context, rating guidelines are as follows: A.M. Best (B+), Standard&Poor's (BBB-), Fitch IBCA (BBB-), Moody's (Baa3), Weiss Research (B-). (The quoted marks are minimum requirements.)

Previously regulations were less detailed (fewer positions than now were mentioned). There was a minimum share of Federal securities (10%), now there is neither upper, nor lower limit for them. Interestingly, in this context there is no compulsory share of Federal securities mentioned in the new list. Formerly, this share was 10% (minimum requirement).<sup>3</sup>

Until 2004, life and non-life insurance business in Russia could be run in one legal entity. For insurers it was convenient to cover tax avoidance by mixing it with real non-life business, or just organizing cash flow to clients of tax avoidance schemes by means of life, non-life insurance and reinsurance.

Quite obviously, activities linked with tax evasion are not in the interest of the state. Thus, reforms in the insurance sector are not surprising.

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<sup>3</sup> See Appendix 2 for more detailed list of reserve portfolio guidelines.

Now the new Law of insurance stipulates that life and non-life insurance business cannot be run within one legal entity. Since January 17, 2004 any newly established insurance company cannot apply for both life and non-life licenses within one company. For companies possessing both licenses on January 17, 2004, the established law allows transitional period until July 1, 2007.

All companies combining life and non-life business at the moment have to choose either life or non-life business. In case the company chooses non-life, existing portfolio of life policies must be transferred to another legal entity (portfolio transfer). Until now, the Supervisor has not worked out the procedure in detail.

#### **4.1.3. Regulation of foreign insurance companies**

The overall share for foreign capital in the aggregate capital of Russian insurance companies was increased from 15% to 25% in the new Russian insurance Law. This change has hardly any importance, because actual (2003) share of foreign capital is about 3,5% or BRUR 6,5. As numerous local companies are now increasing their capital according to new capital requirements, the share of foreign capital will decrease.

Foreign subsidiaries or insurance companies with over 49% share of foreign capital are not allowed to write life insurance, compulsory insurance, insurance related to governmental contracts, insurance of property interests of governmental or municipal organisations in Russia.

Exception is made for such foreign owned companies that obtained licenses for life or compulsory insurance before the amendments to the Law made on November 20, 1999 became effective.

Subsidiaries of EU companies are free from all the above limitations (excluding the total quota of foreign charter capital). They are even granted the right to appoint foreigners to be general managers or chief accountants of their Russian companies.

Like mentioned above, the foreign related companies are not playing any significant role on the Russian insurance market. The six companies listed here include two (AIG Russ and ROSNO) big ones while the other four (4) are middle size Russian insurance companies.

Qualification requirements are introduced in the new Law (January 17, 2004) for general managers and chief accountants of Russian insurance companies. General manager of a Russian insurance company should have higher education in economics or finance and have at least two (2) years experience in insurance or finance<sup>4</sup>. Chief accountant of an insurance company should have at least two (2) years experience in insurance accounting (insurance company, reinsurance company, insurance broker company).<sup>5</sup>

General managers and chief accountants of insurance companies should be Russian citizens<sup>6</sup>. The new law stipulates requirements to provide annual actuarial analysis of liabilities of insurance companies from 2007. Actuaries should pass qualification and obtain certificates in FSSN. The details of such procedure will be established by FSSN. The Supervisor should be ready to issue certificates in mid 2006.

## **4.2. Russian insurance companies**

### **4.2.1 Insurance companies in figures**

Although Russian insurance companies have increased their capital during the past several years, Russian insurers remain comparatively small financial institutions. For example, aggregate assets of Top 100 Russian banks exceeded aggregate assets of Top 100 insurers by 14,7 times.

Aggregate assets of Top 100 Russian insurers reached BRUR 288,4 (BUSD 9,4) and net assets BRUR 281,1 (BUSD 9,16). The largest insurance companies by assets are SSO BRUR 30,6, Rosgosstrakh (Group) BRUR 30,5, Ingosstrakh BRUR 19,1, Capital-Strakhovaniye BRUR 16,4 and RESO-Garantiya BRUR 13,1. Net assets of Top 10 insurers reached BRUR 153,7 in 2003.

According to a study by Interfax (a news agency), 135 largest insurers' share of equity capital in total assets of insurance companies increased from 21,1% in 2002 to 22,7% in 2003 and reached BRUR 2,16 (generally the growth of equity capital of insurers decelerated in 2003).

According to official information provided by Supervision, the aggregate charter capital of Russian insurers exceeded BRUR 88,6 in 2003. The growth compared to 2002 was 86,1%.

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<sup>4</sup> Federal Law No 4015-1, Article 32.1, paragraph 1

<sup>5</sup> Federal Law No 4015-1, Article 32.1, paragraph 2

<sup>6</sup> Federal Law No 4015-1, Article 32.1, paragraph 5

According to a study by Interfax, top 100 insurance companies had an annual asset growth of 45,7% in 2003. Most probably the growth is related to the new capital requirements introduced by the new Law on Insurance. These requirements were known already in 2003 and many small companies started to increase their capital in advance.

The largest companies by equity capital (as of end of 2003) are:

- Rosgosstrakh Group – BRUR 6,8 (almost 300% growth during 2003)
- Capital RE – BRUR 6,8
- Capital Strakhovaniye – BRUR 4,9
- Ingosstrakh – BRUR 4,2
- RESO-Garantiya – BRUR 3,3

When the two companies of Capital Group are counted together, this group exceeds Rosgosstrakh in terms of equity capital. Capital Re's capital belongs to Lukoil, one of the largest and most successful oil companies in Russia.

Aggregate equity capital of Top 10 Russian companies in 2003 reached BRUR 35,3

According to Interfax's Top 100 –report there was a 47,3% growth of insurance reserves in Russia in 2003. The share of reserves in total liabilities remained stable (57,1% on January 1, 2003 and 58,0% on January 1, 2004). At the same time the share of life insurance provisions was decreasing. The absolute sum for life insurance provisions was BRUR 40,67, which is 17% higher than in 2002.

The share of investment in total assets of insurance companies has been decreasing within the last 4 years from 51,2% in 2000 to 40,7% in 2003. In 2002 and 2003 the decreasing trend mostly concerned life companies. When cancelling tax avoidance schemes, insurance companies used investment assets to fulfil the liabilities.

The share of liquid assets in insurance companies' portfolio increased from 13,9% in 2002 to 20,5% in 2003. This change obviously reflects general uncertainty in the Russian securities market. On October 25, 2003, Mikhail Khodorkovsky, the chief executive officer and main shareholder of Yukos (the biggest oil company in Russia) was arrested and accused of fraud and tax evasion. Charges against the richest man of Russia have changed, but no concrete court case has taken place.

The case against Yukos and its main shareholder is a permanent source of nervousness in Russia's capital market, in which traded shares comprise mainly companies active in

extractive industries (like oil for example), and utilities. The Yukos affair may be one of the reasons for the above-mentioned figures: insurance companies prefer liquid assets.

One problem insurers are facing in the emerging market of Russia is the non-payment of premiums agreed upon. If clients delay or neglect their payments, there is hardly any de facto legal path open for insurance companies to force policyholders to fulfil their payment obligations. Thus, insurers face the problem of so-called virtual reserves: all written premiums are not covered with actual payments.

Even if the share of investments in assets of insurance companies is falling, the absolute amount of investment is increasing. 135 largest insurers showed a 40,3% growth of investments in 2003. The aggregate investments reached BUSD 3,86 in 2003.

Enterprise bonds and loans to other companies take far the largest position in the overall portfolio: buying the biggest companies' bonds and crediting them took over 40% of the overall portfolio in 2003. This position grew in 2003 by almost 60% against 2002. The second most important position is holding shares of other companies. The annual increase in 2003 of this part of the portfolio was about 50%. However, the share of this position increased only slightly, from 19,2% in 2002 to 20,4% in 2003.

Thus, Russian insurers mainly finance the company sector, which gets over 60% of the money invested by insurance companies. Bonds and loans (over 40%) are preferred to risk capital investment (over 20% of the investment under review is in company shares).

A rather high sum is invested in deposits. This secure form of investment had a share of almost 15% in the overall portfolio of big insurers in 2003. The share of this position shows a decrease, even if the absolute sum grew somewhat in 2003.

The highest yearly growth rate can be found in investing into government bonds in 2003. The growth was almost 80%. However, state bonds only take a minor (less than 4%) share in the total portfolio. At the same time, insurers reduced their involvement in real estate, as well as keeping bonds of their own subsidiaries and crediting them.

Obviously, government bonds are regarded as low risk investment alternative in the West. The crisis of 1998 showed that the risk of defaulting was a real one in Russia. In the post-crisis period, the attractiveness of state bonds has clearly increased, which explains the high growth in this sphere in the insurers' portfolio.

**Table 9 Structure of investment portfolio of 135 largest insurers (BRUR)**

	2002		2003		Growth (%)
	BRUR	Share (%)	BRUR	Share (%)	
<b>Investments</b>	84.397.375	100,0	118.451.111	100,00	40,3
Real estate	1.262.231	1,5	684.999	0,6	-45,7
Shares of subsidiaries and affiliates	3.232.055	3,8	5.672.482	4,8	75,5
Bonds of and loans to subsidiaries and affiliates	789.893	0,9	202.968	0,2	-74,3
Participations in subsidiaries and affiliates	4.474.555	5,3	4.727.041	4,0	5,6
Shares of other companies	16.158.400	19,2	24.162.832	20,4	49,5
Bonds of and loans to other companies	31.711.672	37,6	49.934.483	42,2	57,5
Participations in other companies	5.688.877	6,7	7.779.261	6,6	36,7
State bonds	2.232.849	2,7	3.952.995	3,3	77,0
Deposits	13.532.922	16,0	17.180.086	14,5	27,0
Other investments	5.313.922	6,3	4.153.965	3,4	-21,8

(Source: CEA of Interfax)

**Table 10 Income and expenditure of 135 largest insurers (BRUR)**

	2002		2003		Change (%)
	BRUR	Share (%)	BRUR	Share (%)	
<b>Income</b>	<b>532.082.232</b>	<b>100,0</b>	<b>539.460.743</b>	<b>100,0</b>	<b>1,4</b>
Life premiums	95.999.043	18,0	94.672.816	17,5	-1,4
Non-life premiums	150.490.813	28,3	210.028.550	38,9	39,6
Life claims covered by reinsurance	3.487.366	0,7	21.796.549	4,0	525,0
Non-life claims covered by reinsurance	8.176.832	1,5	9.688.504	1,8	18,5
Investment income	265.837.726	50,0	189.779.341	35,2	-28,6
Commissions	1.479.981	0,3	2.475.106	0,5	67,2
Other income	6.610.472	1,2	11.019.877	2,0	66,7
<b>Expenditure</b>	<b>-504.923.541</b>	<b>100,0</b>	<b>-479.331.775</b>	<b>100,0</b>	<b>-5,1</b>
Claims (life insurance)	-113.934.053	22,6	-99.193.593	20,7	-12,9
Claims (non-life insurance)	-33.544.323	6,6	-51.229.689	10,7	52,7
Life premiums ceded to reinsurers	-8.510.782	1,7	-15.661.665	3,3	84,0
Non-life premiums ceded to reinsurers	-82.138.847	16,3	-105.242.279	22,0	28,1
Investment costs	-245.221.411	48,6	-169.604.147	35,4	-30,8
Insurance operations costs	-8.430.373	1,7	-16.452.863	3,4	95,2
Administration costs	-8.486.683	1,7	-14.479.209	3,0	70,6
Other expenses	-4.657.069	0,9	-7.468.330	1,6	60,4
<b>Reserves (provisions)</b>	<b>-16.015.061</b>	<b>100,0</b>	<b>-46.130.722</b>	<b>100,0</b>	<b>188,0</b>
Profit (pre tax)	11.143.630		13.998.246		25,6
Net profit	9.472.380		12.828.166		35,4
Net income before creation of reserves	27.158.691		60.128.968		121,4

(Source: CEA of Interfax)

The bookkeeping of the biggest 135 insurance companies shows some interesting points in the revenue development. In 2002, just half of the overall revenue came from investment

income. In 2003, the equivalent share was only slightly over 35%, while the absolute value of investment income dropped no less than 28,6%. As mentioned above, the overall investment portfolio of the 135 leading insurers grew by some 40% in 2003. These figures indicate that the investment portfolio managers in the Russian investment sector had a miserable year in 2003.

Obviously, portfolio management is not easy in the Russian insurance companies, because there are certain guidelines limiting investment activity and regulations concerning foreign investment. Moscow stock exchange has a very limited range of stocks, the value of which is affected by internal and external factors. As mentioned above, the Yukos affair has increased uncertainty in the securities market. Interest rates have a tendency to go down with more moderate inflationary expectations.

The most important revenue position of the biggest insurance companies was in 2003 non-life insurance premiums with a heavy annual increase by 40%. This part brings in almost 40% of the entire income, while life premiums make up less than 20% (17,5%). The life insurance premium development was slightly negative in 2003.

On the expenditure side of the big insurers' bookkeeping, investment takes more than one third of the total sum in 2003. Investment costs decreased by more than 30% against the previous year.

The second highest expenditure position is with 22% share non-life premiums ceded to reinsurers, which in this context received about 28% more money from insurers in 2003 than in 2002. Claims in life insurance take about one fifth of the entire expenditure of the big insurers showing a 13% decline from 2002 level. Non-life claims make up about one tenth of the insurers' costs with a huge increase of 53% between 2002 and 2003.

Running insurance operations in Russia is getting more expensive. The operation costs of the biggest 135 companies almost doubled in 2003. At the same time, administration costs experienced a hike of 71%. It can be assumed that the rapid growth in these two expenditure positions are closely linked with CMTPL schemes, which call for new retail networks and cause high marketing costs.

The capital level of companies and solvency margins create a situation in which Russian insurance companies' self-detention of the risks is very limited and thus, they need

comprehensive reinsurance solutions to back up their business. This means that premiums (money) go to reinsurers instead of the companies writing the risks.

Like every other emerging market, Russian insurance industry already now faces rather heavy competition for the clients. When rates are going down, underwriting results are coming down as well. In the situation where solvency margins of Russian insurance companies are narrow, their buffer to participate to the competition gnaws the solvency of companies.

Appendix 1 provides comprehensive data of 100 biggest insurance companies in Russia.

#### 4.2.2. Leading insurance companies

On January 1, 2003 there were over 1.200 registered insurance companies in Russia and over 30 reinsurance companies.

According to the information of Ministry of Finance of Russia (Minfin) the total premium income was BRUR 432,4. Compared to 2002 the growth was 44%. In 2002, the growth was only eight (8)%.

**Table 11 Insurance premium growth 1998–2003**

	<b>Growth (%)</b>	<b>Premium income (BRUR)</b>	<b>Rate RUR/USD *</b>
1998		42	9,71
1999	131	97	24,62
2000	76	171	28,13
2001	62	277	29,17
2002	8	300	31,35
2003	44	432	30,57

\* Important to notice in comparisons

Almost the whole year 2002 the growth was decelerating, because many companies started to get rid of tax avoidance and money laundering insurance. Due to changes in insurance legislation, life insurance premiums predictably fell. Experts predicted property insurance to double, but the growth in this area remained modest.

There is a clear consolidation process in the Russian insurance market: the share of Top 20 insurance companies is about 50% of the total. Share of Top 100 exceeds 77%.

Top 10 insurance companies have following features:

1. Five (5) of top 10 are specialized in tax avoidance and are not involved in real insurance (life premiums over 80%, low marketing activities).
2. One of top 10 companies has the share of compulsory (medical) insurance in its portfolio over 99%.
3. Only two of top 10 companies (Reso-Garant and Ingosstrakh) reached high results due to real business success.
4. There are no captive companies in top 10 (Uralsib should be considered like a captive of Uralsib Financial group as this company has already been in top 10 before Uralsib purchased it).
5. There are no foreign related companies in top 10.

Top 20 assessments:

1. Eight (8) of top 20 are specialized in tax avoidance schemes. Another two of 10 have over 50% share of life business, which is also a sign of tax optimisation.
2. Two companies have the share of compulsory insurance in its portfolio over 99%.
3. There are three (3) captives in top 20 (SOGAZ, Soglasie, Capital-Strakhovaniye, belonging to Gazprom, Interros and Lukoil respectively). These companies are not 100% captives, but big portion of their insurance portfolios consist of mother companies' risks. Initial success was guaranteed by ability to create portfolios of big industrial risks without competition.
4. There is only one (1) foreign related company in top 20 – ROSNO. It is important to mention that ROSNO was in top 20 already before Allianz Group (Germany) joined the company. In 2002 its rank was number four, now it is in place 11. Obviously, ROSNO has lost its position in top 10, because the new owner has started to clean the company from tax avoidance to increase underwriting standards and implementation of company's management guidelines.

Top 100 list comprises following points:

1. At least 16 companies have concentrated on tax optimisation.
2. At least 25 companies are captives or belong to oligarch<sup>7</sup>, banks, oil, gas companies or other so-called natural monopolists.
3. There are 37 companies with the share of compulsory insurance over 1/3. These are mostly medical insurance companies but also some other lines of compulsory insurance are involved (insurance of military and other state personnel, travellers' insurance etc).
4. There are only two (2) foreign related companies in top 100 (AIG-Russ and ROSNO). Ost-West Allianz is in place 105 and very close to top 100.

#### **4.2.3. Regional distribution of premiums**

In the early period of Russian transition, the economy declined continuously. Amid this economic slump, it became clear that the state couldn't maintain an extensive safety net. Thus, it is understandable that certain compulsory insurance schemes, for example in health care, were introduced.

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<sup>7</sup> Oligarch is a term used to describe new rich Russians, who own (and run) big companies.

At the same time, the share of private consumption of GDP increased. In this context, car density, which remained on a very low level in the communist period, started to increase. Car demand shows continuously increasing trend, and thus, insurance policies linked with car ownership have increasing potential. The introduction of CMTPL (Compulsory Motor Third Party Liability insurance) has enhanced insurance business considerably.

By definition, compulsory insurance schemes comprise the entire population, which means that the new demand must be covered with supplementary supply. Local insurance companies have emerged changing the geographic pattern of the insurance sector.

The share of Moscow-registered companies decreased from 65% of the entire insurance business in 2002 to 55% in 2003. At the same time, the share of Moscow region (Moskovskaya oblast) declined from 5,8% to 5,4%. Compulsory insurance schemes have obviously influenced the geographic distribution of the sector under review.

In all Western industrialized countries, a strong consolidation process has taken place. Every mature market economy has an oligopolistic insurance market with very few national players. Big companies have swallowed small ones. In the fierce competition, economies of scale have a decisive importance: a handful of big players with local offices dominate the scene. The biggest insurance companies have become international behemoths.

It is highly likely that a similar consolidation will take place in Russia. This concentration process in the Russian insurance market is likely to last several decades, not some years.

Appendix 3 describes insurance business in 80 regions of Russia. The list contains overall premiums collected in different parts of the country.

In the turn of the century, Russia was divided into seven macro-regions in an administration reform. The Central Region comprises Moscow and its surroundings. The north-western macro-region contains the second metropolitan area – St. Petersburg with her surroundings.

The Central macro-region with the capital city in it, is far ahead in collecting voluntary insurance premiums taking almost 73% of the overall figure. The Volga macro-region is on the second place in this competition with a share of close to 8%. The north-western territory with St. Petersburg in it is third with a less than 7% share.

In the compulsory insurance business segment (excluding compulsory health insurance), the picture is very much different. The Central macro-region is also in this comparison in the leading position, but only with a 44% market share. The Volga region is the second with an almost 15% marking, and north-western territory on the third place with roughly one tenth of compulsory premiums collected.

In the compulsory medical insurance premium table, the distribution is more even, than in the previous comparison. The Central region is once more in the lead with over 40% share, but now the Siberian macro-region comes the second with almost 20% of the premiums. The north-western is third with a percentage of 13,5.

In sum, the Central macro-region (Moscow as a part of it) dominates very clearly the voluntary insurance business. Compulsory medicare and non-medicare arrangements affect strongly the insurance business scene and even out regional differences in collecting insurance premiums.

**Table 12 Insurance premiums according to the federal districts**

Federal district	Voluntary		Compulsory (except for medical)		Total (except for compulsory medical)		Compulsory medical	
	BRUR	% of total	BRUR	% of total	BRUR	% of total	BRUR	% of total
Central	239,1	73	12,9	44	252,0	70	29,8	41
North-West	22,5	7	2,9	10	25,4	7	9,9	14
South	6,0	2	2,7	9	8,7	2	6,0	8
Volga	25,7	8	4,3	15	30,1	8	5,9	8
Urals	17,1	5	2,6	9	19,7	6	2,1	3
Siberia	14,9	4	2,7	9	17,6	5	14,3	19
Far-East	4,1	1	1,0	4	5,2	2	5,5	7
<b>TOTAL</b>	<b>330</b>	<b>100</b>	<b>29 304 744</b>	<b>100</b>	<b>358,9</b>	<b>100</b>	<b>73,6</b>	<b>100</b>

#### 4.2.4. Foreign insurance companies in Russia

Foreign insurance companies' presence on the Russian insurance market has permanently been very modest. From 1992 to 1997 foreign ownership participation was limited in every single company to 49%. After 1997, the rules were changed to a quota for foreign capital in the aggregate capital of all Russian insurers. The foreign charter capital in Russian insurance companies was not allowed to exceed a 15% ceiling of total capital involved.

The rules concerning involvement of foreign capital in the Russian insurance business have permanently been vague. Foreign direct investment (FDI) means that a foreign juridical or physical person is investing across the border looking for dominance in an economic unit abroad. Portfolio equity investment is also a form of risk capital movement, but in this case the foreign investor is said to be passive: portfolio investor seeks with a small stake increase value for shares bought in a foreign stock exchange; portfolio investor is not interested in dominating the company, in which the investment is made. The rules valid in Russia since 1997 stipulate that these two forms of investment taken together are not supposed to have more than a 15% of the overall capital in the Russian insurance market.

Some Western companies established holding companies in Russia in the 1990s. These holding companies were by definition local (Russian) ones. Some of these holding companies bought or established local insurance units. Thus, some Western insurance companies got their wholly owned subsidiaries in Russia (via holding companies).

Twelve (12) Russian registered insurance companies have foreign ownership of 49% or more. The main players are the following ones (source of official information: State Register of Insurers as of April 1, 2004):

#### *AIG Russia*

(ZAO AIG Russia)

[www.aigrussia.ru](http://www.aigrussia.ru)

- Licence from 1994
- Operations started in 1995
- Life licence and operations since 1997
- Activities in Russia: Life insurance / non-life insurance (big industrial and commercial Russian risks, serving AIG's global clients in Russia and individual clients)
- Major products: Property, liability, financial risks, energy risks, cargo, motor, private property, personal accident, travel insurance, medical, life and pension insurance.
- Charter capital MRUR 42,6
- Life and non-life operations are run within one legal entity
- Office in St.Petersburg since 1996
- Problems with license in 1999–2000 mainly due to political reasons

#### *Zurich-Russ*

[www.zurich.com](http://www.zurich.com)

- Operations started in 1994 as a local company Vestrosso. 1996 the company was purchased by Zurich
- In 2003 Zurich's share was increased up to 99,7%.
- Major activity areas in Russia: Life and pension insurances, big industrial and commercial Russian risks, marine insurance and serving Zurich's global clients in Russia
- Charter capital since 2001 MRUR 40
- License for life and non-life insurance
- Operations are run within one legal entity

- Rep offices: St.Petersburg, Ufa, Vladivostok, Khabarovsk

#### *Russ*

[www.al-h.de](http://www.al-h.de)

- Vladislav Reznik established the company in 1990. He is currently the Chairman of the Committee on Banks and Financial Markets of Duma (this committee is also in charge of insurance legislation)
- The company is based in St.Petersburg (All other foreign subsidiaries are Moscow-based)
- Major areas of activities in Russia: industrial and commercial risks, private lines and serving Alte Leipziger's (AL) global clients in Russia
- Charter capital MRUR 37,2
- Life and non-life operations are run within one legal entity
- Main task in 2004 is to improve their position in Moscow market. For this purpose AL's management planned to invest MEUR 20 in the company

#### *Ost-West Allianz*

[www.allianzgroup.com](http://www.allianzgroup.com)

- The company was established in 1990.
- The company provided all lines of insurance and had a branch office in St.Petersburg
- In 2002 Allianz purchased 45,7% of ROSNO and decided to develop the latter as a market project of Allianz
- Ost-West Allianz closed their office in St.Petersburg and significantly decreased the number of personnel in Moscow
- At the moment the company is concentrated on global clients
- Charter capital MRUR 86

#### *ROSNO*

[www.rosno.com](http://www.rosno.com)

(OAO ROSNO – one of the largest Russian full-service insurance companies)

- 100 branch offices united in 10 regional departments and 186 agencies
- Representative office in Kazakhstan and subsidiary company in Kirgyszstan
- Major shareholders: AFK Sistema – 47%, Allianz AG 45,3%
- Charter capital as on 31.12.2003 BRUR 1,5
- Insurance reserves BRUR 5,3
- Reinsured at Allianz, Hannover Re, SCOR, Munich Re, Swiss Re, Russian reinsurance companies and Lloyd's

#### *Principal*

A group of British Investment funds, an insurance company and the European Bank of Reconstruction and Development (EBRD) established the company in 1995 as a life insurer. As the company reached no success under its original ownership structure, it was sold to Pohjola Group (Finnish Insurance Group) in 1998. By means of nominal holding, 1/3 of the company belongs to EBRD and 2/3 to Pohjola.

Pohjola converted the company to non-life insurer. Later (in 2001) Pohjola's strategy related to international insurance business changed and it lost its interest in Russian insurance market and decided not to invest more into the company. At the moment, the company is not active

and is for sale. According to market rumours (unofficial information) the most probable buyer candidate for Principal is Uralsib, one of the largest Russian insurers.

In August 13, 2004 the Russian insurance Supervisor withdrew Principal's insurance license because Principal didn't fulfil the new capital requirements before July 1, 2004. Principal was one of the 151 companies whose insurance license was withdrawn for the same reason.

#### *Other companies*

The other six companies with foreign involvement are very small ones and not very active on the market.

#### **4.2.5. Russian insurance lines and products**

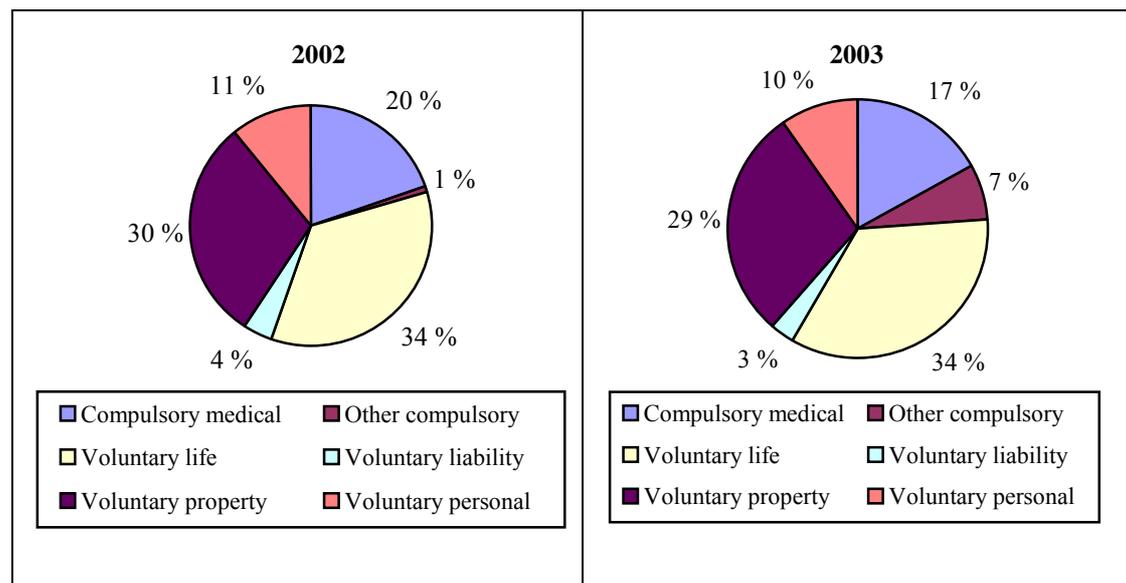
Structural changes took place in the Russian insurance market in 2003. Captives came actively to the open market. Major Russian insurers continued to decrease their share of tax avoidance life insurance and to increase the share of real insurance including real classic life insurance.

The share of voluntary insurance continued to decrease from 79,4% in 2002 to 76,2% in 2003. The share of the personal insurance lines also decreased from 10,7% in 2002 to 9,6% in 2003, property insurance from 30% in 2002 to 29,1% in 2003, and liability insurance from 4,1% in 2002 to 3% in 2003. The share of life insurance decreased insignificantly from 34,6% in 2002 to 34,5% in 2003.

The share of compulsory insurance lines increased from 20,6% to 23,8%. It is important to notice that the share of compulsory medical insurance decreased from 19,6% in 2002 to only 17% in 2003.

**Table 13 Insurance lines per cent from total in 2002–2003**

	<b>Compulsory Medical</b>	<b>Other Compulsory</b>	<b>Voluntary Life</b>	<b>Voluntary liability</b>	<b>Voluntary Property</b>	<b>Voluntary personal</b>
2002	19,6%	1,0%	34,6%	4,1%	30,0%	10,7%
2003	17,0%	6,8%	34,5%	3,0%	29,1%	9,6%

**Table 14** Structure of insurance premiums in 2002–2003 (%)

Source: Ministry of Finance of Russia ([www.minfin.ru](http://www.minfin.ru))

According to information by Ministry of Finance (Minfin) total premiums in voluntary insurance in 2003 reached BRUR 329,5 (38,2% increase), while claims reached BRUR 208,1 (20,6% growth).

Property insurance premiums reached in 2003 BRUR 125,7 (growth 39,5%), claims BRUR 23,5 (60,1% increase compared to 2002). The market leader in property insurance was RESO-Garantiya – BRUR 7,7. The share of 10 largest property insurers in 2003 was BRUR 44,6 or 35,5% (in 2002 – 42,2%). There are many captives of big industrial (mostly oil and gas) groups in top 100.

**Table 15** Top 10 property insurers and largest foreign companies

Company	Register Number	Premiums MRUR	Claims MRUR	Loss ratio (%)
1 Reso-Garantiya	1209	7.676	1.812	23,6
2 Ingosstrakh	928	6.976	2.182	31,3
3 Soglasie	1307	5.034	406	8,1
4 Capital Strakhovaniye	1298	4.864	1.075	22,1
5 National Insurance Group	1826	4.474	151	3,4
6 Sogaz	1208	3.531	348	9,9
7 URALSIB (Former NIKOIL)	983	3.486	597	17,1
8 Priroda	3130	3.139	387	12,3
9 ROSGOSSTRAKH (Without Subsidiaries)	1	2.737	295	10,8
10 Rosno	290	2.666	1.048	39,3
46 Aig Russia	3256	608	56	9,2
49 Ost-West Allianz	2294	549	75	13,7
92 Zurich-Russ	212	275	48	17,5

(Source: VSS according to information from Minfin)

Liability premiums increased to BRUR 12,9 (growth 5,1%) in 2003. Claims were BRUR 2,4 (growth 36,3%). Introduction of CMTPL almost eliminated the market of voluntary MTPL. The leader of this sector was NESO with MRUR 946 of liability premiums. The share of 10 largest voluntary liability insurers was 42,1% of BRUR 5,43 turnover.

There are captives and companies specialized in marine and aerospace insurance in top 100.

In Russia there is so-called voluntary–compulsory insurance. The term voluntary–compulsory describes a situation, in which there is no law that would make insurance compulsory, but buying such insurance from a certain (normally affiliated with federal or more often local authorities) company is a precondition for participation in governmental and municipal tenders for construction, supply of goods etc.

**Table 16 Top 10 liability insurers and the foreign ones**

	<b>Company</b>	<b>Register Number</b>	<b>Premiums MRUR</b>	<b>Claims MRUR</b>	<b>Loss ratio (%)</b>
1	NESO	3310	946	0	0,0
2	Ingosstrakh	928	819	317	38,7
3	Reso-Garantiya	1209	715	262	36,6
4	Russo-Garant	3417	534	2	0,5
5	Moskva	191	479	2	0,4
6	Maks	1427	478	59	12,4
7	Soglasiye	1307	463	45	9,6
8	Priroda	3130	362	3	0,8
9	Military Ic	621	322	118	36,8
10	Avest-Classic	3495	308	41	13,4
11	Rosno	290	295	89	30,0
14	AIG Russia	3256	230	0	0,1
44	Zurich-Russ	212	54	6	11,6
66	Ost-West Allianz	2294	32	1	2,0

(Source: VSS according to information from Minfin)

Life insurance premiums reached BRUR 149,4 (43,8% increase) in 2003. Claims exceeded premiums amounting BRUR 157,3 (15,5% growth). Still life business is mostly tax avoidance. Market leader was SSO (Stolichnoye Strakhovoye Obshestvo) – premiums over BRUR 33,7.

Top 10 life insurers collected 85,1% of premiums (79% in 2002) – BRUR 127,1.

**Table 17 Top 10 life insurers and foreign ones**

	<b>Company</b>	<b>Register Number</b>	<b>Premiums MRUR</b>	<b>Claims MRUR</b>	<b>Loss ratio (%)</b>
1	SSO	3258	33.734	24.128	71,5
2	URALSIB (Former Nikoil)	983	23.574	25.150	106,7
3	Classko	806	18.665	20.492	109,8
4	Yakor	1621	11.811	11.959	101,3
5	Doverie	428	10.451	10.049	96,2
6	NSG	1826	6.398	8.085	126,4
7	Russo-Garant	3417	6.357	6.697	105,3
8	Nadezhda Baltiki	1325	5.581	5.662	101,4
9	Standart-Reserv	1137	5.444	8.750	160,7
10	Komestra-Centr	949	5.079	3.981	78,4
15	Rosno	290	1.641	1.164	71,0
21	AIG Russia	3256	701	4	0,6
61	Ost-West Allianz	2294	67	10	15,2

(Source: VSS according to information from Minfin)

Personal insurance (except for life) – premiums reached a total of BRUR 41,5 (growth 29,4%) in 2003, while claims amounted to BRUR 24,9 (25,3% growth). The leader was ROSNO with collected premiums of BRUR 2,6. Top 10 insurers in the sector collected 39,3% of premiums or BRUR 16,3.

The most important lines here are personal accident insurance, medical insurance and travellers insurance. Medical insurance often is not a typical insurance at all, but just a convenient and cost-efficient way to receive medical services. Captive companies in the list of top 100 insurers have grown big especially via medical insurance and personal accident business.

**Table 18 Top 10 and foreign-related companies in personal insurance**

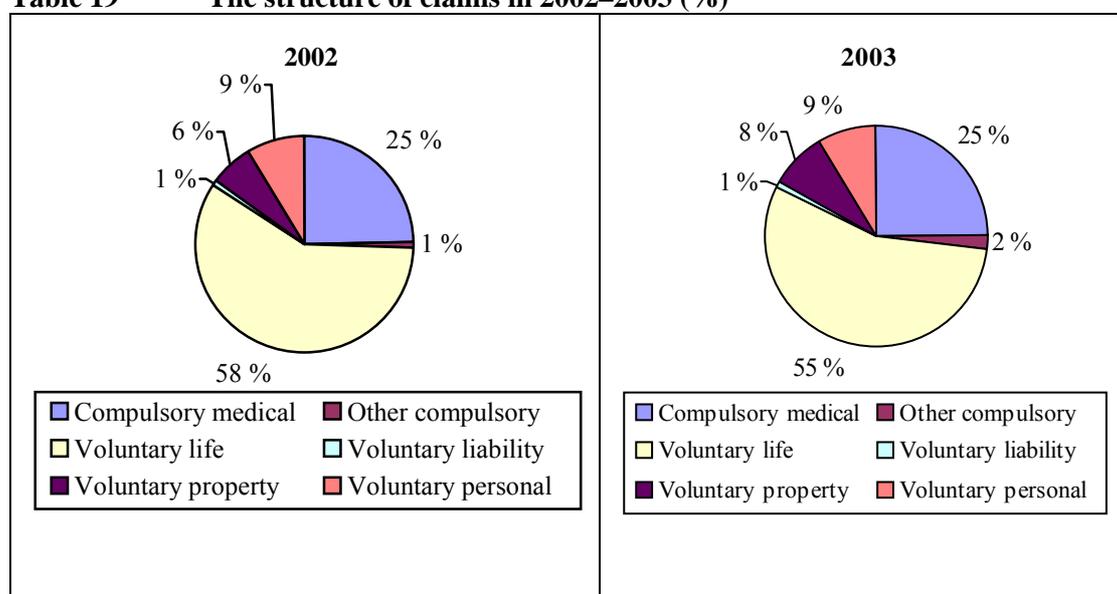
	<b>Company</b>	<b>Register Number</b>	<b>Premiums MRUR</b>	<b>Claims MRUR</b>	<b>Loss ratio (%)</b>
1	Rosno	290	2.628	1.484	56,5
2	Gazprommedstrakh	3230	2.523	2.229	88,4
3	Sogaz	1208	2.289	1.702	74,4
4	Maks (Moscow)	1427	2.182	1.546	70,9
5	Reso-Garantiya	1209	2.038	649	31,8
6	Zhaso	263	1.219	1.042	85,5
7	Ingosstrakh	928	1.112	486	43,7
8	Capital Strakhovaniye	1298	812	377	46,4
9	Renaissance Insurance	1284	785	258	32,8
10	Surgutneftegaz	3127	734	682	92,9
20	Aig Russia	3256	368	200	54,4

(Source: VSS according to information from Minfin)

The share of compulsory insurance (other than medical) increased, from 0,9% in 2002 to 6,8% in 2003. This growth took place mainly due to introduction of Compulsory Motor Third Party Liability Insurance in July 2003. Obviously, further growth of this sector will take place in the immediate future.

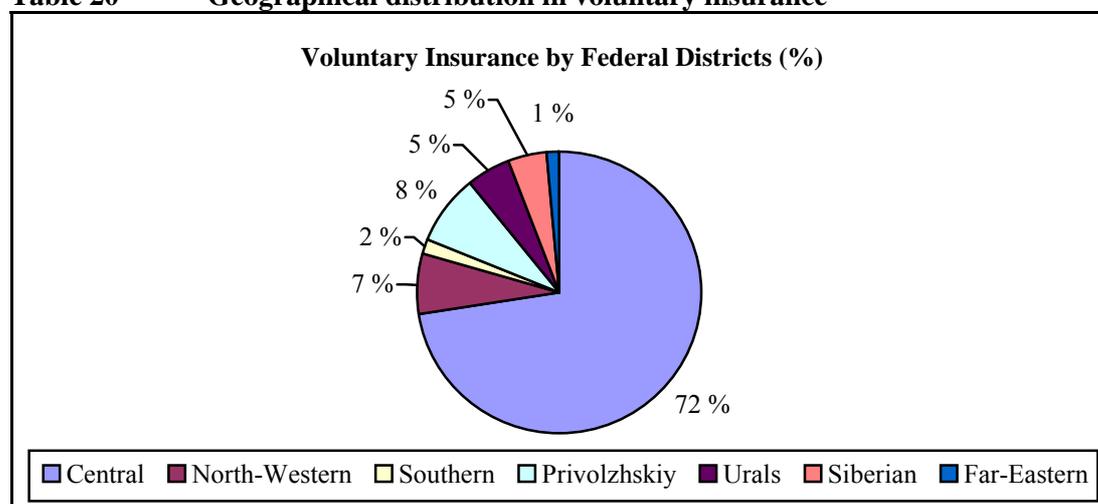
Major growth is expected in property insurance and liability insurance. Real life insurance is expected to grow, too, but statistics might show the opposite: real life business and tax avoidance are not separated in the statistics. Claims in 2003 were not growing as fast as premiums. Total claims paid in 2003 amounted to BRUR 284,5 (22,8% increase compared to 2002). The share of claims in voluntary insurance decreased from 74,5% in 2002 to 73,1% in 2003.

**Table 19 The structure of claims in 2002–2003 (%)**



(Source: Ministry of Finance of Russia)

**Table 20 Geographical distribution in voluntary insurance**



One of the most interesting features of the Russian transitional process is the uneven distribution of income, not only on the personal (household) level, but also on the regional level. In Moscow, the average living standard is about four times, and in St Petersburg about twice as high as the national equivalent. Thus, people living in these two metropolitan areas have essentially higher discretionary income (after paying taxes and necessities) than persons in the other regions (outside of the two metropolitan areas).

Obviously, discretionary income is the key factor in selling voluntary insurance policies. Persons who have no or very little income left after taxes, housing costs and groceries, have no option or limited interest to conclude voluntary insurance schemes.

Thus, it is no surprise that almost 80% of voluntary insurance premiums are collected in two regions (central and north-west), which contain those two metropolitan areas. Central district collects no less than 72% of the total premiums, over 90% of this huge share is written in Moscow. The northwestern district has a far more modest share of the national total (7%). More than two-thirds of this slice originate from the city of St. Petersburg. Similar picture can be observed in other districts: voluntary insurance arrangements are sold to rich city-dwellers in major urban centres.

In practice it means that insurance density outside the largest cities is very low, and thus, insurance companies are not very eager to go to locations with meagre discretionary income.

Compulsory insurance premiums were BRUR 102,9 (66,1% growth) in 2003, while claims were BRUR 76,4 (growth 29,2%).

**Table 21 Top 10 compulsory insurers**

	<b>Company</b>	<b>Register Number</b>	<b>Premiums MRUR</b>	<b>Claims MRUR</b>	<b>Loss ratio (%)</b>
1	Maks-M	2226	8.090	7.636	94,4
2	Rosno-Ms	2890	5.386	5.514	102,4
3	Skpo	3014	2.610	1.864	71,4
4	Military Insurance	621	2.304	1.769	76,8
5	Reso-Garantiya	1209	2.197	130	5,9
6	Skpo-Med	2326	1.991	1.933	97,1
7	Spasskiye Vorota-M	2354	1.966	1.961	99,7
8	Solidarnost Dlya Zhizni	257	1.941	1.829	94,3
9	Kuzbass	1965	1.571	1.519	96,7
10	Gsmk	2071	1.549	1.484	95,8

(Source: VSS according to information from Minfin)

Compulsory medical insurance remained the most important part of the sector with BRUR 73,6 of premiums (growth 24,8%). Claims amounted to BRUR 71,3 (growth 25,1%) in 2003. As a matter of fact, compulsory medical insurance is more related to social security than insurance. The total volume of market depends only of total volume of legal salaries. Companies can compete (and only in very narrow limits) only for a share of market but they cannot influence the overall volume premiums within a region or the country as a whole. From Top 10 table it is easy to find compulsory medical insurers by loss ratio about 100%.

CMTPL appeared only in the middle of 2003, and thus, no comparison with 2002 can be given. It is also important that most of sales were made in the end of the year, thus claims were low in 2003, but show a growing tendency.

The main reason for underdevelopment of real life insurance sector is the low interest of both insurers and clients in this activity. Firstly, potential clients are unaware of the services and products available. Secondly, the general economic uncertainty keeps insurers and clients away from long-term schemes.

Rosgosstrakh representatives expect strong growth of 50–60% in the sector in 2004. Number of insured people will increase by 15–20%. Rosgosstrakh estimates that the total amount of savings in Russia increased from BUSD 48 in 1996 to BUSD 103 in 2002.

This estimation hints on an increasing propensity to save in Russia, which is good news for the insurance business. However, it is rather difficult to predict, whether the population under present circumstances is ready to commit to long-term saving arrangements. Probably, liquid forms of savings will be preferred. Comparing returns of long-term investment with availability of funds is a new difficult element in the everyday life of post-Soviet citizens.

There is compulsory liability insurance for dangerous production units. Limits of indemnity are modest. According to information of VSS volume growth in this sector was only 9% in 2003 and the total premium volume reached BRUR 3,6.

The leaders of the market in this insurance line are Soglasiye, MAKS, SOGAZ, Surgutneftegaz, Uralsib, Ingosstrakh, ROSNO, NSG, Choulpan and Neftepolis. It is important to mention that the big ones (four from ten) in this sector are captives of big industrial holdings (mostly oil and gas).

Due to fixed rates and stable number of potential objects there is no noticeable growth to be expected in the sphere of dangerous production units. Draft of the new Law in respect of this insurance matter contains provisions about guarantee fund and certain extension of limits of indemnity. This segment is not able to play an important role in the overall business of insurers. Only a handful of companies is active in this sphere.

In July–December 2003 Russian Insurers issued 12,9 million policies of Compulsory Motor Third Party Liability (CMTPL). The Law on CMTPL came into force July 1, 2003. This law and reform in Russian insurance industry is one of the most important ones so far. The Government approved tariffs in May 2003. Penalties to uninsured cars have been charged since January 1, 2004.

According to the CMTPL Law in August 2002, All-Russian Union of Motor Insurers (RSA) has been established. Membership in RSA is inevitable (according to the Law) for obtaining license for CMTPL. Currently, there are 174 members, but only 156 of them have obtained a license.

Decision-making in this legal issue caused chaos on the market in 2003. Potential policyholders decided to wait as long as possible. Thus, the sales of policies in October–November dropped down significantly. It resulted in excessive demand in late December–January (2004) when people hurried up to buy a policy to avoid penalties. Such a situation forced clients to buy policies without really choosing the company. The main criterion to buy was availability of company's sales office. At the same time the share of false policies has been reported to reach 3% of the total number.

Altogether 148 insurance companies provided reports on their results in CTMPL. Premiums reached BRUR 24,83 in 2003. According to information of RSA, 12,9 million policies were issued in July–December 2003. Number of policies and amount of premiums in the 4<sup>th</sup> quarter exceeded results of the 3<sup>rd</sup> quarter by 1,6 times. Most of the 8 million policies sold in the 4<sup>th</sup> quarter were issued within two last weeks of December. Average price of one policy in Russia was RUR 1.922.

BRUR 1,2 of indemnities were paid during the second half of 2003 and 5/6 of this amount were paid in the 4<sup>th</sup> quarter. In 2004, all Federal Governmental organizations have budgeted resources for CMTPL. Interfax (Russian Information Agency) estimates that Federal Government will spend about 3,5 BRUR to CMTPL insurances for governmental vehicles.

Despite a sceptical attitude against CMTPL, the majority of car-owners have purchased policies. Still some of them decided to avoid it as long as possible.

In late January 2004, VCIOM 8 (Russian opinion poll company) interviewed 1.600 Russians. 36% of them declared that they had cars. 68% of the car-owners had insurance policies. 30% acquired policies in July–mid December, 24% did it within the end of December, 14% in January. 20% of the car-owners were not insured, but were planning to buy policies, but 5% decided not to do it at all.

The main reason for refusal was the price of the policy. Respondents from this group said that they had financial problems and couldn't afford buying insurance. Another reason for refusal was the attitude (unwillingness to obey orders).

VCIOM reported that only 13% of respondents supported the Law as it is. 23% agreed with the idea of CMTPL, but they wanted the Law to be changed, 17% rejected the idea of CMTPL and 40% (probably most of them were pedestrians) did not have any opinion on the subject.

10 insurance companies collected over 70% of CMTPL premiums in 2003. 10 leaders sold 9,62 million policies and collected BRUR 17,64 in premiums. Claims paid by these top 10 companies in July–December exceeded MRUR 821,3. All of the leaders are Moscow-based, but some of them collect major part of premiums outside Moscow (for example Rosgosstrakh, SKPO). Most insurance companies expect that loss ratio will reach its peak in 2 years after the introduction of the system.

From July 2003, Rosgosstrakh (including all subsidiaries) has been the leader of the CMTPL market with the share of over 50%. In 2003, it sold 6,3 million policies and collected BRUR 9,3 of premiums.

Since February 2004, rumours about changes in tariffs have been circulating on the market. Russian insurers are concerned that this topic will appear in Russian Duma. Some insurers already announced that they are going to quit the market in case of substantial decrease in tariffs. Some are ready to continue even if the prices will be 15–20% lower. It is important to notice that CMTPL has very costly infrastructure to be paid by insurers. Thus, the difference between loss ratio and combined ratio is high.

In spring 2004, Ministry of Finance proposed the system of day-off insurance. There are many unsettled problems left in the Law and in tariffs approved by the Government. One of the crucial problems is bonus-malus system. The description of the system is so incomplete, that it is very easy to avoid paying extra premium in case of a bad loss record. Another problem is that RSA has not launched the information system. Thus, companies have no possibility to check information if the client changes the company.

It is expected that about 1,5–1,6 million new cars will be sold in 2004. New cars, especially imported ones, create major part of the demand for motor hull insurance. As motor transport is actively renewed in Russia, obviously this sector of insurance will keep developing in the future. Expenditures for private motor (hull) insurance are likely to exceed BUSD 1 in 2004.

In 2003, Russians spent BUSD 4,0 for purchasing Russian cars and about BUSD 4,7 for purchasing new foreign cars. 195.700 new imported cars were sold in Russia in 2003, in comparison to 111.300 in 2002. Premium volumes doubled in this sector and claims grew 1,5 times in 2003. Number of policies issued increased by 90%. Motor insurance plays an important role in portfolios of most of insurers involved in real business.

Corporate motor insurance increased by 33%, claims by 38% and number of policies by 60% in 2003. It is important, that average sums involved increased almost 3 times. Introduction of CMTPL made a positive shift in the market, as potential clients were forced to get acquainted with the service.

General economic growth increases transport operations both domestically and internationally. Experts expect growth in transport turnover of 25% in 2004. Cargo insurance is expected to grow respectively or even faster.

One of the obstacles in cargo insurance is the high share of illicit operations:

- Imported goods are often declared much cheaper than their real value. Thus, it is not possible to show the real value in insurance policies.
- Unregistered carriers often carry Russian domestic motor transport. Official cargo documents are often missing or contain false information. Thus, it is difficult to claim dishonest carrier in case of his fault.

The leaders of the cargo insurance segment are Soglasiye, Ingosstrakh, SSO, Uralsib, MSC, Oranta, Rossiya, Pari, Neftepolis and Metropolis.

According to information of VSS<sup>8</sup>, aviation market showed 15% growth in 2003. Development of leasing operations and improvement of the aviation park allows to expect growth to continue in 2004. According to VSS estimation growth will reach 20–25%. As the prospects of aviation industry are promising, prognosis for aviation insurance is positive.

Number of aviation policies issued in 2003 increased 1,5 times. The leaders in this sphere are Ingosstrakh, Uralsib, Guta-Strakhovaniye, ROSNO, SOGAZ, BASK, Soglasie, SSO, MAKS, Spectr-Avia S and Surgutneftegaz.

The information from insurance companies shows that the number of insured small private aircrafts increased sufficiently, but the share of this segment in the whole aviation sector is still miserable (0,3%).

The emerging insurance market of Russia has created the need of brokerage in this sector. As mentioned above, no licence is required for broker operations. After July 1, 2005 all the brokers have to obtain a license. Qualification requirements will be introduced for general managers and chief accountants of insurance brokers. General manager of the insurance broker should have higher education in economics or finance and have at least 2 years experience in insurance or finance<sup>9</sup>. Chief accountant should have at least 2 years experience in accounting.<sup>10</sup> General managers and chief accountants of insurance brokers should be Russian citizens.

One quite problematic change has been made in the definition of the insurance broker. Earlier the broker could act as a representative of insurer or insured. The new rule does not allow brokers to act on behalf of insurers. Now such activity is specified as agency activity and prohibited to brokers. It is important to notice that in Russia the practice (due to legislation gaps) has so far been that clients pay premiums directly to insurance companies and insurers transfer commission to brokers afterwards.

According to the information of VSS, the number of insurance agents increased by 30% in 2003. Some experts expect a further growth in 2004. The new situation with CMTPL in the end of 2003–January 2004, inspired some companies to hire agents just to cope with very strong growth of the amount of clients.

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<sup>8</sup> VSS (All-Russia Insurance Association) – Annual Report 2004

<sup>9</sup> Federal Law No 4015-1, Article 32.1, paragraph 1,

<sup>10</sup> Federal Law No 4015-1, Article 32.1, paragraph 3

In 2004, insurers will have more time to serve these clients and pure CMTPL agents will be converted to full-service agents. Anyhow, many of them will probably quit insurance business. Total number of agents in 2003 was estimated to be about 105.000–110.000.

Rosgosstrakh possesses the network of 40 thousand individual agents. Ten thousand of them are employed especially for CMTPL. Still many agents are working like wild brokers selling services of several companies, finding the best solutions to the clients. Main potential for the growth of agency networks is the growth of private clients segment in insurance. The turnover in this sector increased 4 times within 3 years.

### **4.3. Russian insurance market**

#### **4.3.1. Russian reinsurance market**

There are three (3) main groups of providers of reinsurance capacity on the Russian market:

- a) Foreign reinsurance companies;
- b) Russian reinsurance companies;
- c) Russian direct insurance companies writing inward reinsurance.

The main foreign players in the Russian reinsurance market are: Munich Re, Swiss Re, Hannover Re, General & Cologne Re, SCOR, Riga Re. Some other reinsurers (including Lloyds) also do write business from Russia, but only via brokers. Major brokers placing such risks are Marsh, AON, Willis Faber and Dumas Limited (WFD), Heath and Lambert, Oakshott. Some others are also present but not in such volumes (for example Harris&Dixon and Rifams).

The main benefits (except Riga Re) of working with foreign reinsurance partners are:

1. Capacity to write the business
2. Experience and skills
3. Solvency questions to carry the risks
4. Reputation

The drawbacks are:

1. Absence of reciprocity (that is very important for majority of the insurers)
2. Language barrier (not for all companies, but at least for many)
3. Cross border operations mean that some additional work has to be done
4. Extremely selective policy of foreign reinsurance companies facultative business (by lines and size of risks)

According to the records in the State Register of the Insurers there are 45 specialised reinsurance companies registered in Russia but much less are really active in the market.

The major Russian companies are:

1. Russian Re
2. Transsib Re
3. Capital Re
4. Moskva Re
5. National Re

Russian Re is the one and only reinsurance company with noticeable participation of foreign insurance capital (Marsh and AIG).

The well-known businessman and millionaire Mr Kaha Bendukidze acquired Moskva Re. He is presently The Minister of Economy of Georgia. Mr. Bendukidze got his share from Moskva Re when the company issued additional shares. By this capital injection into Moskva Re, its charter capital raised significantly.

Small treaties and facultative covers are not interesting for big foreign reinsurers. Anyhow, they are eager to write the same risks, if risks are in a package and they are able to do it on non-proportional (facultative and excess of loss) basis.

Reinsurance between Russian direct insurance companies is popular mostly because of reciprocity reasons.

Two (2) main alterations were made in the new version of the Law on Insurance (17.01.2004) that relate to Russian reinsurance practice.

Separate licence is needed for reinsurance in Russia. Until January 17, 2004 the license for reinsurance was needed only for specialised reinsurance companies that had no other insurance license. All other insurers were authorised to write inward reinsurance (their license for direct insurance was enough). Since January 17, 2004 all direct companies willing to write inward reinsurance have to get a separate license for that.

The new version of the Law on Insurance prohibits writing property reinsurance in case the company possesses a licence for direct life insurance. Over 800 insurers lost the right to accept risks linked with reinsurance. In June 2004, insurance lobby in Duma managed to convince the deputies to make an amendment to this article making it valid from July 1, 2007 – the deadline for separation of direct life and non-life portfolios.

These two novelties were introduced with quite a big uncertainty. There is no direct statement in the law that a separate license is needed for reinsurance, only some indirect references concerning licensing procedure. Thus, it is not clear to the companies if they should apply for a license or not. The Supervisor made the situation even more complicated by publishing the list of over 800 companies that lost the right to write reinsurance business, as they possessed life insurance licenses. In such circumstances the insurers made the conclusion that those who have no license for life insurance can go on with reinsurance. The Supervisor made an official comment that the license for reinsurance is needed for direct insurers willing to combine it with reinsurance. The insurance market was disoriented. Many companies, who had life license but no life business appealed to the Supervisor for cancellation of their life licenses. Many companies were willing to get reinsurance license, but there was no clear procedure for that. That is a typical example of how Russian legislation works. The law itself is unclear and the supervisory authority has the possibility to choose whatever position it prefers.

The magnitude of the reinsurance business is difficult to analyse because of lack of official information from supervision or from the insurance companies directly. The role of Russian life insurance companies and their actions between each other make it complicated to evaluate the real reinsurance business and the game around tax avoidance schemes.

However, an estimation of reinsurance business in 2002 can be made. The total premiums in 2002 were BRUR 16,1 of which 82% was life insurance treaties. Motor insurance share was 10%, and the rest was 8%. These numbers are calculated separately in the Supervision office and are not official data.

**Table 22 Premiums and claims of reinsurance specialized companies 2002**

	Company	Premiums MRUR	Claims MRUR
1	Nadezhda Re	6.479,6	328,3
2	Industrial Re" (currently Capital Re)	3.627,6	515,7
3	Universe Re	934,3	79,6
4	Transsib Re	826,6	111,5
5	Universalnoye Re	782,4	0
6	Express Re	552,7	2,4
7	Russian Re	491,1	201,1
8	ROSNO – Centr	482,9	10,0
9	Moskva Re	395,9	150,0
10	Nevskoe RE	262,0	0
11	Noviye Technologii Re	246,6	0,6
12	United Re	246,1	0,1
13	Maggelan In&Re	195,9	0
14	Mikora Re	171,2	0
15	Nakhodka Re	105,1	88,7
	Top 15	15.800,0	1.488,0
	Total	16.101,0	1.584,6

(Source: Ministry of Finance)

**Table 23 Direct insurance Companies on Reinsurance market 2002**

	Company	Reinsurance premiums written (MRUR)	Premiums (ceded) to reinsurers (MRUR)
1	Ingosstrakh	2.786,1	3.475,9
2	Alpha Strakhovanie	1.184,3	1.472,7
3	ROSNO	1.065,6	2.899,2
4	Rosgosstrakh	834,4	698,8
5	Uralsib (former Nikoil and PSK)	671,4	207,7
6	Soglasiyе"	544,4	5.547,9
7	SSO"	337,1	624,4
8	ASOPO	157,2	161,3
9	Oranta	153,0	197,8
10	NASTA-centr	119,8	861,8
11	MAKS	114,1	256,6
12	Rossiya	55,3	533,5

(Source: VSS (All-Russia insurance Association))

For the year 2003, Moskva Re estimates that the total reinsurance premium is BRUR 4,0. This sum is cleaned from tax avoidance schemes, which are still the main part of the business. 60% of total is from local reinsurers (insurance and reinsurance companies).

#### 4.3.2. Russian insurance market in international comparison

In the mature markets of the industrialized world, the insurance market is huge business that is facing a high level of saturation. This business is getting more and more international which

means that there are less and less players. Remaining companies must have a reasonable size with economies of scale. The mature markets have been unable to dismantle business cycles. Thus, there are fluctuations in insurance business in the rich part of the world.

In the group of countries called the emerging markets there is still plenty of space for growth in the insurance business. Therefore, all established insurance companies have interest in the emerging markets, a part of which is Russia.

It is possible to draw a rough picture of the differences between the mature markets in the West and the emerging markets in insurance branch by using two countries, Finland, belonging into the first group, and Russia, as a part of the second. In 2003, insurance premiums paid in Finland per capita were about USD 612 in the non-life sector. The equivalent sum in Russia was about USD 63, or roughly one tenth of the Finnish one. In the life insurance branch, the per capita amount in Finland was (2003) about USD 2213, while the equivalent in Russia was about USD 33. The first amount is about 66 times higher than the second one. The difference is striking.

In these comparisons it is useful to bear in mind that Finland is a typical Nordic welfare state with heavy public sector involvement in social safety net. Thus, Finland is not an ideal country from the point of view of selling private insurance policies.

As Table 24 below shows, industrialised countries had an annual growth of almost 6% in non-life insurance business in 2003. At the same time, the life-section declined by almost 2%. Emerging markets booked rather high growth rates in both categories.

**Table 24 Real insurance premium growth in 2003 (%)**

	<b>Life</b>	<b>Non-life</b>
Industrial countries	- 1,7	+ 5,7
Emerging markets (total)	+ 6,6	+ 8,5
Total	- 0,8	+ 6,0

(Source: Swiss-Re Sigma 2003)

The emerging markets' registered growth is below their long-term average. However, growth rates varied considerably between the individual regions and markets. Transitional economies (including Russia) had very high growth rates in 2003.

The strong premium growth in Russia reflects economic recovery and positive development. However, due to tax avoidance schemes and booming grey area in Russian economy, the growth rates contain some biases. However, insurance market in Russia is relatively modest.

**Table 25 Comparison of gross premiums in selected countries, 2003 (MUSD)**

	Gross Premiums Written	
	Non-life	Life
Russia	9.220	4.868
UK	91.891	154.842
France	58.244	105.436
Finland	3.058	11.065
Poland	3.946	2.312

(Source: Swiss Re Sigma 2003)

In the Western system, insurance industry is regulated and monitored strictly by authorities who act to follow both policyholders and insurers. In Russia this system is not yet perfect. The loopholes in the system are used not only in positive ways. The latest events in legislation and Supervisory body hopefully improve the situation from everybody's (policyholders and insurers) point of view.

Even after the new capital requirements to Russian insurance companies, the reserve level is not adequate enough to establish an environment where Russian insurance companies are able to act like real risk carriers. Fortunately these requirements represent a minimum and many real players do have their capital much above these requirements. Anyhow, reinsurance schemes and support of international reinsurance companies are essential to Russian insurance industry at the moment. Reinsurance arrangements between Russian direct insurers are not always very reliable.

Investment instruments of the Russian companies are not very attractive. It is not easy to have a stable and reliable investment portfolio in the long run. Insurance companies have their own investment regulations and guidelines, which may cause problems.

Insurance business segments in Russia differ from the Western ones. The main clients of Russian insurers are foreign related companies in Russia, Russian biggest enterprises, and certain parts of the public sector administration.

An average private household clientele, in the Western sense, is almost missing. Generally, a Russian citizen is not aware of insurance philosophy. Living standard is not high enough to

enable citizens to spend very much in insurance. The lack of confidence to Russian financial institutes after the crisis in 1998 is understandable.

Before the economic crisis of 1998, there was an embryo of Russian middle class. In 1998 and 1999, this class was badly hurt. The middle class is normally one of the foundations of successful insurance business. As mentioned earlier, the new CMTPL Insurance is one of the biggest and most important steps forward in Russian insurance industry. Now the private persons are in a way forced to learn insurance and its philosophy. A big file of personal particulars will arrive because of this compulsory insurance line. This data can be exploited for marketing purposes when other insurance products are sold to individuals.

Insurance product development has been very exciting during the past years. Thus, now almost all the needed insurance products are available (this is of course related to Russian business environment) to finance business risks in Russia.

In the post-Soviet era, an extremely important learning process has taken place. The insurance branch, which in its modern form was entirely alien during communism, has accumulated plenty of experience and skill comprising theoretical and practical elements. Thus, insurance companies active in the Russian market can rather easily find suitable persons for all positions in the branch. In this sense, the post-Soviet Russia has integrated herself very well into the global economy.

## 5. Prospects of the Insurance Industry

Most of the Russian insurance experts expect substantial growth in Russian insurance sector. For example, Alex Bertolotti, a partner of Moscow office of PriceWaterhouseCoopers said that he expects that GPW (Gross Premium Written) in Russia will reach BUSD 200 in 5–10 years<sup>11</sup> (14,1 BUSD in 2003). Mr. Bertelotti is not the only one who has announced the same type of forecasts. There are several Russian insurance companies' representatives, who have announced similar positive forecasts.

There are several reasons for optimism regarding Russian socio-economic development. President Putin was re-elected in 2004 to serve a second four-year-period. His supporters have a clear majority in the parliament. Thus, conflicts between the presidential office and Duma, which were permanent in the 1990's, are unlikely to occur.

Mr. Putin has become a symbol of stability after the stormy years of Mr. Yeltsin's rule. The new stability contains many authoritarian features. Many Western observers are worried about limitations in e.g. freedom of press.

In the sphere of economics, immediate prospects are very good, because the world market price of oil is on new record level. Over 50% of Russian export consists of fossil energy (oil and gas). Thus, annual real growth rates of GDP are likely to be about 6–7%.

In the Putin era, Russia has successfully stabilized her economy. In the aftermath of the 1998 Rouble crisis, the state has achieved continuous surpluses in her budget, which is an excellent result in comparison to permanent deficits in the pre-crisis period. In addition, the state has established a reserve fund from her oil income. This reserve can be used to even out business cycles, if there is a sudden decline of oil income.

Inflation is much better under control than in the 1990's. However, in international comparison price increases (of over 10% annually) are still relatively high. Incentives to save have thus improved, but further positive results in fighting inflation are needed. Financial institutions do not yet enjoy unlimited trust among population.

Obviously, the very serious conflict in Chechnya is not yet over igniting extensive terrorism. Controlling regions in Caucasus has become a long-lasting issue.

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<sup>11</sup> Interfax

The Yukos affair has created a lot of uncertainty on the financial markets affecting the investment climate. It is difficult to judge, in how far the Yukos case has influenced investment decisions among potential foreign investors. In October 2004, Conoco oil company (US) bought a BUSD 2 stake of LUKOIL, the leading Russian oil giant. This large deal is mentioned in the international financial press as a herald of post-Yukos era: multinational companies regard Russian risk worth taking. Obviously, it is assumed that Yukos remains a unique incident in the history of Russian transition.

In sum, the general framework of the Russian society offers good prospects for the insurance sector to flourish. The branch-specific framework is still far from perfect, even if the latest improvements in the legislation are judged positively above.

In all industrial societies of the West, one of the most important tools of the capital formation is the insurance branch. Thus, it is in the interest of the Russian state to develop this tool of wealth creation in her transitional phase.

The state can extend compulsory insurance schemes, and thus, force the population to save. In this case, the public sector allocates risks and risk management to citizens. An obvious alternative is that the state increases taxes (to cover, for example, all health care costs) which is nothing else but forced saving.

One option the state has (in Russia and elsewhere) is to give tax incentives for insurance policy-takers. For example, in Finland voluntary old-age pension schemes contain tax advantages. Thus, the state can use direct and indirect methods to advance the insurance sector, the success of which is essential in growing investable capital.

On the other side of the scale is the population, a big part of which is not familiar with the insurance philosophy. Many citizens cannot see potential benefits in taking insurance policies, which are often perceived as tricks of dishonest financial moguls. The recent economic history of Russia has contributed to this existing distrust.

Thus, insurance companies in Russia have a double task: they must lobby the state to improve the institutional framework, and at the same time, they must improve their own image by paying attention to their own information policy. This means increasing marketing costs.

From the point of view of insurance companies, demographic trends are important. The Russian population in the transitional period has decreased permanently, even if there has been net immigration from the other former Soviet republics. Thus, the death rate has far exceeded the birth rate.

The life expectancy of male persons is in Russia about 60 years, which in international comparison is an extremely low figure. This figure was relatively low already in the last years of the Soviet power, but decreased in the early period of transition. One of the background factors is the collapse of the health care system.

In the meantime, compulsory medical insurance (CMI) scheme was introduced, which, however, can only finance about one third of the medical services. The CMI system ought to be revised and modernised. Obviously, there is also some potential for voluntary medical insurance, which clearly can only be aimed at the wealthy part of the population.

Minister of Health and Social Development, Mikhail Zubanov, suggested some time ago that insurance companies might be allowed to participate in the statutory pension system after 2005. This idea was supported by Mr. Lomakin-Rumyantsev (the head of the insurance supervision), but he pointed out that it is only possible when real life insurers start emerging in Russia. The obvious aim of officials is to root out tax evasion schemes from the life insurance business and make this branch transparent. He also says that granting tax benefits to insurance business depends upon openness and honesty of the companies.

According to valid Russian bookkeeping rules companies can only deduct a minor part of their voluntary insurance expenses from taxes (two per cent of the turnover). Therefore, voluntary medical insurance is only a rarity concerning some large local or foreign owned companies, which cover their employees by this method. Individuals have no tax reduction options from any insurance policies they take. Tax relief for voluntary pension schemes would obviously be a good business from the point of view of the state, which struggles to fulfil her pension obligations.

In the early period of post-Soviet time, the big bulk of housing stock was privatised. About 60% of the population live in their own flats or houses. At the same time, the state transferred the housing stock remaining in public sector ownership to municipalities.

According to a study by ECE (Economic Committee of Energy), the housing stock in general is in a very bad shape and deteriorating because of lack of maintenance. In the multi-store

buildings, individuals normally own separate flats, but the rest of the building (common space) is not owned by anybody. Therefore, maintenance is a very serious problem.

In Finland, flat owners normally belong to a shareholding company which insures and repairs the building. This system in USA is called condominium.

Equivalent system has come up in Russia in very few cases. With this method there is a shared responsibility concerning the whole building. In most cases households own the flats, while roofs, lifts etc. are not owned by anybody.

The Civil Code of Russia doesn't oblige property owner to insure the property. If somebody rents a flat on the free market, he/she is forced by law to insure the rented property to the benefit of the landlord, who cannot be legally forced to insure his own property.

Russian municipalities have a huge housing stock in their hands, but obviously no special funds to maintain that massive piece of property. Also in this case new solutions, for example, compulsory insurance schemes, ought to be created.

Obviously, wealthy citizens with new houses and weekend cottages can take a voluntary insurance. Packages covering several pieces of property are on offer. House mortgage market is in its infancy. However, mortgage schemes have become available. This branch naturally offers new business opportunities for insurance companies who can create protection to collateral property.

Undoubtedly, the insurance sector in Russia faces new challenges, during which considerable restructuring and consolidation cannot be avoided. It is expected that at least half of Russian insurance companies, which existed at the beginning of 2004, will not be able to cope with the new capital requirements and disappear within three years. In the first half of 2004, no less than 142 insurers lost their license after being unable to increase the capital to the required level.

It is highly likely that the biggest Russian companies will start an acquisition spree and swallow numerous small ones. It can be assumed that an oligopolistic market with a few big units covering the entire territory, or at least the most important industrial centres, will emerge. Moscow will self-evidently be the centre of the Russian insurance business.

It can be assumed that foreign insurers will not expand their operations rapidly on the Russian market. Big international players are mainly interested in large industrial risks. Retail business is only attractive in the two metropolitan areas. Creating national networks is costly under circumstances of high uncertainty. Rules to invest mainly or entirely in Russia are not very attractive from the portfolio income point of view.

As mentioned above, the foreign involvement in insurance sector is not supposed to exceed 25% of the total assets. This new ceiling is obviously without substance, because the foreign involvement is far away from this set limit.

The destiny of re-insurance business is highly interesting. It is evident that Russian primary insurers are not able to carry risks they have taken without reinsurance cover. Russian domestic reinsurance companies are not necessarily strong enough to carry high risks from their own portfolios. Thus, Russian reinsurers have reinsured their portfolios abroad.

The capital outflow taking place in this context is obviously disliked by Russian officials. There are clear signs that rules concerning reinsurance business will be modified, in order to limit the monetary outflow.

Obviously, rules can be changed. However, modified rules can hardly reduce risks. Thus, in the worst-case scenario, Russian insurance market will carry risks that are over and above its capability. Therefore, it is important to find a compromise, which takes overall risks and the local content of insurance business carefully into consideration.

Previous version of the Law on Insurance contained a possibility to establish mutual insurance companies. However, precise stipulations concerning them were not announced. New edition gives the reference to a special Law on Mutual Insurance Companies. However, not even a draft of such a law is known to be in process. There is a small probability that it might appear in the nearest few years.

In voluntary Motor Car Insurance certain development is expected. There is a lot of competition, rates margins are low and costs are high. More and more new cars are insured, but still old cars occupy a big share of Russian transport fleet. Obviously, such old cars are not attractive for insurers.

Cargo is likely to show gradual growth, which is mostly related to general economic (and trade operations) growth. Transfer of operations from grey area to legal sector has a self-

evident influence on growth in cargo. When it comes to either aviation or marine hull, development of the sector strongly depends on Russian aircraft and ship owners' ability to replace old units by new ones. Currently the share of very old aircrafts and vessels in Russia is very high. Certain part of new units might be insured abroad (for example, in case the nominal owner is a foreign one, leasing company etc.).

General liability and product liability become more and more popular. Still their importance in overall turnover of insurance industry will be low in the nearest future until the year 2007.

Professional indemnity (voluntary professional indemnity insurance) is not widespread. Poor or missing legal practice cannot stimulate development of that sector.

Employer liability insurance is a missing class in Russia. It can be expected that in the long run this product can partly replace corporate accident insurance or even become compulsory. Still, no crucial development can be expected in the nearest couple of years.

As shown above, there is a clear consolidation of the Russian insurance market taking place. Big companies will acquire smaller ones. The winners of this process will have a reasonable capital base to cope with the growing and obviously also more diversified market. It will be interesting to observe, whether foreign companies will get a bigger share of the future insurance sector in Russia. So far, the foreign involvement in the business under review has been very modest indeed.

The tendency is to separate various business lines (life and non-life, reinsurance segments) in the Russian insurance business. Therefore, it is likely that the insurance companies will be somehow specialized on different production lines of the branch.

## 6. Conclusions

Insurance business is a two-way road. Companies involved take in money (savings) and invest a big part of that sum. Thus, insurance companies have extremely important macro-economic functions (in capital formation: insurance premiums paid in enhance overall saving.) At the same time, insurance companies provide capital to the local economy by investing a big part of the money collected from clients.

One of the basic rules of the market economy is that the higher the risk of your investment, the higher your return is supposed to be. Obviously, insurance companies must be able to meet the claims of their clients. If all the income is invested in high-risk investments, the result may be insolvency. Thus, insurance companies are not supposed to be venture capitalists. There are good reasons to regulate somehow the insurance branch.

In every market economy, there is the danger of the so-called snowball effect. Mr X saves money and deposits it in a bank. The bank buys shares of a company that collapses. Suppliers of that company go bust. A negative spiral starts spinning: the snowball grows when rolling down. That is exactly what happened in the US economy in the 1930s causing a global depression.

In the early period of Russian transition, thousands of financial institutions came into being. Many of them are now solid companies with accumulated capital and sound business strategy. However, thousands of them just disappeared after a short period of time, or went bust during the devaluation crisis. A multitude of individuals and firms lost money in this context. Thus, it is understandable that a big part of the population is reluctant to use services of any financial institution voluntarily.

The first President of the post-Soviet Russia, Boris Yeltsin, became a symbol of instability in the second half of the 1990s. His administration was not able to deal with public sector finances, in which high deficits were covered by selling government bonds in a massive scale. Amid the economic crisis, the state defaulted her internal debt and rescheduled her international obligations. Obviously, there were catastrophic losses for many investors who had stakes in the bond market.

In the turn of the century, Yeltsin was replaced by Vladimir Putin, who virtually immediately became a symbol of stability. Mr Putin, who serves his second term as a President, has a solid support in the Parliament (Duma) for his policies.

In the post-devaluation era, the world market price of oil increased essentially (in 2000) staying on high or even on a very high level. More than half of Russian export is oil and gas, and thus, the country has been able to receive windfall profits on the world energy market. In the aftermath of the Rouble crisis a strong and so far sustainable economic growth has taken place.

Amid this boom, investment started increasing in real terms. High oil price and the realistic exchange rate are the most important background factors of the booming economy. Import-substituting activities have become profitable after 1998. Furthermore, strong economic boom in China creates demand in Russian basic industries, like metallurgy.

In the context of economic development, it is important to consider the level of living standard which is in Russia about one third of the average in the Western Europe (calculated on the basis of GDP per capita and purchasing power parity adjusted). Thus, Russia is still far away from the level of Western welfare states. Life insurance premiums paid in Finland annually are many times higher than in Russia calculated per capita. The equivalent difference in non-life segment is ten times.

Income in Russia is very unevenly distributed. It is estimated that about one fourth of the population lives in poverty. At the same time, Russian oligarchs can be found among the richest people in the world. Moscow has a living standard roughly four times higher than Russia in average. Inequality is thus obvious on the personal, as well as local level.

It is self-evident, that the Russian public sector cannot extract tax income in the same manner as Scandinavian welfare states with high living standard. Therefore, parts of the social safety net must be organised via insurance business concerning, e.g., health care. It is thus highly likely that more and more compulsory insurance policy schemes are in the pipeline.

Increasing living standard in Russia takes visible forms: the stock of cars and new houses has expanded rapidly. A new middle class is obviously emerging with valuable belongings worth to be insured not only on compulsory, but also voluntary basis. This enhances the chances of the insurance branch to grow rapidly.

It was pointed out above that Russian insurance companies invest a big bulk of the overall portfolio in the enterprise sector by buying bonds and giving credits. Equity investment (collecting shares of companies) is also important. However, the share of equities in the insurers' portfolio is only about one fifth. State securities (bonds, treasury bills) are not accumulated in large quantities by insurers (only 3,3% of overall portfolio). The reason is clear: in the late 1990s, the state did not meet her obligations. On the long run, the popularity of state papers in the insurers' investment decisions is likely to increase.

Under present circumstances, sustainable economic growth combined with relative political stability is of utmost importance for all insurance companies in Russia. Obviously, insurers are not looking for the highest possible risks in their investment activity. Spreading the risks in a relatively conservative manner is essential.

In this respect, the overall situation is rather favourable: the predictability of the Russian socio-economic situation is fundamentally better than in the late 1990s. The state budget has shown a yearly surplus for several years. Inflation rates are still higher than in the West, but price increases are not out of control. In many industrial branches, consolidation takes place. Institutional changes advance, not necessarily fast, but in the right direction. The business climate is getting brighter.

In this respect Russia is not in the same situation, as transitional economies in Central Eastern Europe, which were forced to mend their institutional frames rapidly amid EU-membership negotiations. Eight of them managed to join the Union in May 2004.

Russia has declared the aim to become a member of the World Trade Organisation (WTO) in the near future. In the membership negotiations, the dominant powers (USA, EU) exercise very concrete pressure not only in matters linked with trade, but in other important issues as well. The aim of this outside pressure is to harmonise all the important aspects of global competition. Therefore, a multitude of issues is under discussion concerning intellectual property rights, pricing practices, free movement of capital, etc. In these complicated negotiations, Russia has made concessions in many spheres, e.g. by promising to mitigate ownership limits for insurance companies coming from EU-region. The final WTO-membership of Russia is still bending.

This process of Russian WTO-membership is as such a positive event. It shows that the present leadership in Kremlin is not aiming at isolation. Russia is interested in advantages from

the international division of labour, but out of historical reasons makes concessions to the outside world only carefully.

In sum, the overall Russian socio-economic scene in this decade differs extremely radically from the 1990s panorama: the latter was a period of economic decline, high political uncertainty, rampant capital flight, reluctant institutional reforms, and faulty economic policy-making (in monetary and fiscal policy). Prospects for the current decade are in every respect essentially better.

However, present-day Russia is still an emerging market, in which the post-industrial service society is far from maturity. Thus, many modern service sectors, including insurance business, will have a long period of structural, not cyclical, growth ahead.

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**Appendix 1: Top 100 Russian insurance companies and the foreign ones in 2003**

Company	Registration No.	Premiums (MRUR)	Change (%)	Life insurance	Share (%)		Compulsory insurance	Rank by claims paid in 2003	Claims paid (MRUR)	Change to 2002 (%)
					Non-life voluntary					
Stolichnoye Strakhovoye Obshestvo	3258	33.734	436,4	96,3	3,7	--	--	2	24.166	761,1
Uralsib	983	23.574	-8,1	79,7	17,7	2,6	--	1	26.169	-16,4
Klassko	806	18.665	45772,1	98,7	1,3	--	--	3	20.492	583903,2
RESO-Garantiya	1209	13.429	110,2	6	77,7	16,4	--	15	3.738	89
Yakor	1621	11.811	3,5	96,5	3,5	0,1	--	4	12.277	-3,8
National Insurance group	1826	11.200	4,2	57,1	41,7	1,2	--	7	8.280	-15,7
Doveriye	428	10.451	110675	99,9	0,1	--	--	5	10.051	55268,7
Ingosstrakh	928	10.001	39,3	--	89,1	10,9	--	20	3.045	17,2
MAKS-M	2226	8.121	63,6	--	0,4	99,6	--	8	7.664	64
Russo-Garant	3417	7.726	356,9	82,3	17,7	--	--	9	6.700	333
ROSNO	290	7.615	-28,9	21,6	73,4	5,1	--	14	3.810	-73,1
Capital-Strakhovaniye	1298	6.782	16,4	13,3	85,1	1,6	--	24	2.052	107,2
SOGAZ	1208	6.595	37,2	4,8	92,2	3,1	--	23	2.246	37,7
Standart-Rezerv	1137	6.279	24,7	86,7	11,2	2,1	--	6	9.076	183,7
Soglasie	1307	6.039	-3,4	0	93,6	6,4	--	71	579	-31,2
Military Insurance Company	621	5.593	62,1	0,9	57,9	41,2	--	21	2.978	86,1
Nadezhda Baltiki	1325	5.588	86887,3	99,9	0,1	--	--	10	5.662	3308
ROSNO-MS	2890	5.437	25,2	--	1	99	--	11	5.548	39
Komestra-Centr	949	5.080	35378,1	100	0	--	--	13	3.981	1599412
MAKS	1427	4.328	103,9	2,3	87,8	10	--	28	1.906	77
Priroda	3130	3.668	76	0	99,8	0,2	--	99	431	6,2
Akustika	658	3.604	713,7	87,2	12,8	--	--	18	3.280	674,4
Transenergopolis	3277	3.403	9771	91,3	8,7	--	--	17	3.303	н. д.
Yedinstvo	3338	3.312	213,9	93,9	6,1	--	--	16	3.425	158,4
Alpha Strakhovaniye	2239	3.200	-63	19,3	63,7	16,9	--	35	1.328	-80,3
Gazprommedstrakh	3230	3.017	25,8	--	83,6	16,4	--	22	2.715	18,6
Rosgosstrakh	1	3.004	159,7	2,4	97,5	0,1	--	98	434	40,6
SKPO	3014	2.952	98,8	0,1	11,5	88,4	--	26	1.983	79,3
Gorodskaya Strakhovaya Kompania	1489	2.899	11,2	94	3,6	2,4	--	19	3.142	-20
Leader	808	2.619	7,2	--	98,8	1,2	--	54	719	333,6
Nasta-Center	1083	2.617	100,5	1,4	75,7	22,9	--	85	494	93,1
Rosgosstrakh-Povolzhye	665	2.574	910,7	2,9	40,8	56,3	--	80	517	466,9
Rekon	1263	2.371	9,7	31,5	63,3	5,2	--	45	897	-34,4
RK-Garant	2905	2.145	99,1	--	99,5	0,5	--	380	37	100,9
Gurta-Strakhovaniye	1820	2.105	117,6	0	86,3	13,6	--	86	490	153,1
Surgutneftegaz	3127	2.073	13,5	5,9	89,2	4,9	--	33	1.422	36

SKPO-Med	2326	2.066	40,6	--	3,6	96,4	25	1.987	51,8
Zhaso	263	2.057	42,8	0	77,5	22,4	42	1.094	51,1
Renaissance Insurance	1284	2.047	17,9	0,1	96,3	3,5	52	832	12,8
Spasskiye Vorota	2992	2.039	135,6	1,5	51,6	47	93	449	62,5
Rosgosstrakh-Centar	1096	2.039	1214,5	4,7	29,7	65,5	123	327	530,8
Rosgosstrakh-Stolitsa	977	1.998	184,1	0,5	50,9	48,6	100	424	66,4
Spasskiye Vorota-M	2354	1.992	-2,3	--	1,3	98,7	27	1.980	2,7
Solidarnost Dlya Zhizni	257	1.974	34,8	--	1,7	98,3	29	1.856	29,6
Rosgosstrakh-South	1374	1.974	1665	2	28,1	69,9	194	163	86,8
AIG РОССИЯ	3256	1.910	21	36,7	63,1	0,2	143	260	-16,7
Energogarant	1834	1.836	4,9	2,9	85,6	11,4	81	515	45,5
Neftepolis	3297	1.829	-23,8	18,7	76,5	4,8	139	280	35,9
Rosgosstrakh-North-West	451	1.780	498,8	0,9	45,5	53,7	103	395	125,7
Progress-Garant	2786	1.621	-52,8	--	98,6	1,4	53	726	-78,4
Rossiya	2	1.620	47,8	2	87,9	10,1	58	703	115,5
Russkiy Mir	1582	1.589	142,7	--	77,4	22,6	121	329	2
Kuzbass	1965	1.587	6,6	--	1	99	30	1.530	5,8
GSMK	2071	1.552	23	--	0,2	99,8	32	1.485	19,4
Medstrakh	484	1.534	25	--	--	100	31	1.495	35,7
Rosgosstrakh-Ural	2366	1.520	390,8	3,7	33,6	62,7	151	248	109,9
Alpha Strakhovaniye	3369	1.461	-27,5	--	100	--	382	37	-74,8
Oranta	3028	1.361	96,2	46,6	47,3	6,1	64	671	5,7
Nadezhda	1447	1.357	35	--	--	100	34	1.328	н. д.
Jugoria	3211	1.334	83	1,8	83,9	14,3	169	216	86,5
Askomed	278	1.314	7,4	--	1,1	98,9	36	1.308	7,2
Itera-Garant	3199	1.310	24,9	--	100	--	287	66	7,3
Usolye-ASKO	2146	1.289	72220,9	5,5	94,5	--	205	144	36543,4
Pomosh	2729	1.285	104	70,2	29,8	--	37	1.217	103,7
Avest-Classic	3495	1.275	84,4	--	100	--	95	442	15,9
Almeda	1102	1.237	24,8	--	0,2	99,8	38	1.202	25,4
Rosgosstrakh-Sibir	2474	1.225	2703,1	1,4	17,2	81,5	224	112	836,5
NESO	3310	1.199	-16,2	--	100	--	665	4	-96
Sheksna	2115	1.191	69,6	0	96,3	3,7	211	131	19,9
Transgaz	3305	1.164	122,1	10,3	89,7	--	207	138	31
Sahamedstrakh	2873	1.157	33,6	--	1,1	98,9	40	1.107	32,2
RESO-Med	879	1.141	106,5	--	--	100	39	1.113	112,4
EMESK	741	1.132	48	--	--	100	41	1.096	48,6
Argysmedstrakh	3415	1.114	30,8	--	--	100	43	1.063	28,5
Corporation of Medical Insurance	356	1.068	21,7	--	0,6	99,4	44	1.047	6,1
Chulpan	1216	1.026	-17,9	30,9	65,7	3,5	89	477	9,7
Dalmedstrakh	2503	985	23,8	--	--	100	47	889	17,1
Itil	1858	965	30	1,6	93,7	4,7	57	706	26,1

Rosgosstrakh-Accord	2309	923	415,4	25,2	31,2	43,6	114	350	344,7
ASKO-VAZ	320	916	14,9	--	9,5	90,5	51	843	8,8
Rusinvest	3686	902	н. д.	--	100	--	537	12	н. д.
Samara-ROSNO-Med	2684	882	8,4	--	2,6	97,4	48	870	8,3
Osnova	3366	861	114,9	--	100	--	325	54	910,2
Russkiy Strakhovoy Centr	159	860	69,7	0	100	--	366	42	-30,9
Transneft	1864	853	70,5	--	96,6	3,4	173	208	153,8
Imperio	3361	852	119,3	96,8	3,2	--	49	869	137
Sheksna-M	2838	832	33,7	--	40	60	50	867	66
Metropolis	81	824	37,2	--	97,9	2,1	337	48	462,9
Ikar	2061	815	30,6	--	0,3	99,7	46	890	35,6
Rosgosstrakh-Tatarstan	2382	810	81,2	7,3	57,3	35,4	142	264	39,6
Megaruss-D	2877	807	34,2	--	84,5	15,5	164	220	351,6
Moskva	191	785	0,8	--	99,6	0,4	445	23	-74
Energeticheskaya SK	1914	785	72,5	2,5	95,9	1,5	345	46	-78
Podderzhka	2647	775	103,1	--	100	--	87	484	185,2
Rosgosstrakh-Dalniy Vostok	468	753	303,9	4,3	26,5	69,1	209	133	81,9
SKM	1047	746	-8,9	0	92,3	7,7	193	164	33,1
Interpolis	629	738	23,9	--	--	100	55	711	18,4
Rusmed	352	733	12,7	--	6,6	93,4	60	698	11,8
MAKS	656	730	57,8	--	--	100	56	710	58,8
NSG-Energo	3295	725	205,3	0	75,9	24,1	149	249	171,4
Ost-West Allianz	2294	661	14,7	10,2	89,8	--	241	98	-1,7
Zurich-Russ	212	344	-7	--	100	--	315	57	28,5
Principal	2929	43	36,8	0	100	--	271	73	-59,6

**Appendix 2. Reserve portfolio guidelines**

<b>Assets</b>	<b>Limit</b> (of total amount of reserves, unless otherwise indicated)
Securities of regional governments and municipal securities	30%
Bank deposits and promissory notes	40%
Shares and bonds (except federal and regional governmental, municipal)	30%
Payments receivable	10%
Reinsurance premiums deposits	10%
Shares in trust and investment funds	5%
Shares in partnerships and shares not A-listed by at least 1 stock exchange (trade system)	10%
Building certificates (except federal and regional governmental, municipal)	5%
Real estate	20% for life insurance provisions 10% for non life reserves
Gold and silver in bars	10%
Securities of 1 regional government	15%
Securities of 1 municipality	10%
Total value of securities, deposits and shares in funds of 1 bank	15%
Total value of securities issued by 1 entity and A-listed by at least 1 stock exchange (trade system)	10%
Total value of securities issued by 1 entity and not A-listed by at least 1 stock exchange (trade system)	5%
Maximum value of one object of real estate	10%
Reinsurers' share in reserves (except for reserve for reported but unsettled losses)	60% (except for reserve for reported but unsettled losses)
Share of 1 reinsurer in reserves (except for reserve for reported but unsettled losses)	15% (except for reserve for reported but unsettled losses)
Foreign Reinsurers' share in reserves (except for reserve for reported but unsettled losses)	30% (except for reserve for reported but unsettled losses)
Foreign assets (except for reinsurers share)	20%

**Appendix 3. Premiums according to the regions and insurance lines (MRUR)**

Region of Russia	Premiums total	Life	Other personal lines	Property	Liability	Compulsory
1 Moscow (city)	239.156	125.310	18.906	66.507	7.980	20.453
2 Moscow oblast	23.470	8.383	1.125	4.560	471	8.931
3 St. Petersburg (city)	23.368	6.779	2.167	6.249	625	7.547
4 Tyumen oblast	11.889	354	2.228	6.208	350	2.749
5 Tatarstan	9.428	1.158	1.445	6.032	128	664
6 Krasnoyarskiy Kray	8.047	135	483	2.688	139	4.602
7 Samara oblast	7.718	179	1.202	2.098	157	4.083
8 Irkutsk oblast	6.351	266	1.070	2.122	37	2.856
9 Chelyabinsk oblast	4.933	1.618	740	1.600	263	712
10 Sverdlovsk oblast	4.817	264	1.158	2.033	201	1.160
11 Kemerovo oblast	4.575	308	763	499	29	2.976
12 Rostov oblast	4.433	183	581	606	105	2.958
13 Nizhegorodskaya obl.	3.904	148	732	1.729	77	1.218
14 Krasnodarskiy Kray	3.884	55	390	1.538	148	1.752
15 Perm oblast	3.781	1.089	530	1.638	88	436
16 Novosibirsk oblast	3.618	108	763	982	86	1.678
17 Vologda oblast	3.445	122	408	1.348	11	1.557
18 Saha (Yakutia)	3.083	83	165	283	14	2.537
19 Stavropolskiy Kray	2.785	9.770	212	480	24	2.060
20 Bashkirya	2.692	774	536	730	87	564
21 Omsk oblast	2.551	731	2.691	1.181	621	965
22 Primorskiy Kray	2.329	88	236	890	100	1.015
23 Voronezh oblast	2.314	25	178	260	32	1.819
24 Tomsk oblast	2.310	32	403	502	32	1.341
25 Tula oblast	1.922	16	111	301	25	1.471
26 Lipetsk oblast	1.872	11	63	555	17	1.227
27 Vladimir oblast	1.701	97	88	345	25	1.145
28 Volgograd oblast	1.698	10	203	729	61	695
29 Belgorod oblast	1.688	15	95	273	15	1.291
30 Yaroslavl oblast	1.662	88	192	3.011	19	1.062
31 Tver oblast	1.593	18	731	5.371	20	945
32 Bryansk oblast	1.577	16	85	193	13	1.270
33 Saratov oblast	1.552	358	282	603	251	284
34 Sahalin oblast	1.439	4	97	314	304	720
35 Murmansk oblast	1.416	16	187	776	246	192
36 Arkhangelsk oblast	1.397	10	58	302	14	1.012
37 Buryatia	1.383	42	31	114	2	1.194
38 Amurskaya oblast	1.353	19	59	142	25	1.107
39 Khabarovskiy Kray	1.328	94	414	539	44	237
40 Chuvashia	1.299	5	73	292	8	921
41 Udmurtia	1.275	287	276	483	25	203
42 Leningradskaya oblast	1.266	13	117	689	187	258
43 Kaliningrad oblast	1.250	6	107	364	67	706
44 Altayskiy Kray	1.250	101	146	709	10	283
45 Ulyanovsk oblast	1.247	74	169	417	122	464
46 Tchita oblast	1.104	9	188	190	5	713
47 Penza oblast	1.103	156	86	107	8	745

48	Kursk oblast	1.040	4	46	102	27	860
49	Ryazan oblast	1.031	7	52	224	10	738
50	Komi	993	52	261	510	24	146
51	Karelia	956	2	116	143	13	681
52	Novgorod oblast	953	20	52	256	12	612
53	Orenburg oblast	943	68	331	197	55	292
54	Astrakhan oblast	868	1	50	107	23	687
55	Kamchatskaya oblast	830	1	17	101	20	690
56	Tambov oblast	816	6	30	165	7	608
57	Kaluga oblast	526	16	24	167	13	305
58	Hakassia	514	16	23	85	5	385
59	Kirovsk oblast	510	10	147	187	6	161
60	Orel oblast	489	12	34	140	9	294
61	Kalmikia	436	3	58	109	11	256
62	Ivanovo oblast	360	102	31	118	7	102
63	Smolensk oblast	333	28	44	124	7	130
64	Mordovia	329	15	32	121	3	159
65	Pskov oblast	320	4	22	77	18	199
66	Kostroma oblast	287	26	22	165	5	70
67	Magadan oblast	249	0	7	43	8	192
68	Mariy El	242	5	27	153	4	53
69	Kurgan oblast	220	4	33	55	5	123
70	Kabardino-Balkaria	182	1	9	31	2	140
71	Altay	180	0	71	77	1	30
72	Dagestan	165	12	36	51	14	51
73	S. Osetia–Alania	126	0	9	59	4	54
74	Adygea	84	0	6	30	2	46
75	Karach.-Tcherkessia	48	0	1	13	1	33
76	Tchukotskiy AO	43	0	7	32	1	3
77	Evreyskaya AO	42	9	7	7	0	18
78	Chechnya	39	0	24	6	3	6
79	Tyva	25	9	3	3	1	9
80	Ingushetia	9	0	1	3	0	5
<b>Total</b>		<b>432.441</b>	<b>149.443</b>	<b>41.525</b>	<b>125.699</b>	<b>12.857</b>	<b>102.918</b>

**Appendix 4. 60 leaders of CMTPL 2003**

Company	City	Premiums Written MRUR	Number of Policies sold	Number of Claims Reported	Number of claims settled	Claims paid MRUR	Average indemnity per claim	Loss ratio %	Average premium per policy
1 Rosgosstrakh*	Moscow	9.299	6.270.000	No data	20.000	454	22.678	4,4	1.483,1
2 RESO-Garantia	Moscow	2.600	1.000.000	13.400	5.000	129	25.800	5,0	2.600,0
3 Ingosstrakh	Moscow	1.284	490.271	5.743	2.596	68	26.178	5,3	2.619,4
4 Spasskiye vorota	Moscow	884	342.226	3.371	1.839	43	23.301	4,9	2.583,8
5 SKPO	Moscow	794	523.000	No data	2.000	46	23.000	5,8	1.518,2
6 Military IC	Moscow	720	340.278	1.431	1.084	23	21.408	3,2	2.115,9
7 Uralsib	Moscow	620	228.000	No data	2.150	30	14.047	4,9	2.719,3
8 NASTA	Moscow	594	235.274	2.836	1.834	27	14.836	4,6	2.525,4
9 Alpha-strakhovaniye	Moscow	522	218.612	2.598	1.390	29	20.586	5,5	2.386,7
10 MAKS	Moscow	425	162.079	2.778	1.190	26	22.006	6,2	2.620,2
11 ROSNO	Moscow	438	146.604	1.265	680	17	24.682	3,8	2.989,9
12 MRSS	Moscow	423	214.812	1.692	1.222	28	22.948	6,6	1.968,4
13 Soglasiye	Moscow	378	173.619	1.499	781	25	31.894	6,6	2.178,1
14 Russkiy Mir	St.Petersburg	358	150.120	1.619	599	17	28.441	4,8	2.388,0
15 Rosstrakh	Novosibirsk	244	127.928	1.164	424	9	20.148	3,5	1.908,6
16 Energogarant	Moscow	215	100.029	494	365	9	24.173	4,1	2.145,3
17 SOGAZ	Moscow	204	94.785	256	150	3	22.930	1,7	2.153,7
18 Jugoria	Kh-Mansiysk	191	83.837	747	469	13	27.002	6,6	2.283,6
19 Progress-Neva	St.Petersburg	184	51.153	674	302	7	24.503	4,0	3.597,1
20 Megaruss-D	Moscow	171	53.243	490	185	4	22.508	2,4	3.204,1
21 Rossiya	Moscow	164	61.238	336	176	5	27.301	2,9	2.682,2
22 Region	St.Petersburg	151	62.597	441	119	3	27.146	2,1	2.416,9
23 NSG	Moscow	139	42.324	610	240	5	20.000	3,5	3.291,7
24 Avest	Moscow	134	32.486	212	134	3	25.197	2,5	4.130,0
25 AFES	Moscow	122	55.623	428	273	8	27.870	6,2	2.198,5
26 Capital	Kogalym	107	38.021	189	93	2	25.000	2,2	2.819,0

27	General IC	St.Petersburg	103	34.000	844	257	5	20.083	5,0	3.029,4
28	Surgutneftegaz	Surgut	102	51.676	389	201	7	32.881	6,5	1.976,9
29	Neftepolis	Moscow	98	38.464	233	178	4	19.956	3,6	2.542,7
30	Avicos	Moscow	94	35.734	188	165	4	25.351	4,5	2.622,5
31	Rosmedstrakh	Moscow	87	47.926	251	104	3	30.269	3,6	1.807,2
32	Oranta	Moscow	83	30.180	588	138	4	25.814	4,3	2.763,8
33	ASKO-Tatarstan	Kazan	78	38.890	440	289	4	15.211	5,7	1.993,5
34	Geopolis	Moscow	76	21.500	250	126	2	19.048	3,2	3.534,9
35	Astro-Volga	Tolyatti	71	33.850	338	258	5	20.020	7,3	2.101,8
36	Angara	Bratsk	71	38.147	486	456	5	9.992	6,5	1.848,7
37	Gorstrakh	Moscow	70	22.370	246	153	3	20.598	4,5	3.141,2
38	Renaissance	Moscow	63	15.112	144	92	3	29.898	4,4	4.149,0
39	Informstrakh	Moscow	61	18.106	199	130	2	11.746	2,5	3.367,6
40	Nadezhda	Krasnoyarsk	56	34.789	583	559	4	6.716	6,7	1.618,0
41	MSK	Moscow	55	15.627	64	41	2	38.951	2,9	3.521,5
42	AGRIS	Moscow	46	26.506	113	45	1	21.853	2,1	1.731,7
43	BASK	Belovo	45	27.146	187	155	3	18.265	6,3	1.664,5
44	Moskovia	Troitsk	44	13.550	86	54	1	23.884	2,9	3.281,4
45	Itil	Kazan	44	22.161	316	197	4	21.214	9,4	1.997,5
46	Shecksna	Cherepovets	44	24.910	241	163	3	21.355	8,0	1.751,4
47	Metroton	Moscow	39	18.996	143	66	1	21.182	3,6	2.030,9
48	Podmoskovye**	Podolsk	37	11.344	102	64	1	22.703	3,9	3.296,9
49	Ariadna	Moscow	36	9.034	128	48	2	35.091	4,7	3.969,2
50	Leader	Moscow	33	45.663	6	6	0	14.704	0,3	721,5
51	Russian IC	Moscow	30	7.263	53	17	0	23.200	1,3	4.185,5
52	MSC	Moscow	25	8.146	46	18	0	15.280	1,1	3.022,8
53	Gefest	Moscow	21	5.018	30	16	0	23.328	1,8	4.145,2
54	Uralros	Yekaterinburg	21	9.586	69	29	1	21.576	3,0	2.146,3
55	ASTO-Garantiya	Moscow	20	5.452	57	25	1	30.027	3,8	3.674,9
56	Medexpress	St.Petersburg	18	6.144	75	24	1	24.235	3,3	2.868,1
57	Regiongarant	Moscow	16	4.460	33	21	1	35.254	4,5	3.657,4

58 Pari	Moscow	13	2.699	58	19	0	14.305	2,1	4.721,7
59 RK-Garant	Moscow	12	3.448	9	3	0	39.215	1,0	3.406,7
60 RUKSO	Moscow	10	2.846	46	32	0	2.253	0,7	3.436,0

(Source: CEA of Interfax)

Comments:

\* Including 10 subsidiaries

\*\* Former Podolsk