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# *Analysis of Factors Influencing the Development of China's Insurance Industry*

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***Abstract:*** The insurance industry is closely linked to individual interests and the overall economy of the country. Nowadays, in the context of Covid-9, the stable development of the insurance industry is particularly important. However, much of the literature focuses on the role of the insurance industry in economic development, but there are few studies that focus on the industry in general and analyze the impact factors of the insurance industry itself from multiple perspectives. To fill the academic gap in the overview of the insurance industry and better promote its future development, this paper explores the role of seven factors such as economic growth, inflation, disposable income of the population, and the scale of social security on the development of the insurance industry from three aspects: macro, micro, and China-specific social background conditions. Through a comprehensive analysis of relevant domestic and international literature in recent years, this paper concludes that: economic growth, higher individual disposable income and better legal system and regulation have a positive effect on the development of the insurance industry; inflation inhibits the insurance industry development. The effects of demographics, social security size and residents' education level on China's insurance industry are somewhat complicated.

***Keywords:*** insurance development, influencing factors, China's insurance industry

## 1. Introduction

In modern society, insurance is one of the most important forms of risk management. The stable and sustainable positive development of the insurance industry is meaningful for individuals, companies and national polities. Because of insurance, individuals who want to protect themselves against risk no longer need to set aside enough money to cover all possible losses, and the difference between it and the insurance premium can be invested or consumed instead, thereby boosting economic growth and market efficiency.

For this reason, in recent decades, many scholars have conducted many studies to illustrate the contribution of the insurance industry to economic development, and these studies have covered not only financial markets but also the real economy. However, there is little literature that explores what factors influence the insurance market itself, and even less literature that focuses on the Chinese region. Based on this fact, this paper will explore the factors affecting the development of China's insurance industry and discuss their specific roles from three main aspects: macro, micro and Chinese social context, aiming to fill the academic gap and provide theoretical references for future related research and policy regulation of industry development.

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## 2. Macro Factors Analysis

This section will analyze the impact of three macro factors on the insurance industry. The three factors are economic growth, inflation and demographic factors.

### 2.1. Economic Growth

According to the nature of insurance itself and its mechanism to protect against economic losses, it is natural to assume that economic growth will boost the insurance industry. As mentioned earlier, there have been many scholars who have conducted quantitative analyses of the correlation between the development of the insurance industry and economic growth. Although they focus more on the insurance industry's role in driving economic growth, some of them inevitably conclude that there is a two-way causal relationship between the two - while the insurance industry fuels economic growth, the growth of the economy will also counteract the insurance industry and contribute to its positive development.

Arena, for example, assembled panel data for 56 countries during the period of 1976-2004 to explore whether there is a causal relationship between economic growth and insurance market activity [1]. She used premium amounts as a measure of insurance activity and divided the entire insurance market into life and non-life insurance. This division is based on her view that life and non-life insurance actually provide different benefits to households, which is in line with the particular social and cultural context and perception of death in China. She eventually concluded that there was a significant causal relationship between life and non-life insurance sector activity and economic growth. And Mehmen Balcilar, Ran Gupta, Chien-Chiang Lee et al found a positive two-way causal relationship between insurance development and economic growth, using 21 years of panel data for eleven countries [2].

### 2.2. Inflation Rate

Inflation is another factor that needs to be discussed. In essence, the real value of pensions, insurance, and marketable securities is reduced by the devaluation of the currency, which obviously reduces the population's desire to take out insurance. At the same time, inflation will also affect the disposable income and consumer savings structure of the population, especially the working class, which makes up the vast majority of China. These effects of inflation can inhibit the growth of the insurance industry.

However, Erik and Rodney et al analyzed panel data for 90 countries in 2000-2008 and found that inflation depresses activity in the life insurance segment, which is consistent with much of the rest of the research literature - and yet had a boost to the non-life insurance sector [3]. Their explanation for this is that the role of inflation in the development of the non-life insurance sector includes the influence of a number of secondary factors. In an economic context where high inflation is expected, people will actively seek ways to counteract the economic losses caused by inflation. One of these is the exchange of currency into value-holding goods such as property to protect against possible future currency devaluation and this could also create a huge real estate bubble. The non-life insurance sector may grow to some extent as a result since it is highly correlated with these commodities.

But this growth effect is linked to consumer psychology, which is a difficult indicator to quantify precisely, and it is difficult to predict whether the magnitude of growth will offset the negative effects of inflation on the economy. This positive effect was then attributed as a secondary factor in Erik's study, leading to the conclusion that inflation will inhibit the growth of the insurance industry.

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### 2.3. Demographic Factors

In addition to economic growth and inflation, another factor to be considered is population, which more precisely involves three dimensions: population size, population density and population structure.

China has the most population all over the world, so when discussing the factors affecting the development of China's insurance industry, there is no way to get around the demographic issue. The subject matter of life insurance is often human life or health, so countries with larger populations should have greater demand for life insurance, while non-life insurance does not seem to be directly related to population size. This factor is also analyzed in Erik's article. He confirms with data that population size has a boosting effect on life insurance, yet small, open economies have a more developed non-life insurance business. In reality, however, it is not the size of the population but the openness of small economies that plays a key role in non-life insurance.[3] Because of the frequent foreign trade of open economies, there is a greater demand for insurance related to the transportation of goods, which has led to the development of non-life insurance. This also shows, in the opposite direction, that population size does not have a direct effect on non-life insurance.

Due to China's vast territory and the uneven development between the east and west, there are huge differences in population density between cities. This factor is less informative when looking at the overall industry development in China.

As for demographic structures, many scholars have introduced an indicator in their studies called the age dependency ratio, commonly defined as the ratio of the population under 15 and over 65 years of age to the working-age population. As Zhang Lianzeng and Wang Jiao mentioned in their paper, China has been plagued by an aging population in recent decades [4]. Despite the fact that China has just enacted a three-child policy, it will take time for this problem to improve. Overall the short-term age dependency ratio in China is stable or even slightly increasing. Therefore this factor is also worth discussing.

The age dependency ratio appears to have a direct impact on life insurance. In the life table, young children and older people are more likely to die, so the larger this group is, the greater the need for life insurance seems to be. Thorsten Beck and Ian Webb found that the old-age dependency ratio has a significant positive effect on insurance penetration by analyzing data for 68 countries between 1961 and 2000 [5]. The results of Zhang Lianzeng's data analysis show that old age and child dependency ratios have a positive effect on the demand for life insurance, but this effect is not significant. This insignificance is most likely the result of the lower income of older adults [4].

It seems to be a social consensus that all people, young and old, are equal in the face of possible property losses. Research on demographics for the development of the non-life insurance sector is scarce and the findings are ambiguous. But we all know that an overburdened population can have a negative impact on economic growth, which can further affect the insurance industry. Elena's analysis of data from 25 countries over the last 40 years found that population burden has a positive effect on insurance density in the short term but a negative effect in the long term [6].

## 3. Micro Factors Analysis

### 3.1. Disposable Income

It is clear that income is the most important driver of insurance growth. Insurance in this case can be considered a commodity. When the disposable income of the population rises, the demand for such non-essential goods will rise accordingly It is worth noting that while all of this literature shows that the higher the disposable income the greater the demand for insurance, there are analyses of wealth

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gap data that suggest that this finding does not apply at the extremes of income. This is because the extremely wealthy have such a high tolerance for risk that they do not need insurance coverage.

### 3.2. Education Level

Due to the professional nature of the insurance industry and the terms of insurance contracts, the public often needs to have a clear and accurate perception of insurance-a perception that seems to be related to the level of education of the population. Ye Jiale and Shen Xiaohong said that actively popularizing insurance knowledge and raising public awareness of insurance so that the general public can look at insurance objectively and rationally, understand and believe that insurance companies and insurance products can provide risk protection for residents is one of the ways to stimulate the development of the insurance industry [7].

Outreville argues that people with higher education tend to be more risk-averse and thus more willing to purchase insurance [8]. However, this research was conducted in 1996. At the end of the last century, higher levels of education often corresponded to more information and higher incomes, and higher incomes and good risk awareness combined to stimulate the demand for insurance among this group. Due to the rapid development of the Internet over the past 30 years, people's access to information is no longer limited to schooling, so the level of education is no longer an important factor in measuring insurance awareness, and the link between education level and insurance development has weakened. In 2016, Shahrzad and Mohammadreza confirmed this by analyzing the results of the questionnaire. They found that the effect of education level on insurance was not significant [9]. With the development of diversified forms of education and the future diversification of scientific knowledge and cognition, the impact of academic education on the demand for insurance will become less and less.

## 4. Analysis of Social Environment Factors in China

### 4.1. Social Security Scale

At a press conference held by the Propaganda Department of the Central Committee of the Communist Party of China on August 25, Li Zhong, Vice Minister of the Ministry of Human Resources and Social Security, introduced that China has built the world's largest and fully functional social security system in the last decade [10]. According to an industry report by the China Banking Regulatory Commission, China has remained in the world's second premium market for the past five years but is also gradually closing the gap with Japan, which is in third place. The gap between the size of Social Security and the level of premiums means that the two are not simply increasing at the same rate. In terms of the insurance industry as a whole, social and commercial insurance can be considered alternative commodities to some extent.

Erik offered a more detailed explanation in his essay: when a country's social security size is expanded, on the one hand, there will be less demand for commercial insurance, on the other hand, it will reduce the disposable income of the population, and under the joint result of these two effects, the development of commercial insurance has to rely more on other influencing factors to stimulate. This is why, although China's social insurance is already the largest in the world, there is still a gap in industry-wide premium revenue compared to the United States.

### 4.2. Legal and Government Regulation

Insurance is a legal transfer of risk according to contractual provisions, so the impact of laws and regulations on the development of insurance is also worth considering. In theory, when the whole process of the insurance industry from contract signing to claim settlement is controlled by laws and

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regulations and a perfect industry supervision system, the credibility of the whole industry in the hearts of the people will increase, and people will be more willing to use the insurance when they need to transfer risks, which in turn will promote the development of the insurance industry. This point is covered in the article by Jiale Ye. She argued that in a society under the rule of law, legal regulation will have a positive guiding and protective effect on the development of any industry.

However, it is difficult to precisely quantify this factor, and only little empirical evidence can be found to support this view. Neil Esho and Ralf Zurbruegg provided the first empirical analysis of the effects of legal origin and judicial efficiency on property insurance by assuming that the role of the legal environment for insurance is mediated by the positive probability of insurer insolvency. Eventually thay concluded that legal origin and judicial efficiency have a positive effect on the insurance industry, which is consistent with common sense and other theoretical arguments in the literature.

## 5. Conclusion

By integrating and analyzing the previous literature and exploring the many factors influencing the development of the insurance industry by substituting them into the specific social context of China, this paper can finally conclude that economic growth, the increase in disposable income of the population and a better legal environment have a positive effect on the development of the insurance industry; inflation inhibits the development of the insurance industry. The impact of demographics, the size of social security and the level of education of the population on the insurance industry is somewhat complex. Countries with larger populations such as China tend to have greater demand for life insurance, while small open economies exhibit more demand in non-life insurance sector; the old age dependency ratio and the young child dependency ratio have an impact on the corresponding types of insurance, respectively, but have little impact from the perspective of the insurance industry as a whole in China; the influence of education level on the insurance industry is gradually disappearing; the size of social security and commercial insurance are a coin of two sides of the same coin, and it is difficult to describe the impact of the size of social security alone from the perspective of the insurance industry as a whole.

It can also be seen that the positive or negative impact of these above-mentioned factors on the insurance industry, including a certain part of it, is not completely isolated. Although they can be tested independently when conducting empirical analysis, when returning to theoretical explanations and actual regulation, changes in one factor often cause changes in another factor to some extent. Such predictions that take into account the changes triggered by the adjustment of one of the interacting factors should be one of the points of examination for future academic research.

At the same time, most of the references cited in this paper are more than five years old due to the paucity of studies on the general development of the insurance industry in recent years. Research based on an overall perspective needs to be further developed.

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