

BY DWIGHT K. BARTLETT III

Bear Market

Trying to Make Insurance Work in Russia

The road to success for Russian insurers may be more difficult than Napoleon's retreat from Moscow. Fortunately, the United States has plenty of advisers who want to help.

ON MY FIRST TRIP TO RUSSIA in June 1998, I found out firsthand how dismal the prospects were for the insurance market in that country. The annual premium income of the entire insurance industry in Russia was equivalent to \$5 billion, about the size of one U.S. carrier. Only 2 percent or 3 percent of Russian households owned any level of insurance coverage, and the rate among businesses wasn't much better.

I was part of a team of present and former state insurance regulators, sponsored by the U.S. Department of Commerce. We met with Russian federal officials and private insurance entrepreneurs to talk about the necessity and focus of insurance industry regulation.

I had the opportunity to visit Russia again in December 1999. This time the purpose of my visit was to provide pro bono consulting to an insurance company in the city of Tver. I was sponsored by the Citizens of Democracy Corps, a private nonprofit agency funded primarily by the U.S. Agency for International Development.

The changes in the insurance market over the 18-month period between my visits were dramatic, and, unfortunately, largely for the worse.

Because of the instability of the value of the ruble, most long-term life insurance policies are denominated in the hard currencies of Western nations. Unfortunately, maintaining proper asset-liability matching requires exporting capital from Russia, a result adverse for the development of the Russian economy. Nevertheless, local and foreign business people expressed a great deal of interest in getting in on the ground floor of a nascent insurance industry.

This hoped-for blossoming was badly blighted by the major devaluation of the ruble that occurred during the summer of 1999. That devaluation caused a major loss of real value in insurance company assets, without a concomitant decline in the value of liabilities. As a result, seven out of the 10 largest Russian insurers became instantly insolvent and stopped paying claims.

Russia apparently has nothing equivalent to our state guaranty funds or state laws providing for the orderly rehabilitation or liquidation of insolvent companies. Public confidence in private insurance, not great to begin with, was badly shaken. Because the average Russian worker earns about \$80 a month—a somewhat misleading figure due to the low cost of living in Russia—insurance is well down the list of priorities for Russian families.

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Less understandable is why Russian businesses have a similar attitude toward insurance. They apparently need to be educated to the necessity for insurance if they're to attract investors, particularly foreign investors.

Some preconditions seem necessary to the development of a significant private insurance industry in Russia:

- Confidence in the stability of Russia's currency. Recent signs offer some hope on this front.
- Creation of an appropriate legal framework. Contract law and tort law appear to be primitive by U.S. standards.
- The emergence of a significant middle class. The currently low incomes of the vast majority of Russian families make insurance coverage unaffordable.
- Education about the uses and necessity for insurance, particularly in the business community.

Cold Weather, Warm Hearts

Though I knew economic conditions were far from ideal, I expected weather conditions to be worse. I assumed I might well be facing subzero temperatures in central Russia in late December, and I wasn't even sure the room I'd be staying in at night would be adequately heated.

So I prepared accordingly. I packed long underwear, took my heaviest coat and a Russian-style fur hat that I inherited from my father-in-law, and purchased thermal socks and heavy boots. I was ready for anything Mother Russia could throw at me.

I was met on arrival at the Moscow airport by local representatives of the Citizens Democracy Corps. They took me, in a car I thought would conk out permanently at any moment, to the Hotel Russia near Red Square in downtown Moscow. The hotel claims to be the largest in Europe, with over 3,000 rooms. By international standards, however, it might rate one-and-a-half stars, if that.

The following morning the CDC staff put me in a first-class compartment on a Moscow-to-St. Petersburg train, with the first stop in Tver. I shared the compartment with three or four other people, none of whom spoke English. But my hosts were generous, warm-hearted people, anxious to make me comfortable any way they could. They offered me tea and made sure I got off at Tver.

There I was met by staff of the Upper Volga Institute, CDC's local partner. The UVI is a teaching and consulting entity affiliated with one of Tver's universities. UVI's director, Irina Askenova, is a high-powered and energetic middle-aged woman, dedicated to importing American business methods into her community. Among other activities, she is the founder of a local chapter of Rotary International, which apparently has about 50 members, most of the top-level business and professional people in Tver.



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UVI provided the translators, who were local university students and very fluent in English. My female translators were uniformly attractive and all had fur coats, viewed as a necessity in that climate in spite of their cost—low by Western standards but high in relation to an average Russian's wages.

Apparently fast-track students in Russia start studying English in about the fifth grade and keep with it for many years. They also gave me a younger person's viewpoint on Russian and world events.

One young man, home for a visit while studying at Drew University in New Jersey, expressed great fear of being drafted and sent to the war in Chechnya. To him this was almost equivalent to a death sentence, because of not only the fighting but also the stories of deadly abuse of draftees by army veterans.

Some of the older business people, too, were quite willing to talk politics. There is a widespread, deep-seated cynicism about government, viewed as the principal barrier to economic progress in Russia, regardless of who is in power. The war in Chechnya is seen as a political device to keep the Yeltsin/Putin faction in power.

Unemployment in Russia, officially reported at about 15 percent, is actually around 20 percent or higher. One of the people I met in Tver told me that she has a graduate degree in mathematics, but has no hope of finding employment in which she can use her training. Directly across the street was a medical college. I was told that half the graduates each year cannot find employment in the medical field.

The infrastructure in Russia has greatly deteriorated in recent years. The streets are badly deteriorated and poorly maintained. Though I saw no new construction of any type in Tver, there seemed to be some in Moscow where, I was told, office rents exceed those in New York. Apparently, Moscow is where all the money is.

Most heavy industry is closed down, unable to compete internationally. The average age of vehicles seemed much greater than in the United States, as might be expected in a country where capital is scarce and labor is cheap.

Christmas in January

My time at the insurance company in Tver was spent mostly with the upper-middle-level staff, who seemed mostly interested in insurance industry developments in the United States, rather than getting my advice about what they ought to be doing in Russia. Sergei, the general manager, seemed somewhat at a loss as to how to make best use of me, and he wasn't very forthcoming about his company's business affairs. He did tell me that it had about 400 home office employees and 250 agents. Their products are mostly personal lines casualty and health insurance. He said they had 100,000 life policyholders before the ruble devaluation and only 2,000 currently. They're anxious to expand into commercial lines, but they're uncertain how to overcome the lack of confidence in insurance companies.

While in Tver I stayed at the Museum Hotel, so named because it's immediately behind one of Tver's museums. But with only half a dozen rooms, it's more like what we would call a bed and breakfast. Though the building appeared somewhat dilapidated from the outside, it was in reasonable condition on the inside.

My room, however, was a different matter. As it turned out, I needn't have worried about being cold at night. The temperatures weren't as intimidating as I feared, and though daytime temperatures were generally in the mid-20 degrees, my room tended to be overheated at night. Apparently heat for all buildings in Tver, public and private, is provided by a central steam heat plant. There are no such things as thermostats, so room temperatures are controlled by opening and closing windows. Add a typically European bed (thin, lumpy mattress laid on a plywood board without springs), and I can't say I had a good night's sleep the whole time I was there.

At the Museum Hotel I found several other CDC volunteers who provided me with some English-speaking company, along with the translators. Nevertheless I felt very isolated much of the time, with no English-language newspapers or TV stations, such as the *International Tribune* and CNN International, which you can get all over Western Europe. Thus, while I was there during the Duma elections, I knew less about the outcome than my wife who was reading about it at home in Annapolis, Md. My sense of relief was palpable when I boarded my return Moscow/New York Delta flight and could speak to the stewardesses whose first language was idiomatic English.

I missed Christmas at both ends of my trip, since I was in Russia from Dec. 15 to 28 and the Russian Orthodox Church follows the Julian calendar, which places Christmas on Jan. 7. But on a free weekend I visited the Church of the White Trinity in Tver for Sunday services. A Russian Orthodox service was a new experience for me: no pews, no heat, mostly beautiful choral music, people coming and going, much swinging of censers, etc. The congregation of about 200 was perhaps 80 percent women in their 50s and older. My young translator was unable to explain the service to me, saying she believed in God but didn't have time for church. It left me wondering about the reported revival of religion in Russia.

Instead, there seems to be a prevailing feeling of hopelessness, reflected in the country's falling life expectancy and plummeting birth rate. Several doctors I talked to attributed the decline to alcoholism and alcohol-related accidents. Accidents are the third leading cause of death in Russia, compared to sixth in the United States. As far as the birthrate is concerned, I was struck by how few children I saw in the streets of Tver and Moscow.

A bright note, surprisingly, was the Russian food. I was invited out for most lunches and dinners and found the food and service uniformly excellent. I was forewarned that I might be pressed to consume more vodka than I could handle (I don't drink), but this didn't seem to be a problem. It wasn't even a problem at the New Year's Eve party I attended at the Rotary International where there was great music with lavish food. The party started at 6 p.m. and was still going strong at 11 p.m. when I made my excuses and left.

If there is hope for Russia, it rests in the courage and perseverance of its people. Surely no nation has had an unhappier history in the past two centuries, but the people soldier on. With much help from the West, I sincerely hope happier days lie ahead for them. Not only the Russians but all peoples in the world will benefit from whatever success they have. I don't know if I will ever return to Russia, but I feel I left many friends there. ●

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