Life Insurance Reborn

By Kojiro Sakai

The rough waves of financial deregulation and internationalization are pounding Japan's financial and economic worlds. The nation's life and nonlife insurance industries, no less than any others, are also being swept into the whirlpool. Battered from without, the industry at the same time is challenged from within by the rapid aging of Japan's population. The life insurance industry today is in the midst of an unprecedented era of change.

Change is coming in many ways. Life insurance companies are evolving into one-stop financial centers offering high-yield financial products to their customers. At the same time they are taking upon themselves the tasks of public welfare, meeting the needs of a graying society with medical care and nursing services for the elderly. And all the while they are striving to meet the needs of modern Japan's sophisticated information-oriented society. Not merely responding to the situation, they have learned to profit from it. For in the final analysis what life insurance companies are doing is what any enterprise must do: expand and bolster customer services and bring new products to the marketplace.

New products and their background

At the end of May 1985, the Insurance Study Council submitted recommendations to the Finance Minister on how the life insurance business should be run to meet the needs of a new era. Taking note of progress in financial deregulation and internationalization, the aging of Japan and the shift toward an information-oriented society, the council stated that life insurance firms should depart from their cartel-like collusion and promote market liberalization. But above all, the council concentrated on future product policy. It stressed that life insurance companies should introduce variable insurance and old-age care insurance policies to satisfy newly emerging needs, and that greater flexibility and diversification were needed in the existing line-up of endowment, whole life and term insurance policies. The recommendations devoted considerable space to explaining how variable insurance could satisfy the needs of a new age. They also advised further study into universal insurance, a product increasingly popular in the United States.

The council's recommendations were accepted not only by the Finance Ministry, but by life insurance companies themselves, which quickly translated the abstract proposals into concrete business moves. They developed a succession of new products. Medical indemnity insurance was introduced in April 1986, variable insurance in October. Many companies also offered modified versions of existing insurance policies. Only three months after the recommendations were issued, Meiji Life Insurance Co. began selling a product christened "Nursing." This was a variation on the whole life insurance policy, with an added provision for care annuity to be paid to bedridden elderly people. Meanwhile, two foreign insurance companies new to the Japanese market also introduced their own distinctive new products. All these new products were developed in line with the Insurance Study Council's call for varied and flexible products able to stand up under twin pressures of deregulation and internationalization.

The most popular products in the whole life insurance field are those that give policyholders the option to decide, upon completion of their premium payments, whether to receive in a lump sum the accumulated dividends and refund for surrender, whether to switch them to whole life annuity or annuity certain, or to retain them as whole life insurance as before.

Life insurance companies also introduced a variety of products for women. Most are whole life insurance policies and term insurance with benefits payable to policyholders in life. These are strategic products developed with the following factors in mind: (1) because women live five years longer than men, the premium is cheaper; (2) now that many women have jobs and enforcement of the Equal Opportunities Law has improved their work environment, women's earning power has increased and their financial standing relative to men has improved; and (3) most women seek security in their lives and therefore choose conservative savings-type financial instruments.

What are some of the new products we have been discussing?

Medical indemnity insurance: This insurance product is intended to supplement the national health insurance scheme. Most insurance companies have been selling policies that cover accidental hospitalization or sickness, either under special clauses or as independent products, for years. Medical indemnity insurance, however, comes armed with a new function. In short, it pays for the portion

Insurance companies are offering new products to meet the demands of senior citizens like these.

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of medical expenses not covered by the public health insurance scheme and which must come out of the patient's own pocket. Medical indemnity insurance was developed in line with the Health and Welfare Ministry's desire to have the private sector supplement the social security scheme. How well this insurance will sell depends on how much the portion shouldered by the patient is actually increased. Significantly, simultaneous with the introduction of medical indemnity insurance, nonlife insurance companies introduced medical expenses insurance policies similar in substance to those offered by life insurance firms.

Variable insurance: The star new product of 1986 was, beyond a doubt, variable insurance. Marketed by a dozen companies, it is the most representative of the many products developed to cope with the deregulation and internationalization of financing in the insurance industry.

A major characteristic dinstinguishing variable insurance policies from conventional life insurance policies is that the insured amount is not uniform. Rather, it fluctuates constantly. When profits from the investment and management of the premiums exceed the assumed rate of interest, the portion in excess of the assumed rate is added to the insured amount. Conversely, the insured amount will shrink by the margin of any losses. However, it comes with a guarantee that in the case of death or serious disability, the claims to be paid will not be smaller than the insured amount specified at the time of the contract. When profits not related to assets management, such as mortality profits or loading surpluses, arise, they will also be recycled to the policyholder as is the case of assurance of fixed sums. Technically, however, such profit is only added to the insured amount during the specified period after the settlement of accounts is made each year.

Variable insurance was developed as a hedge against inflation. The collected premiums are invested in securities, mainly stocks, to realize capital gains. Introduced about 20 years ago in Europe and the United States, variable insurance was researched in Japan for more than a decade before it was finally commercialized. What suddenly brought variable insurance into the spotlight in Japan was not the need to hedge against erosion of assets from inflation, as was the case in Europe and America, but the need to develop a high-yield insurance product to satisfy consumers' desire to benefit from financial deregulation.

Variable insurance has no advantage over assurance of fixed sums such as endowment and whole life insurance unless its yield exceeds an average 9% annually. Since the assumed rate of interest of variable insurance is more than 1% lower than that of assurance of fixed sums (or 4.5%), the premium is therefore 10–15% higher than that of assurance of fixed sums. Fund managers in charge of variable insurance assets are constantly striving to ensure an average annual yield of 10%.

The unprecedented appreciation of the yen has brought on an era of low interest rates. Life insurance companies cannot help but suffer from diminishing yields on their managed assets due to falling interests on loans, securities, deposits and savings. In fiscal 1987 they will have to cut the interest surplus dividend by about 0.5%. The relative advantage of variable insurance, which is not affected by such environmental change, over assurance of fixed sums is expected to increase in the future.

Foreign life insurance firms' entry into market and its impact

There have been three growth periods for foreign life insurance companies in the Japanese market.

During the initial period, unlike today, there were no restrictions on foreign life insurance companies' entry into Japan. However, as a "backward country," Japan was not an attractive market. From an insurance standpoint the Japanese people were poor risks, while their lack of knowledge about the insurance business and the country's low economic level militated against market participation.

In the Taisho and early Showa periods (1912–1945), Japan's economy grew and living standards rose. But then foreign insurance companies could not compete with Japanese counterparts that conducted "human wave" marketing, mobilizing a huge army of life underwriters. Many life insurance firms from the United Kingdom and the United States set up shop in Japan, but their combined market share barely exceeded 3%.

After World War II, Japan developed into a promising and attractive insurance market subsequent to the country's economic resurrection and rapid growth. But the Finance Ministry, which gave top priority to protecting and fostering domestic life insurance companies, did not allow foreign life insurance companies to do business in Japan until well after the liberalization of trade and capital transactions.

The first foreign life insurance company allowed to sell yen-denominated insurance policies to Japanese under the Foreign Insurance Dealers Law was Alico Japan, which was authorized in December 1972. Later, American Family Life Assurance Co. of Columbus and Combined Insurance Co. of America gained entry into the Japanese market in 1974 and 1981, respectively.

In 1975, Seibu Allstate Insurance Co. was established in Japan under the Insurance Business Law as a 50–50 Japan-U.S. joint venture. Similarly, Sony Prudential Life Insurance Co. was founded in 1979. A wholly-owned foreign subsidiary in Japan, INA Life Insurance Co., was licensed in 1981. Until recently, all foreign companies were American. But in March 1986, the Dutch company Nationale-Nederlanden Levensvergekering Maatschappij N.V. established a Japan branch called National Life Insurance. At the end of 1986, a total of nine foreign life insurance companies were engaged in business in Japan.

In gaining access to the Japanese market, all of these companies prepared unique products to satisfy the Finance Ministry's condition that "they should bring fresh air into the Japanese insurance business." One such product was nonparticipating insurance. All Japanese companies, regardless of whether they are joint-stock companies or mutual companies, offer participating insurance policies. Nonparticipating insurance does not pay dividends, but from the outset its premium is smaller than that paid on participating insurance.

Another unique life insurance policy that foreign companies brought into Japan is the cancer insurance offered by American Family Life. Sickness insurance was developed in Japan before American Family entered the market, but not cancer insurance. Cancer insurance was a far greater success in Japan than anyone had expected. Within five years, American Family Life has sold as many as 1.64 million policies, with contracts amounting to ¥5.3 trillion.

From the beginning, foreign companies' sales approaches have been different from those of Japanese insurance firms. Whereas the 20 Japanese companies depend solely on hordes of life underwriters—as many as 350,000, it is said—foreign and joint-venture companies resort to storefront and mail order sales. Some emphasize agents, while others use their own life planner system. They do so not only because they are critical of the Japanese "human wave" strategy, which they are reluctant to copy

Table 1
Contracts Concluded in Fiscal 1985

Personal insurance

New contracts	(1,000 cases)	(¥ billion)
Endowment	5,000	25,755.6
Term insurance	1,860	17,662.6
Whole life	2,300	34,305.7
Savings-type	750	539.6
Others	2,560	7,240.5
Subtotal	12,470	85,504.0
Pension insurance	500	2,267.1
Grand total	12,970	87,771.1
Old contracts in force		
Total	90,870	610,828.2

Group insurance contracts in force

	(1,000 persons)	(¥ billion)
Insurance against death	257,750	270,139.3
Pension insurance	77,400	9,472.1
Total	–	279,611.4

Table 2
Foreign and Foreign Joint-venture Companies

Name of company	Principal products	Start-up in Japan
Alico Japan (American Life Insurance Co.)	New sickness insurance Group term insurance	Dec. 1972
American Family Life Assurance Co. of Columbus	New cancer insurance Dementia care insurance	Oct. 1974
Combined Insurance Co. of America	Term insurance	Dec. 1981
Seibu Allstate Life Insurance Co.	Nonparticipating term insurance Nonparticipating whole life insurance	Dec. 1975
Sony Prudential Life Insurance Co.	Term insurance Whole life insurance	Aug. 1979
INA Life Insurance Co.	Term insurance Whole insurance Cancer insurance	July 1981
United of Omaha Life Insurance Co.	Sickness term insurance	Oct. 1985
National Life Insurance (Nationale-Nederlanden Levensvergekering Maatschappij N.V.)	Joint life annuity Sickness term insurance	Mar. 1986
Equitable Life Assurance Co.	Variable insurance	Oct. 1986

because of the difficulty of recruiting, organizing and training such huge numbers of sales personnel, but also because their principal products are not savings-type insurance but rather sickness and mortality policies.

The combined market share of the nine foreign companies in Japan (of which two had just gained entry into the Japanese market in fiscal 1985) totaled about 10 million policies, with a contract value of approximately ¥10 trillion, 4% and slightly more than 1% of the total market, respectively. Their combined premium incomes totaled ¥245 billion, or 1.7%, and net assets ¥465 billion, or about 1%. Such tiny shares are natural given the fact that they are late starters in Japan, even the oldest having only been here 14 years, with low recognition levels among the Japanese public and limited sales power. But it also reflects a Japanese preference for financial products that double as savings, while most policies sold by foreign companies provide security, not savings.

The situation may yet change. As society ages, people will expect private insurance companies to supplement the gradually increasing share of medical expenses that public health insurance subscribers have to pay out of their own pockets. This will help foreign insurance companies, which already stress medical insurance. Moreover, the variable insurance that appeared in October 1986 was entirely new to Japanese insurance companies. Foreign firms have 10 years' experience and a solid business record in this field, giving them a relative advantage over their Japanese competition.

As financial deregulation progresses, American and European life insurance companies will continue to enter the Japanese market. Discerning consumers will not hesitate to purchase products offered by foreign companies if they are superior to what is already available.

Foreign insurance companies have never been and are not at present a threat to Japanese insurance firms. Most likely their share of insurance in force and premium income will never exceed 10% and 5%, respectively. But the stimulation they give Japanese companies with their new products, new sales methods and fresh business management—and the warning they sounded to the collaborative and complacent way of Japanese insurance management—should not be underestimated. As outsiders, foreign insurance firms will continue to demonstrate their value, all the more so as the pace of deregulation in the life insurance business accelerates.

Japanese consumers at large, who have learned the merits of life insurance as a financial instrument, will clamor for the introduction of universal insurance, which has already swept through the American market. The Insurance Study Council, in its recommendations, described universal insurance as "a compound product having a great variety of characteristics, including flexibility in premium payment; this is worthy of study by insurance companies when they develop new products."

As the graying of Japan progresses, insurance policies will appear that provide actual services, such as nursing care for bedridden senior citizens. The single premium endowment will lose its present popularity as a result of reduced interest surplus distribution and imminent tax reform. Whole life insurance, providing nursing and other real services, will take the top position among insurance products capable of satisfying the diversified needs of Japanese consumers. ●