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Japanese life insurers

No policy is the best policy

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The condition of Japan's life-insurance industry is not improving

SIX Japanese life insurers have gone bust in the past three years. Like their counterparts elsewhere, Japanese firms are locked into unprofitable long-term contracts. Sold in the bubble years, these promise to pay high rates of return, far above what life insurers can earn at a time of ultra-low interest rates and deflation. On November 26th, the top seven Japanese insurers showed that they have still found no way out of this dilemma. They predicted that they would lose ¥1.1 trillion ($9 billion) in the year to March 2003—extending a decade-long run of losses.

Policyholders are responding by cancelling policies, putting fresh pressure on the insurers. But they may soon have even more to worry about. The industry's policyholder-protection fund, set up in 1999 with ¥560 billion of contributions from the industry and a promise of another ¥400 billion of public funds (for a limited period), is about to run out of money. Most of the industry's funds have now been used up, while the state's portion expires next March. The government must decide whether to extend its contribution by the end of December, when it draws up its budget for the next fiscal year.

Life and near-death
Japanese top seven life insurers

	Unrealised gains/losses on domestic equity portfolios, ¥ bn		Operating profits, ¥ bn
	30/3/02	30/9/02	Mar-Sept 02
Nippon Life	1,722	1,048	265
Dai-ichi Mutual	379	31	176
Sumitomo Life	-283	-384	134
Meiji Life	306	132	121
Yasuda Mutual	-33	-84	90
Mitsui Mutual	-144	-230	53
Asahi Mutual	-106	-211	29

Source: Company reports

The life insurers are bracing for a big fight. Regulators want them to contribute more in return for an extension, something the battered industry can ill afford. Some officials point to new bankruptcy laws, which have allowed the latest three collapsed insurers to find buyers for their operations quickly, bypassing the protection fund. Industry folk say this does not mean that fresh bankruptcies will be resolved as swiftly, especially if they are of bigger insurers. Besides, they add, an empty protection fund could further erode confidence.

One reason why the government may find it hard to be tough is that the life insurers have linked their fortunes to the big banks, which are also in a terrible state. Life insurers prop up their solvency margins—measures of their capital adequacy—by turning to banks for loans. In turn, they help out the banks by lending them money and buying their shares.

Take Sumitomo Life, the third-largest life insurer, and Mitsui Mutual, the seventh; both have close relationships with Sumitomo Mitsui Banking Corporation (SMBC). According to the Japan Centre for Economic Research and Mitsuhiro Fukao of Keio University, at the end of March SMBC had provided ¥150 billion-worth of funds to the two insurers. It is also thought to have lent up to ¥760 billion more in subordinated debt, pushing its exposure to the two to some 16 times its net profit. The two insurers, in turn, held about ¥160 billion-worth of the bank's shares.

Other life insurers and banks have similar relationships, which is why many people worry that a big bankruptcy in the life-insurance industry could bring down a bank, and vice versa. That might be why regulators and politicians are mulling over an idea that would help the life insurers by forcing them to lower their guaranteed rates of return. But this would be tantamount to a default, says Standard & Poor's, a credit-rating agency.

What is more, such a proposal would not be easy to implement. Nippon Life, the biggest life insurer, bitterly opposes the plan. With most Japanese owning several life-insurance policies each, the proposal would also be hugely unpopular. Besides, asks Mr Fukao, why should policyholders, who in bankruptcy proceedings have precedence over subordinated-debt holders, lose out first?

In any case, the government needs to tread carefully. Past experience has shown that its efforts, even though well-meant, often end up highlighting the industry's woes and scaring off customers. For the life insurers right now, that may be the deadliest threat of all.