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# Japan's Life Insurance Companies

## A Look at FY97 first-half results

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*The collapse of Nissan Mutual Life Insurance had a major impact on first-half earnings at Japan's life insurance companies, with the outstanding balance on personal life insurance policies falling for the first time since the end of WWII.*

*The industry may well turn out to be unable to stem the outflow of dissatisfied consumers unless it starts to make a determined effort to disclose pertinent and correct information, including negative factors such as the amount of nonperforming assets.*

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### 1. First decline in personal life insurance policies since WWII

The collapse of Nissan Mutual Life Insurance highlights the very tough environment that Japan's life insurance companies find themselves in this term, as the economy and investment environment remain in the doldrums. Last year, the cut in assumed interest rates on group annuities spawned a move within the corporate pension segment to be more selective about choosing life insurance companies. With Nissan Mutual Life going to the wall, an event that had a major negative impact on many holders of personal policies at the company, this tendency has spread to the area of personal insurance policies as well.

Figure 1 shows the relationship between the balance of outstanding policies and latent gains/losses on equity holdings in FY96 and FY97. Various factors in combination can be used to assess the financial well-being of a life insurance company, but here we have used latent gains on equities (in this case, the value of the Nikkei Average when such gains are zero) which provide a relatively easy-to-measure benchmark, and which can be found in various newspapers and publications.

It can be seen that, in the case of group annuities, growth in the number (value) of policies is small in both FY96 and the first half of FY97 at companies where latent gains on equities were small. Thus, it is clear that the move towards a more stringent selection of companies, that became apparent in FY96 as a result of the cut in assumed interest rates, has continued into FY97. On the basis of FY97 figures, this trend appears to have spread to the personal insurance segment too, although it was not noticeable during FY96.

However, there is a more serious problem, namely the mounting lack of public confidence in the life insurance sector as a whole, a phenomenon that has manifested itself in the first decline in the value<sup>1</sup> of personal insurance policies since the end of WWII. When public confidence was

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<sup>1</sup> The first decline in numbers was recorded in FY96.

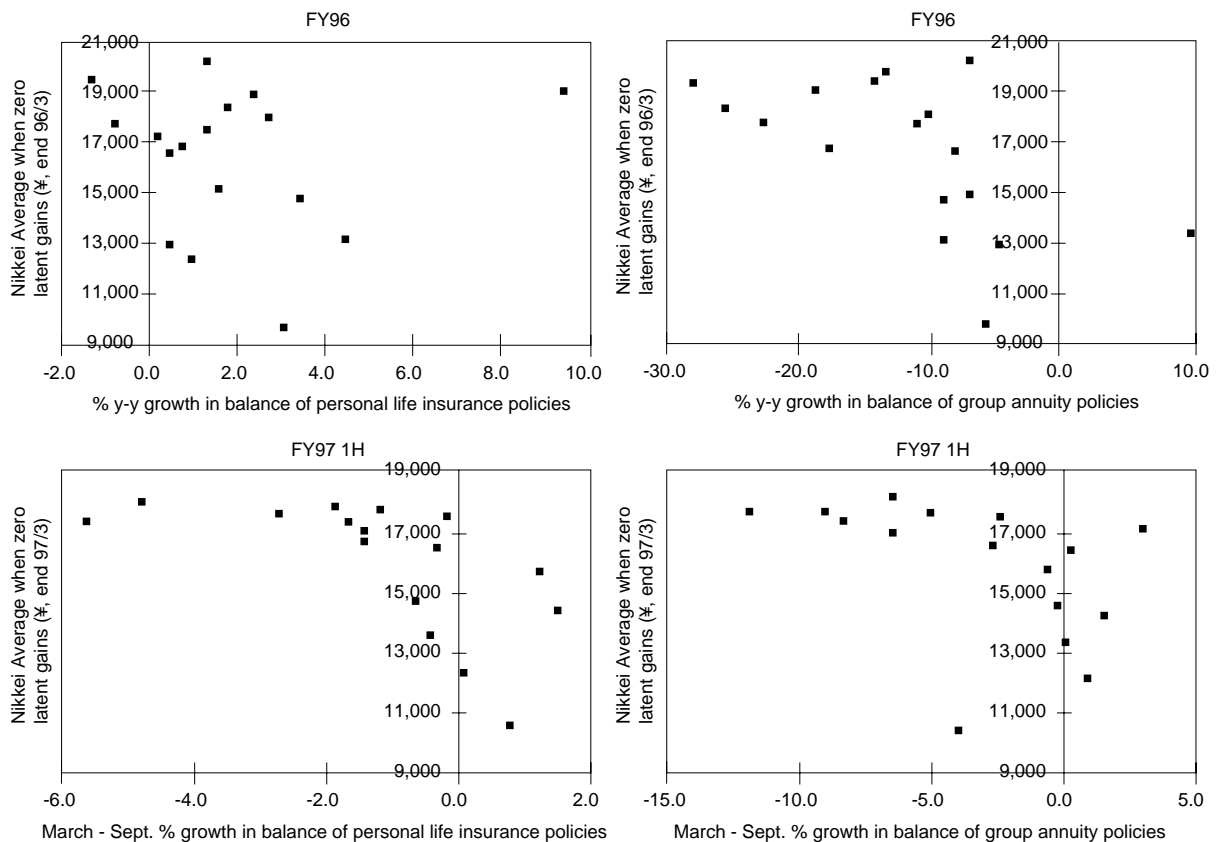
**Table 1. Balance of insurance policies in force at major life insurers  
as of end-September 1997**

(¥ bn, %)

	Balance of insurance policies								
	Personal insurance		Personal annuities		Group insurance		Group annuities		
		vs end-March		vs end-March		vs end-March		vs end-March	Chg in value
Nippon	343,146.6	0.1	17,022.4	-0.2	75,073.5	-23.8	10,287.1	0.8	84.4
Daiichi	241,577.1	-0.5	7,853.1	-0.9	57,949.0	-16.4	7,891.7	-0.1	-8.6
Sumitomo	222,731.3	-0.1	11,955.8	-0.0	45,994.1	-24.2	5,571.5	-2.5	-145.5
Meiji	136,507.7	-0.4	8,833.1	-0.5	50,095.2	-26.5	5,312.8	0.0	0.8
Asahi	92,502.5	-1.3	8,506.9	-2.6	27,943.7	-20.5	3,184.2	-2.7	-86.9
Mitsui	77,537.5	-1.5	2,747.4	2.6	33,366.6	-13.1	3,546.2	2.8	95.6
Yasuda	78,347.4	-0.2	5,016.4	-1.0	63,711.5	-4.1	3,524.9	0.1	4.9
Chiyoda	42,596.3	-4.5	1,994.2	-5.1	19,692.3	-14.4	2,253.7	-4.4	+103.6
Taiyo	10,539.0	0.8	4,675.4	0.9	9,469.0	-13.3	671.5	-4.2	-29.3
Toho	22,092.0	-5.5	2,573.1	-7.7	13,114.0	-4.7	1,102.8	-8.2	-98.7
Kyoei	49,271.9	-1.2	1,778.4	1.0	17,250.1	-11.1	853.0	-9.0	-84.6
Daido	38,099.1	1.3	1,229.5	-1.0	14,653.6	-18.7	2,314.2	-0.5	-12.3
Nippon Dantai	13,655.9	-1.3	3,534.0	-5.9	20,912.5	-4.1	1,386.5	-5.8	-84.7
Fukoku	33,261.5	1.5	2,591.8	-0.2	11,645.1	-6.9	1,534.0	1.3	20.1
Daihyaku	21,792.7	-2.7	1,565.5	-1.1	7,049.9	-20.3	632.0	-11.4	-81.1
Tokyo	7,063.2	-1.7	781.2	-5.8	8,585.2	-6.0	459.2	-5.7	-27.9
Total	1,430,721.7	-0.6	82,658.2	-1.1	476,405.3	-17.0	50,525.3	-1.1	-557.4

Source: Based on materials supplied by individual companies.

**Figure 1. Growth in number of insurance policies and latent gains on shareholdings**



Source: Based on materials supplied by individual companies.

eroded in the troubled bank sector, funds flowed into the biggest banks, such as Bank of Tokyo-Mitsubishi. However, this pattern has not been repeated in the life insurance sector. Even the biggest and healthiest of the Japanese companies, Nippon Life, saw a mere 0.1% increase in the value of personal insurance policies between March and September last year.

All the life insurance companies are faced by a large number of maturing single-premium endowment insurance policies that they marketed during the bubble period, and their inability to prevent people from drawing down these funds is, we believe, one reason why there has been such poor growth in the balance of policies. With Japanese interest rates at such low levels, there is a tendency among consumers to seek greater liquidity in managing funds. In this respect, products marketed by life insurance companies, which by their very nature tend to be relatively illiquid, are far inferior to the choices offered by banks. For example, in the case of a 10-year single-premium endowment insurance policy, it can take more than a year to get back the principal if the policy is terminated before maturity<sup>2</sup>. To make matters worse, the depressed investment environment means that the companies are unable to offer attractive yields<sup>3</sup>.

Herein lies one of the reasons for the fall in the number of policies and the sluggish growth in assets. As maturing single-premium endowment insurance policies are expected to climb to a peak in FY98, conditions surrounding the life insurance sector are unlikely to improve for about two years, unless there is a dramatic change in the investment environment.

## 2. Fluctuations in assets and asset management

Total assets at Japanese life insurance companies (43 companies excluding Aoba Life Insurance) grew by around ¥3 trillion half on half in the first half of FY97, a rise of 1.6%. These figures included fluctuations in receipts on collateral involved in repo transactions and customers' liabilities for acceptances and guarantees, so to examine the increase in assets in real terms, we looked at the 16 majors (companies with total assets of over ¥1 trillion, excluding Aoba Life Insurance). Total assets at the 16 majors rose by ¥2.5 trillion, or 1.4% half on half. This is 0.2 percentage point lower than all-company growth. In real terms (ie excluding the impact of receipts on collateral involved in repo transactions and customers' liabilities for acceptances and guarantees) assets grew by ¥1.5 trillion, which only represents 0.8% half-on-half growth (Table 2).

Life insurers' assets grew by only 0.6% (and fell by 0.2% in real terms) in FY96, so to that extent FY97 has shown some degree of recovery. That said, we must not forget that FY96 figures were skewed by major outflows of pension fund assets, in particular the outflow of around ¥4.1 trillion in Pension Welfare Service Public Corporation funds. FY97 growth is also extremely low in historical terms - total assets grew by 5.4% in FY95, and 5.2% in FY94.

Pension fund assets alone decreased by around ¥550 billion in the first half of FY97, while pension fund assets on general account fell by around ¥1.34 trillion over the same period (of which ¥780 billion remained in the special account). In FY96, pension fund assets fell by around ¥5.5

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2 As life insurance premiums and administrative costs are included in single-premium endowment insurance policies, these are deducted from any monies returned in the event of the policy being terminated shortly after its inception.

3 For a policy taken out on 1 April 1997, the assumed dividend yield is 1.83%. (Source: Monday Nikkei in the *Nihon Keizai Shimbun*)

**Table 2. Change in total assets and group annuity assets**

(¥ bn, %)

	Total assets					Change in group annuity assets		
		vs end-March(value)	vs end-March(%)	Change, excl.repo collateral & customers' liabilities for acceptances and guarantees	vs end-March(%)		of which, general acct	of which, special acct
Nippon	41,029.9	991.7	2.5	814.8	2.1	84.4	-159.4	243.8
Daiichi	28,759.9	727.4	2.6	463.6	1.7	-8.6	-203.8	195.2
Sumitomo	24,048.4	658.3	2.8	458.4	2.0	-145.5	-255.5	110.0
Meiji	16,808.0	98.9	0.6	123.9	0.7	0.8	-41.2	42.0
Asahi	12,071.9	57.9	0.5	-5.8	-0.0	-86.9	-143.0	56.1
Mitsui	10,521.9	313.4	3.1	194.4	1.9	95.6	42.7	52.9
Yasuda	9,369.1	135.7	1.5	136.2	1.5	4.9	-41.4	46.3
Chiyoda	5,822.1	5.9	0.1	-188.8	-3.3	-103.6	-140.3	36.7
Taiyo	6,761.8	58.3	0.9	39.4	0.6	-29.3	-21.3	-8.0
Toho	4,214.8	-294.7	-6.5	-294.7	-6.5	-98.7	-86.5	-12.2
Kyoei	5,585.1	-139.9	-2.4	-139.9	-2.4	-84.6	-80.5	-4.1
Daido	5,152.2	93.1	1.8	54.1	1.1	-12.3	-19.0	6.7
Nippon Dantai	3,966.7	-80.6	-2.0	-80.6	-2.0	-84.7	-84.7	0
Fukoku	4,207.3	79.0	1.9	79.0	1.9	20.1	5.3	14.8
Daihyaku	3,185.1	-133.6	-4.0	-133.6	-4.0	-81.1	-82.2	1.1
Tokyo	1,426.7	-41.8	-2.8	-41.8	-2.8	-27.9	-28.6	0.7
Total	182,931.0	2,528.8	1.4	1,478.6	0.8	-557.4	-1,339.5	782.1

Source: Based on materials supplied by individual companies.

trillion across the industry, and as we stated earlier, public pension funds (the Pension Welfare Service Public Corporation) accounted for around ¥4.1 trillion, with the remaining ¥1.4 trillion flowing out of private-sector funds. As a result, FY97 figures indicate that asset outflows are still continuing from private-sector pension funds. Furthermore, holding on to assets in the special account should become more difficult in the future, now that the disposal of Nissan Mutual Life Insurance has placed a burden on the special account too. In addition, fluctuations in pension fund assets vary appreciably among individual life insurers, with some companies experiencing major falls in their assets, owing to substantial pension fund asset outflows.

Falling interest rates in FY97 saw life insurers shift from JGBs to low-liquidity, high-yield corporate and municipal bonds in order to boost their return on assets. At the 16 majors, the balance of JGBs fell by ¥930 billion half on half, while the balance of other public and corporate bonds rose by the broadly equivalent figure of ¥1.09 trillion.

In addition, the widening gap between Japanese and overseas interest rates and the trend towards yen depreciation have (as of FY96) continued to prompt increased investment in overseas securities. At the 16 majors, the balance of overseas securities rose by around ¥1.8 trillion half on half, which is about the same as the overall increase in assets. This figure includes yen-denominated overseas securities (samurai bonds) and instruments for which forward exchange contracts have been concluded (and the conversion rate is a known quantity). The balance of purely foreign currency-denominated assets subject to with exchange rate risk (including other assets such as deposits in foreign currencies) increased by ¥1.5 trillion half on half.

The 16 top-tier companies also increased their exposure to foreign currency-denominated assets by a hefty ¥2.8 trillion in FY96. As a trend, the smaller the latent profits on securities held (as a proportion of total assets), the more aggressive has been the move into foreign currency-denomi-

**Table 3. Assets on general account (as of end-September 1997)**

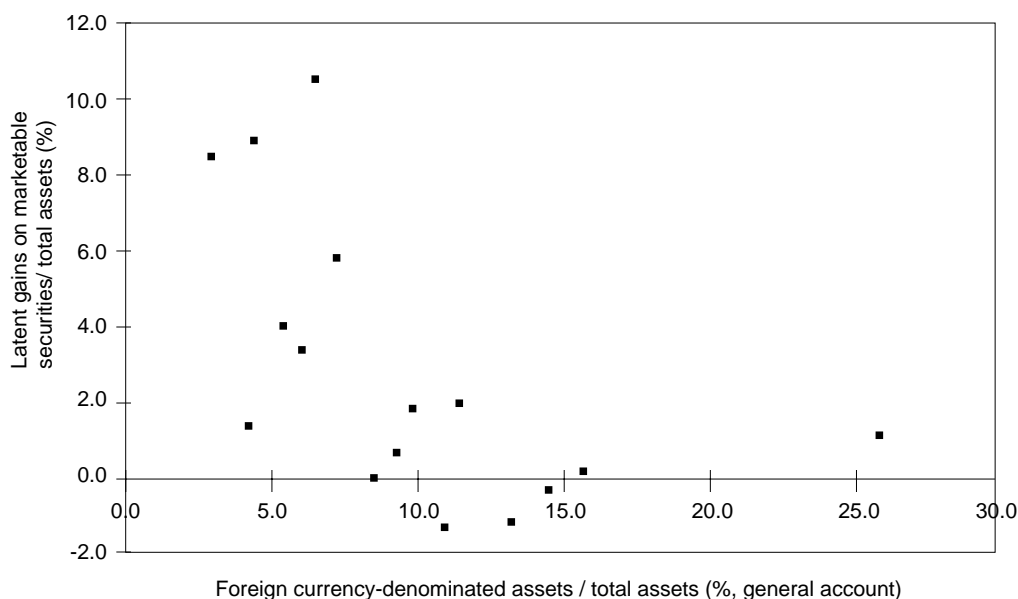
(¥ bn, %)

	Cash & deposits / call loans			Public bonds			JGBs			Other			Lending		
	share	chg vs end- March	chg in value	share	chg vs end- March	chg in value	share	chg vs end- March	chg in value	share	chg vs end- March	chg in value	share	chg vs end- March	chg in value
Nippon	4.3	-0.6	-209.1	23.4	1.1	596.0	13.6	0.8	419.9	9.8	0.3	176.1	36.9	-0.3	156.1
Daiichi	4.0	1.1	312.4	24.0	0.8	339.1	13.2	-0.2	24.7	10.8	0.9	314.5	31.4	-1.8	-309.6
Sumitomo	8.2	2.5	608.2	28.4	-1.4	-161.6	22.2	-1.7	-256.2	6.3	0.3	94.6	30.1	-1.7	-222.9
Meiji	2.8	-2.7	-431.6	21.4	0.8	139.5	13.1	-1.0	-145.6	8.2	1.8	285.3	38.3	0.1	33.7
Asahi	6.7	0.9	97.5	15.6	-2.6	-292.1	12.5	-3.8	-434.2	3.1	1.2	142.0	36.2	-0.9	-96.7
Mitsui	8.0	2.5	2,57.1	11.2	-3.5	-301.2	7.2	-2.0	-166.1	4.0	-1.6	-135.0	40.3	-2.2	-99.5
Yasuda	1.8	-2.5	-2,17.8	14.7	-1.1	-84.8	9.7	-1.5	-122.3	5.1	0.4	37.3	40.4	-0.5	-6.6
Chiyoda	4.2	-0.7	-38.0	10.4	0.2	5.7	10.0	0.1	3.1	0.3	0.1	2.6	46.0	-1.6	-100.9
Taiyo	9.7	-0.4	-22.3	24.2	0.0	16.4	11.1	-2.0	-123.5	13.2	2.0	139.9	40.0	-1.4	-65.3
Toho	6.3	1.7	57.4	12.4	-1.3	-94.4	3.6	-2.5	-119.3	8.9	1.1	24.9	34.1	-1.4	-156.7
Kyoei	7.3	-1.0	-67.6	22.1	0.3	-11.1	12.3	0.9	37.0	9.9	-0.6	-48.1	40.3	0.1	-48.2
Daido	5.8	-0.6	-25.4	44.5	-0.2	31.9	12.4	-2.2	-93.9	32.1	2.0	125.6	27.1	-0.6	-2.6
Nippon Dantai	5.1	-2.1	-89.8	9.0	-3.1	-130.5	6.1	-1.2	-53.3	2.8	-1.9	-77.3	38.5	-0.8	-62.4
Fukoku	7.8	-1.1	-39.1	21.9	3.1	136.9	7.8	2.8	119.0	14.1	0.2	18.0	35.5	-0.0	21.6
Daihyaku	1.9	-2.7	-89.5	16.9	-0.3	-32.3	14.4	0.3	-11.3	2.5	-0.6	-21.1	39.9	0.1	-50.8
Tokyo	3.8	-3.4	-49.6	10.1	0.3	0.1	7.5	-0.6	-11.0	2.5	0.9	11.1	33.1	-1.7	-38.5
Total	5.3	-0.0	52.7	21.7	-0.1	157.6	13.1	-0.7	-933.0	8.5	0.5	1,090.6	35.8	-1.0	-1049.3

	Shares			Foreign securities			General account total		
	share	chg vs end- March	chg in value	share	chg vs end- March	chg in value	end- Sept. balance	chg vs end- March	of which, forex-denom assets share chg in vs end- value March
Nippon	17.6	-0.4	-10.7	8.6	0.1	104.4	39,124.1	777.3	6.6 0.2 124.9
Daiichi	18.7	-0.4	-19.1	9.3	0.6	215.6	27,561.9	537.8	7.0 -0.1 23.9
Sumitomo	14.5	-0.8	-89.4	7.4	-0.2	3.3	22,986.7	550.8	4.4 -0.8 -149.9
Meiji	20.0	-0.2	-22.9	5.6	2.0	326.3	16,037.7	60.6	4.8 1.5 246.0
Asahi	22.1	0.1	12.9	9.2	0.5	55.9	11,411.1	2.6	9.2 0.6 63.9
Mitsui	18.2	-1.2	-64.4	9.4	4.5	446.2	9,662.6	262.2	9.3 4.6 451.1
Yasuda	16.4	-0.3	-15.0	13.0	2.7	249.3	9,009.2	90.4	10.8 2.8 259.3
Chiyoda	16.7	-0.3	-21.2	8.8	1.2	64.1	5,438.4	-29.6	8.0 1.1 58.6
Taiyo	11.3	0.0	10.3	5.9	0.8	54.2	6,677.8	66.0	3.0 0.7 50.2
Toho	11.1	-0.3	-46.4	16.7	1.4	12.5	4,119.9	-281.9	15.7 2.0 43.4
Kyoei	6.5	0.4	12.8	14.0	-1.2	-85.8	5,504.0	-135.5	13.0 -1.5 -101.6
Daido	7.6	-0.7	-29.1	6.7	1.2	63.1	4,890.2	87.8	5.5 1.8 91.2
Nippon Dantai	9.0	-0.6	-33.1	29.5	6.7	246.0	3,950.5	-80.6	25.5 6.2 228.2
Fukoku	13.0	-0.1	2.3	8.8	-0.4	-9.1	4,079.5	63.3	6.0 0.4 21.2
Daihyaku	16.2	1.0	10.3	11.5	1.5	31.3	3,053.3	-133.7	10.4 1.1 20.6
Tokyo	18.5	-0.6	-16.5	18.6	4.6	56.8	1,365.3	-42.3	14.6 3.5 42.6
Total	16.5	-0.4	-319.1	9.4	1.0	1,834.0	174,832.3	1,795.3	7.6 0.8 1,473.8

nated assets. Yen depreciation has enabled life insurers to secure major exchange rate gains, but there must be question marks over whether sufficient risk control is being exercised in investments, given that the forex market can fluctuate wildly in a short space of time. (Figure 2)

**Figure 2. Latent gains on marketable securities and investment in foreign currency-denominated assets**



Source: Based on materials supplied by individual companies.

### **3. Insurance payout/premium balances, asset management balances, and current account balances**

Total insurance premium income at the 16 majors fell 1% year on year in the first half of FY97 (Table 4). Policy cancellation payouts fell considerably year on year at a number of companies because of the large number of cancellations by pension funds the previous year, but the balance (insurance payouts / premiums x 100) was still over 100 for companies that saw only a small decrease in cancellation payouts and companies where cancellation payouts continued to increase.

Life insurers maintain liability reserves to cover all payments they will have to make. They also have 20-30% of their total assets in the form of highly liquid assets such as cash & deposits, JGBs and equities. This means that they are unlikely to find themselves unable to make the necessary payouts immediately, even when their payout/premium balance is more than 100. However, if their assets continue to decrease at the current rate, the companies will not only be distressed by payouts, but also assets with unrealised losses, such as nonperforming assets, might come to account for a greater proportion of their total assets.

Income from interest and dividends on investments at the 16 majors fell by 2.4% in the first half of FY97, because of the fall in market interest rates, poor corporate earnings, and the decrease in life insurers' own assets. Some companies have already started to realise profits on the sale of securities. For example, Sumitomo Life Insurance, faced with the fall in interest rates and the need to dispose of its nonperforming assets, has written down a large amount of profits on the sale of bonds. In addition, the weakening of the yen has made forex-denominated assets more valuable, but we think that the life insurers are still holding back from taking profits on these investments, although they will have sold some overseas securities in order to secure profits.

The Nikkei Average was 17,888 at the end of September 1997, 115 points lower than at the end

**Table 4. Balance on insurance operations (as of first half of FY 97)**

	1. Premium income		2. Payouts				2 ÷ 1 x 100
		% y-y		% y-y	of which, repaid on early termination		
						% y-y	
Nippon	2,935.6	0.8	2,393.6	-17.9	626.1	-50.7	81.5
Daiichi	1,938.6	1.1	1,664.5	-23.6	462.2	-53.4	85.9
Sumitomo	1,656.9	-1.9	1,610.9	-19.6	367.2	-50.9	97.2
Meiji	1,230.1	0.4	1,109.9	-30.4	208.6	-58.9	90.2
Asahi	836.9	-3.5	871.9	-35.9	223.8	-64.4	104.2
Mitsui	904.6	10.1	743.4	-28.8	230.9	-50.5	82.2
Yasuda	770.8	4.5	644.7	-34.2	164.9	-63.6	83.6
Chiyoda	423.7	-2.6	641.7	-40.1	227.3	-55.8	151.5
Taiyo	617.1	-1.0	646.7	11.1	123.6	-17.5	104.8
Toho	262.2	-13.3	593.8	-16.6	301.7	8.3	226.5
Kyoei	396.2	-9.7	513.6	-7.9	178.5	17.0	129.6
Daido	548.1	-2.1	444.1	-31.5	113.4	-64.3	81.0
Nippon Dantai	316.0	-1.9	452.8	11.2	184.4	69.7	143.3
Fukoku	355.7	-19.9	287.0	-19.9	76.9	-33.5	80.7
Daihyaku	228.8	-8.2	366.8	-17.8	170.1	-20.8	160.3
Tokyo	84.8	-15.9	146.2	-17.7	48.6	-35.4	172.4
Total	13,506.0	-1.0	13,131.5	-22.9	3,708.4	-47.0	97.2

Source: Based on materials supplied by individual companies.

**Table 5. Return on assets (as of end-September 1997)**

(¥ bn, %)

	Return on assets														
	Interest & dividend income				Proceeds of securities sales										Foreign exchange gains (general account)
					of which, general account										
	% y-y chg	% y-y chg	y-y change in value	y-y change in value	Shares		Bonds		Foreign securities						
Nippon	864.6	8.2	715.2	1.0	108.4	35.1	74.5	15.2	29.4	1.9	11.1	-14.9	33.9	28.2	-
Daiichi	516.4	2.8	431.9	-1.2	61.9	8.8	30.8	-5.9	10.4	-4.5	10.5	-3.3	9.9	1.9	5.8
Sumitomo	696.3	32.9	354.0	-4.6	296.1	157.2	286.1	153.1	42.2	19.5	222.7	115.2	21.1	18.5	0.2
Meiji	291.6	1.3	255.7	3.0	15.7	-10.8	6.7	-15.2	5.9	-15.1	0.3	-0.1	0.4	0.1	-
Asahi	233.0	11.1	169.4	-9.1	51.3	38.0	41.1	30.5	32.1	27.8	7.6	1.5	1.3	1.3	-
Mitsui	223.6	10.7	158.9	-2.3	42.2	14.2	22.7	6.1	10.9	1.9	3.9	2.9	7.8	1.3	-
Yasuda	202.1	16.2	139.3	-5.5	43.1	27.7	38.7	27.1	17.2	14.6	11.5	8.9	9.9	3.5	2.5
Chiyoda	110.5	-16.4	79.0	-4.3	27.2	-20.8	19.0	-25.8	8.2	-20.5	9.0	-3.2	1.7	-2.1	0
Taiyo	137.4	10.5	105.2	-7.8	28.5	20.6	26.9	19.5	11.6	7.0	12.4	10.0	2.8	2.5	-
Toho	95.9	-0.9	71.1	-2.2	20.2	-0.5	18.3	-1.5	14.0	8.3	2.2	-4.9	2.0	-4.9	-
Kyoei	123.6	13.8	83.7	-6.1	37.9	18.9	34.7	16.9	27.8	13.9	2.1	0.5	4.8	2.4	-
Daido	118.3	10.4	95.6	0.3	14.4	4.6	8.3	2.2	0	-1.0	7.2	5.4	1.1	-2.1	-
Nippon Dantai	103.5	8.8	64.7	-9.1	33.6	12.7	33.0	12.5	18.4	6.5	7.4	1.8	7.1	4.2	-
Fukoku	76.0	8.4	64.6	1.1	4.3	2.2	3.2	1.9	0	-0.2	2.1	1.7	1.0	0.4	-
Daihyaku	67.7	6.2	47.8	-5.0	169.6	5.6	13.5	3.7	8.1	-1.0	1.6	1.6	3.6	3.0	-
Tokyo	33.5	-6.2	21.7	-15.9	8.9	0.1	7.4	-0.9	4.5	-3.1	2.1	1.7	0.7	0.6	-
Total	3,894.1	10.2	2,857.9	-2.4	810.3	313.5	664.9	239.3	240.7	55.9	313.8	124.8	109.0	58.8	8.5

Source: Based on materials supplied by individual companies.



of March 1997, but apart from Daido Life Insurance and Nippon Dantai Life Insurance, the life insurers did not write down valuation losses on securities in the first half of FY97, partly because interim results do not have to be de jure as full-year results. Deferred valuation losses amounted to ¥1.9 trillion at 15 majors (Table 6). Life insurers originally write down the value of their bond holdings at cost (except for bonds held on their trading accounts), so we think that equities account for most of the securities on which they chose not to write down the lower of cost of market value, and thus deferred writing down their unrealised losses. At companies with only a small amount of unrealised gains on equities, as much as 60-70% of their equity holdings have a market value that is lower than their book value.

The Nikkei Average continued to fall from the end of September, reaching the year's low of 14,799 on 22 December 1997, so life insurers' unrealised losses grew further. On 24 December 1997, the Ministry of Finance made it possible for life insurers to write down their equity holdings at cost<sup>4</sup>. However, unlike bonds, equities do not mature, and if the price of an equity does not recover, it has to be written down as a loss eventually. This means that equities on which the life insurers have deferred writing down valuation losses are effectively nonperforming assets like nonaccrual loans and loans to bankrupt customers.

However, since deferring losses lowers the market's assessment of a company, and high book values are a disadvantage in terms of solvency margin ratios, companies that can may offset their valuation losses with profits on the sales of securities and profits on forex-denominated assets in the second half of FY97.

**Table 6. Securities to which "lower-of-cost-or-market" is not applied (at end-Sept.97)**

(¥ bn)

	Securities to which "lower-of-cost-or-market" method is not applied				
		Book value		Market value	Latent valuation loss
		as % of total assets	as % of general account shares		
Nippon	2,035.7	5.0	29.5	1,729.8	-305.8
Daiichi	1,931.7	6.7	37.4	1,624.8	-307.0
Sumitomo	1,605.6	6.7	48.3	1,334.0	-271.6
Meiji	791.3	4.7	24.6	662.2	-129.1
Asahi	1,393.9	11.5	55.3	1,162.3	-231.7
Mitsui	960.4	9.1	54.9	808.4	-152.0
Yasuda	1,167.3	12.5	78.9	1,001.1	-166.2
Chiyoda	703.0	12.1	77.4	620.7	-82.3
Taiyo	206.1	3.0	27.3	174.4	-31.8
Toho	309.1	7.3	67.6	253.7	-55.4
Kyoei	230.6	4.1	64.3	191.0	-39.6
Daido	-	-	-	-	-
Nippon Dantai	136.4	3.4	38.5	119.7	-16.7
Fukoku	273.1	6.5	51.4	228.0	-45.1
Daihyaku	355.9	11.2	71.9	298.8	-57.1
Tokyo	154.2	10.8	60.9	134.4	-19.8
Total	12,254.4	6.7	42.5	10,343.4	-1,911.1

Source: Based on materials supplied by individual companies.

<sup>4</sup> This was in response to the credit-crunch by the banks. Lower-of-cost-or-market basket method is to be applied to equities traded short-term (ie, separated out from other equities for appraisal purposes, in the same way as with tokkin); for other stocks, companies have the choice of lower-of-cost-or-market or at-cost methods.



**Table 7. Cost of asset management (as of first half of FY97)**

(¥ bn, %)

	Cost of asset management																
	Losses on securities sold												Loss on securities revaluation		Loss on sec. redemption (gen. acc.)	Exchange loss (gen. acc.)	
	Shares		Bonds		Foreign securities												
	% y-y chg	% y-y chg	% y-y chg	% y-y chg	% y-y chg	% y-y chg	% y-y chg	General acc.	Special acc.								
Nippon	197.2	52.3	43.3	30.3	25.0	18.3	2.9	2.6	4.4	-0.9	17.6	16.5	-	5.5	55.3	4.5	-2.1
Daiichi	136.3	8.5	-	-	-	-	-	-	-	-	-	-	-	1.8	34.9	-	-27.7
Sumitomo	241.0	202.1	71.6	53.7	61.2	45.8	3.6	2.9	46.0	32.5	11.6	10.5	-	4.2	25.9	-	-5.1
Meiji	58.0	-14.8	7.5	4.5	2.0	1.9	1.5	1.5	0.1	0.1	0.3	0.3	-	5.6	26.5	1.1	-21.4
Asahi	35.6	36.3	8.5	5.1	4.4	3.5	0.5	0.4	2.0	1.3	1.9	1.9	-	1.9	5.6	1.6	0.4
Mitsui	61.2	1.6	12.6	4.4	6.5	1.0	1.7	1.5	1.7	0.8	3.1	-1.2	-	3.8	8.8	8.8	-5.1
Yasuda	31.2	63.2	12.7	7.1	10.2	7.0	0.7	0.7	3.1	1.2	6.3	5.1	-	0.6	3.7	-	-
Chiyoda	26.3	35.4	19.8	9.6	-	-	-	-	-	-	-	-	-	0.5	0.4	-	-0.4
Taiyo	10.7	-34.3	0.8	0.5	0.1	-0.1	-	0	0	-0.2	0.1	0.1	-	2.3	3.7	1.6	-8.6
Toho	19.7	47.8	5.3	-0.5	4.3	-0.7	2.0	1.2	0.6	-1.6	1.5	-0.5	-	0.1	0.1	1.2	-0.4
Kyoei	56.4	400.5	39.1	34.0	38.0	33.1	9.2	6.9	1.1	-0.4	27.7	26.6	-	0.4	1.9	11.1	10.1
Daido	64.4	148.4	4.0	0.8	1.2	-1.0	0.4	-0.8	0.4	0.1	0.3	-0.3	35.5	3.1	10.1	2.8	0.7
Nippon Dantai	50.1	59.8	5.0	-11.6	4.9	-11.6	0.4	-8.0	3.2	-4.0	1.2	0.4	11.9	0.5	3.9	13.3	13.3
Fukoku	9.6	27.9	4.3	1.6	3.9	1.2	0.9	0.8	2.7	2.2	0.1	-1.9	-	-	0	1.4	1.1
Daihyaku	28.6	165.2	12.6	8.4	11.3	7.4	1.1	1.0	4.7	2.3	5.4	4.0	-	0.4	4.0	0.3	0.3
Tokyo	8.3	-3.6	3.9	0	3.5	-0.1	3.0	3.0	0.5	-0.7	-	-1.3	-	0.2	0.2	0.7	0.7
Total	1,064.6	58.5	250.9	147.8	176.5	105.7	27.8	13.7	70.5	32.7	77.1	60.2	47.4	31.0	185.0	48.4	-44.2

Source: Based on materials supplied by individual companies.

The current account balance of the 16 majors increased by ¥8.5 billion year on year in the first half of FY97<sup>5</sup>. However, if we adjust this figure to exclude net profits/losses on the sale of securities, we come up with a decrease of more than ¥150 billion year on year, and three companies have a current account deficit, which indicates that they relied on profits from the sale of securities even more than in FY96. Moreover, if we adjust the current account balance figures to exclude deferred valuation losses on securities, only 5 of the 16 companies have positive current account balances (compared to 14 in the first half of FY96), giving a total current account deficit at the 16 companies of ¥360 billion.

<sup>5</sup> The term “current account balance” is used to signify that this figure refers simply to recurring income minus costs, and not to a figure subject to taxation or distribution through dividends. Interim results do not present definitive figures, as simplified accounting methods are used to calculate reserves brought forward and drawbacks, and because some appraisal losses are deferred.

**Table 8. Current account balance (as of first half of FY97)**

(¥ bn)

	Current account balance		Current account balance - Profit / losses on securities sold		Current account balance - latent valuation losses on securities		
		y-y chg in value		y-y chg in value	FY97 1H	FY96 1H	Change in value
Nippon	353.9	-27.1	288.8	-31.9	48.1	362.2	-314.2
Daiichi	198.8	-9.0	136.9	-17.8	-108.2	192.3	-300.5
Sumitomo	322.5	9.0	98.0	-94.5	50.9	297.6	-246.7
Meiji	146.4	15.3	138.2	30.6	17.3	116.6	-99.3
Asahi	80.5	8.4	37.6	-24.6	-151.2	60.3	-211.5
Mitsui	106.5	10.7	76.8	0.9	-45.5	83.4	-128.9
Yasuda	133.8	10.7	103.3	-9.9	-32.4	116.1	-148.5
Chiyoda	35.7	-31.6	28.2	-1.2	-46.6	59.7	-106.3
Taiyo	33.9	22.7	6.1	2.6	2.1	10.4	-8.4
Toho	8.5	0.2	-6.4	0.2	-46.9	-3.3	-43.6
Kyoei	17.6	0.3	18.8	15.4	-22.0	13.3	-35.3
Daido	30.5	-22.2	20.0	-26.0	30.5	52.6	-22.2
Nippon Dantai	13.2	0.8	-15.4	-23.5	-3.5	12.4	-15.9
Fukoku	40.1	13.3	40.1	12.8	-5.1	18.3	-23.4
Daihyaku	19.2	8.0	15.2	10.8	-37.9	6.8	-44.7
Tokyo	3.7	-1.3	-1.3	-1.3	-16.2	-0.8	-15.4
Total	1,544.6	8.5	985.2	-157.2	-366.5	1,398.1	-1,764.6

Source: Based on materials supplied by individual companies.

## 4. Latent gains on securities holdings and bad loans

In this chapter, we will discuss the present state of latent gains/losses on securities holdings and of nonperforming loans, both of which are off-balance sheet items. At the end of September 1997, the Nikkei Average stood at 17,888, 115 points lower than at the end of March 1997. As a result, nine of the 16 majors, saw the latent gains on their stock portfolios shrink, while three companies actually posted losses on their total securities holdings. It should be noted that while some companies suffered a major drop in latent gains, others actually enjoyed an increase. This widening gap between individual companies can be ascribed to the impact of the polarisation of share prices. Latent gains have gone up at companies that mainly hold international blue-chips, the shares prices of which have risen, while gains have shrunk at companies with a high exposure to certain financial, securities and construction stocks, which have fallen substantially. For 10 of the 16 majors, the projected Nikkei Average level at which latent gains become zero is now higher than 16,000, testament to the severity of the situation facing the life insurance industry.

The further drop in interest rates has seen latent gains on bond holdings rise across the board. However, in recent years, companies where latent gains on stock holdings were small have propped up their recurring income levels by taking profits on bonds, thus eroding their financial cushions even further.

Compared to the end of March, the publicly disclosed nonperforming loans at the 16 majors rose by ¥186 billion. This increase can be attributed almost entirely to bankruptcies among debtors, and given that major bankruptcies have continued at an undiminished pace since September, the depreciation burden on these insurers will probably grow heavier still. On the other hand, whereas in March, only two life insurers had reserve ratios against these bad loans of over 100%, by the end

**Table 9. Latent gains / losses on securities**

(¥ bn)

	Latent profit / losses on securities															
				Equities			Bonds			Foreign securities			Other			
				Chg at the end of Mar.	Latent ratio (%)	Nikkei when gains are zero*	Chg at the end of Mar.	Latent ratio (%)		Chg at the end of Mar.	Latent ratio (%)		Chg at the end of Mar.	Latent ratio (%)		
Nippon	4,285.5	253.4	10.4	3,175.7	94.2	47.0	12,168	616.0	139.2	8.2	497.0	20.1	19.1	-3.2	0.0	-4.5
Daiichi	1,825.2	205.3	6.3	1,429.3	155.7	28.3	13,938	258.5	48.4	5.9	140.6	0.2	10.3	-3.2	1.0	-31.9
Sumitomo	346.8	-126.8	1.4	100.6	-20.3	3.1	17,348	202.3	-88.3	3.7	43.8	-18.3	6.3	0.0	0.0	0.0
Meiji	1,493.0	152.6	8.9	1,117.5	55.0	35.7	13,184	180.0	28.2	6.4	195.6	69.5	38.1	-0.1	0.0	-1.9
Asahi	96.9	-88.1	0.8	101.4	-107.2	4.1	17,188	43.0	25.4	3.0	-47.5	-6.3	-5.9	0.0	0.0	-0.0
Mitsui	178.8	39.7	1.7	87.9	9.5	5.2	17,006	34.9	11.2	3.5	56.0	19.0	7.5	-	-	-
Yasuda	167.3	-79.0	1.8	20.9	-118.9	1.5	17,629	46.4	16.6	3.8	100.1	23.3	11.0	-0.1	0.0	-1.2
Chiyoda	4.8	-0.1	0.1	5.0	-6.3	0.6	17,789	9.2	6.3	1.7	4.1	-0.4	1.4	-13.5	0.3	-48.7
Taiyo	577.8	-28.2	8.5	466.7	-39.3	62.6	11,003	100.6	8.5	8.5	19.2	2.8	7.3	-8.7	-0.2	-9.4
Toho	7.4	-8.6	0.2	3.9	-16.8	0.9	17,726	15.0	7.3	4.4	2.3	-1.0	0.7	-13.9	1.8	-37.0
Kyoei	-59.6	-23.1	-1.1	-19.3	-26.9	-5.4	18,919	13.9	11.4	1.2	-7.9	-8.4	-1.5	-46.3	0.9	-21.6
Daido	206.5	29.7	4.0	68.8	13.9	19.2	15,008	123.3	14.2	9.2	14.3	1.5	5.1	-	-	-
Nippon Dantai	41.1	6.2	1.0	36.6	11.0	10.4	16,192	5.9	2.7	2.1	11.5	-7.5	1.4	-12.9	0.1	-26.6
Fukoku	145.4	-4.8	3.5	127.9	-13.0	24.4	14,374	35.6	11.0	6.2	1.8	-2.1	2.0	-19.9	-0.7	-27.2
Daihyaku	-36.4	-29.8	-1.1	-25.8	-35.9	-5.3	18,888	11.1	6.4	2.4	-0.2	-1.1	-1.5	-21.5	0.8	-30.8
Tokyo	-3.7	2.8	-0.3	1.9	1.2	0.8	17,753	1.7	1.4	1.3	-0.7	0.5	-0.4	6.5	12.8	52.8
Total	9,276.9	301.1	5.1	6,699.0	-44.2	23.8	11,003	1697.4	252.0	5.7	1,030.1	91.7	9.9	-136.8	16.7	-17.4

Notes: \*We have assumed that equity holdings remain unchanged from end-September 1997, and that the equity portfolio is perfectly linked to the Nikkei.

Source: Based on materials supplied by individual companies.

of September that number had already risen to eight. Companies with low reserve ratios are not making much headway in writing off their bad loans either, hampered as they are by the shrinkage in latent gains and other resources, and the gap with competitors that already have made such progress is set to grow larger.

6 Main equity includes the following items: funds (capital), legal reserves, voluntary reserves + contingency reserves (both as at 3/31), price fluctuation reserves, general allowances for doubtful debts, the amount of reserves for dividends to policy holders not yet allocated (as at 31 March) and the tax effect on the sum of price fluctuation reserves and the amount of reserves for dividends to policy holders not yet allocated.

**Table 10. Bad lonas as of the end of September 1997**

(¥ bn)

	Disclosed bad loans												Est. value of depreciation	Special bad debt reserve	Reserve ratio
					Loans to bankrupt customers	Nonaccrual loans	Restructured loans		Supported loans						
	change in value at the end of March	as % of ordinary loans	as % of total assets	change in value at the end of March	change in value at the end of March	change in value at the end of March	change in value at the end of March								
Nippon	138.6	49.4	1.1	0.3	71.2	48.5	55.3	0.4	12.1	0.5	-	-	92.8	94.1	101.4
Daiichi	147.9	18.0	1.9	0.5	58.1	20.9	35.2	5.8	54.6	0.5	-	-9.1	84.4	106.0	125.5
Sumitomo	369.4	47.7	6.0	1.5	76.6	27.6	31.8	-5.0	41.9	0.1	219.1	25.0	167.2	185.6	111.0
Meiji	56.5	6.5	1.0	0.3	17.4	6.5	16.3	-0.1	21.8	0.1	0.9	0.0	31.6	37.2	117.8
Asahi	118.3	-33.5	3.1	1.0	37.1	20.3	20.3	2.6	60.9	-6.2	-	-50.1	61.5	34.1	55.4
Mitsui	135.2	16.8	3.7	1.3	93.5	16.1	33.5	3.2	8.3	-2.6	-	-	91.8	100.1	109.1
Yasuda	29.1	11.1	0.8	0.3	17.4	11.2	6.1	0.0	4.1	0.0	1.4	0.0	18.4	22.7	123.4
Chiyoda	202.4	-12.6	8.3	3.5	38.5	-3.7	130.6	2.9	7.2	-0.1	26.0	-11.7	130.0	49.5	38.1
Taiyo	76.9	13.9	3.1	1.1	15.7	13.9	3.2	0.0	58.1	0.0	-	-	33.5	12.7	37.8
Toho	106.8	47.0	8.0	2.5	15.3	11.1	50.7	36.4	40.9	-0.5	-	-	60.5	12.5	20.7
Kyoei	30.6	-0.3	1.4	0.5	23.9	0.4	5.8	-0.6	0.9	0.0	-	-	21.1	18.6	88.2
Daido	54.8	3.3	4.2	1.1	23.8	7.2	20.2	-3.5	10.8	-0.4	-	-	34.6	39.5	114.2
Nippon Dantai	31.7	5.5	2.1	0.8	17.4	-0.7	7.1	3.3	7.2	2.9	-	-	19.7	22.6	114.8
Fukoku	34.1	26.2	2.5	0.8	9.7	8.2	7.3	1.5	17.1	16.5	-	-	17.9	10.8	60.4
Daihyaku	67.1	-6.6	5.8	2.1	21.4	3.3	33.1	-1.2	12.6	-8.7	-	-	42.6	24.6	57.7
Tokyo	11.8	-6.6	2.8	0.8	7.3	4.0	4.6	2.4	-	-13.0	-	-	8.3	3.4	40.5
Total	1611.3	186.0	2.8	0.9	544.3	194.7	461.1	48.0	358.4	-10.8	247.4	-45.9	915.8	773.9	84.5

Note: Estimated value of depreciation =(loans to bankrupt customers + nonaccrual loans+ 1/2 of restructured loans + 1/2 of supported loans + loans to non-banks in Nippon Credit Bank's group) x 0.7

Source: Based on materials supplied by individual companies.

## 5. Equity

In the first half of FY97, four companies (Chiyoda Life Insurance, Toho Life Insurance, Daihyaku Life Insurance and Tokyo Life Insurance) bolstered their equity by attracting new funds. Another two companies (Nippon Life Insurance and Sumitomo Life Insurance) did likewise, just as they had done a year earlier. Furthermore, since most companies boosted their price fluctuation reserves, the ratio of main equity<sup>6</sup> to total assets increased at all 16 majors.

In August, the legal ban on funding through the issue of subordinate loans and bonds by life insurance companies was lifted, but main equity (as defined here) is already close to the maximum amount where such subordinate funds may be counted as equity in the calculation of solvency margin ratios (items such as allowances for losses on trading securities, capital furnished by foreign life insurers, the surrender value surplus and part of tax effect-equivalent amounts are not included). This means that those companies that would still compare unfavourably with the competition even after attracting the maximum possible amount of subordinated funds have to use other ways to lift their solvency margin ratios. These would include increasing the maximum level for funding with subordinate debt through bolstering on-balance sheet equity, decreasing stock holdings and other high-risk assets in order to decrease price fluctuation risk, which accounts for roughly 80% of total risk.

**Table 11. Equity as of the end of September 1997**

(¥ bn)

		*Main equity				Main equity including latent gains on securities		
		vs total assets(%)	Change vs end of March	Increase in funds		vs total assets(%)	Change vs end of March	To price fluctuation + credit risk
Nippon	1,329.8	3.2	0.4	150.0	5,615.3	13.7	0.7	126.7
Daiichi	766.6	2.7	-0.0	-	2,591.8	9.0	0.5	79.6
Sumitomo	718.3	3.0	0.4	100.0	1,065.1	4.4	-0.2	40.6
Meiji	583.1	3.5	0.0	-	2,076.2	12.4	0.9	110.9
Asahi	376.6	3.1	0.1	-	473.5	3.9	-0.7	26.5
Mitsui	197.5	1.9	-0.0	-	376.3	3.6	0.3	29.9
Yasuda	411.2	4.4	-0.0	-	578.5	6.2	-0.9	54.5
Chiyoda	160.1	2.7	0.9	50.0	164.9	2.8	0.9	18.4
Taiyo	162.6	2.4	0.0	-	740.4	11.0	-0.5	119.3
Toho	41.0	1.0	0.3	10.0	48.4	1.1	0.1	8.7
Kyoei	97.8	1.8	0.1	-	38.3	0.7	-0.4	8.1
Daido	212.0	4.1	-0.1	-	418.5	8.1	0.5	119.9
Nippon Dantai	84.3	2.1	0.1	-	125.4	3.2	0.3	24.8
Fukoku	111.6	2.7	0.0	-	257.0	6.1	-0.2	64.5
Daihyaku	88.5	2.8	0.7	19.0	52.1	1.6	-0.2	12.0
Tokyo	42.8	3.0	1.1	14.0	39.1	2.7	1.3	20.4
Total	5,383.9	2.9	0.2	343.0	14,660.9	8.0	0.3	70.8

Note: Main equity + funds (capital) + legal reserve + voluntary reserve (end of March) + contingency reserve (end of March) + price fluctuation reserve + reserve for general possible loan + losses + unallocated sums from reserve for policyholders' dividends (end of March) + tax effect equivalent sum of unallocated portion of reserve for policyholders' dividends and price fluctuation reserve.

Source: Based on materials supplied by individual companies.

## 6. Conclusion

So far, the second half of FY97 has seen a continuation of major bankruptcies among securities companies, banks and trading houses. The impact on the share prices of, and loans outstanding to, these companies is hurting the assets of life insurance companies, and the concomitant deterioration in the confidence of consumers and their increasing sense of anxiety are greatly exacerbating their problems.

We expect all the life insurance companies to continue bolstering their equity through attracting new capital and subordinate funds, as well as making efforts to cut risk exposure. That said, since all these companies are mutual companies, and therefore neither listed on the stock exchange nor used to timely disclosure of corporate information, the lack of reliable information may further erode the already shaky confidence of consumers."

From time to time life insurance companies issue statements like "the profitability of guarantee products is greater than that of savings products", "as policies closed in the bubble period mature negative spreads improve" and "operating costs are falling owing to cuts in the cost of sales", but in reality, it is totally impossible to ascertain to what extent there is a concrete impact on the health of the life insurance business. The industry may well turn out to be unable to stem the outflow of dissatisfied consumers unless it starts to make a determined effort to disclose pertinent and correct information, not merely negative factors such as the amount of nonperforming assets, but also positive factors as stated above.