Alliance between Toho Mutual Life Insurance Co. and GE Capital

The Creation of GE Capital - Edison Mutual Life Insurance

Takeshi Inoue

On April 1, 1998, the newly formed firm GE Capital - Edison Mutual Life Insurance started operation. This is a joint venture between Toho Mutual Life Insurance Co., a middle-tier Japanese life insurance company, and GE Capital of the U.S., the biggest non-bank firm in the world.

In recent years, Toho has fallen into a business slump, with a steady increase in the number of canceled contracts and poor performance in new sales. With this alliance with GE Capital, Toho will begin to deal with its current difficulties. On the other hand, GE Capital will enter into the Japanese insurance market, which is currently largest in the world and which is undergoing liberalization as a result of Japan's "Big Bang."

1. Alliance Scheme

On February 18, 1998 it was announced that GE Capital and Toho Mutual Life Insurance Co. entered into an alliance to establish a joint venture company and the operations of Toho Mutual Life Insurance Co. were transferred to the new company. On March 6th, an extraordinary representative general meeting[1] was held and it was decided to transfer the goodwill and delegate some aspects of operations to the new life insurance company. Subsequently, the new company, GE Capital - Edison Mutual Life Insurance Co. was granted a license to undertake life insurance operations on March 19th and commenced operations from April 1st.

The alliance scheme is as follows:

1) A new life insurance company[2] was established by financing from Toho and GE Capital.[3] The name of the new company is GE Capital - Edison Mutual Life Insurance Co. The

1 In the case of mutual life insurance companies, under the law, the policy holders (employees) have the right to participate in management. Important issues in terms of management are decided by a general meeting of employees. As normally, the number of such employees in a mutual company amount to a vast number, in place of an employees' general meeting, the articles of association permit the establishment of a representative meeting made up of representatives selected from the employees. (Article 42 of the Insurance Business Law)

2 In actuality, this new company will be formed by changing the objective of GE Super Abrasive Inc. a wholly owned insurance subsidiary of GE Financial Assurance Holdings.

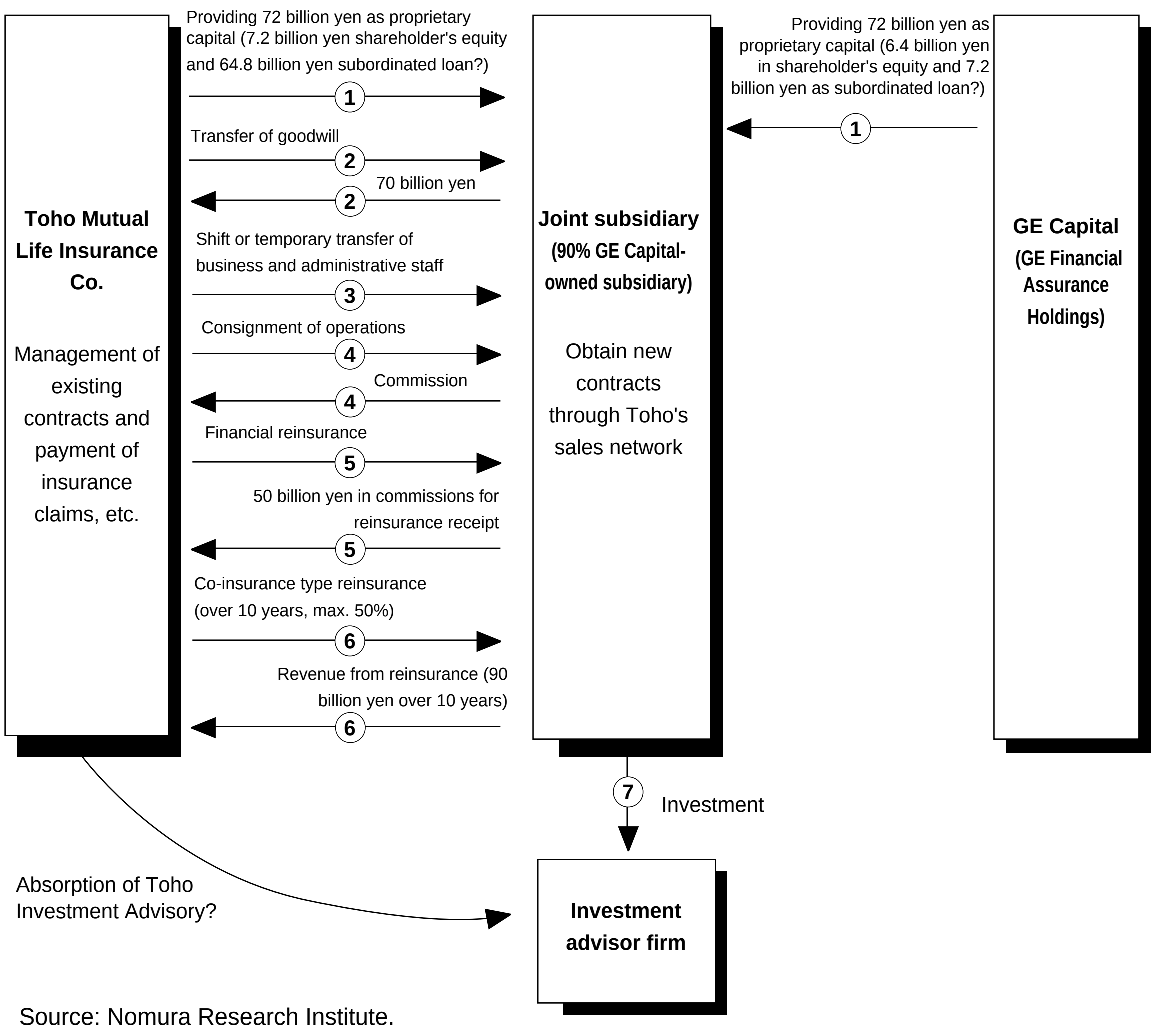
3 To be precise, this is GE Financial Assurance Holdings, a wholly owned insurance subsidiary of GE Capital.

company's proprietary capital totals 144 billion yen, of which 72 billion yen (36 billion yen in capital and 36 billion yen in legal reserves) are shareholders' equity and 72 billion yen is a subordinated loan. Although the amount invested by both companies is equal (72 billion yen each), capital with voting rights is apportioned 10% for Toho and 90% for GE Capital. In other word, as far as capital composition is concern, the new company is deemed to be a 90% owned subsidiary of GE Capital.

2) The new company has taken over Toho's sales network, operating assets, etc. as an enbloc goodwill (business rights) at a cost of up to 70 billion yen, and is carrying out new sales and the underwriting of life insurance products. On the other hand, Toho is no longer committed to new sales, i.e. it is devoting itself entirely to operations involving existing contracts and asset management. Regarding the transfer (sale and purchase) of the goodwill (business rights) worth 70 billion yen, there is a clause stipulating that in the case of the business plans for the period from fiscal 1999 to fiscal 2001 not being achieved, this sum shall be reduced by up to 20 billion yen. However, from that time onward (2001) to 2008, if the initial business plans are achieved, this 20 billion yen shall revert back to Toho in the form of revenues from joint insurance type reinsurance.

3) 7,000 of Toho's sales force have been transferred to the new company, and another 2,340 administration staff are either temporarily transferred or employed by the new company.

Figure 1. Tie-up scheme between Toho Mutual Life Insurance Co. and GE Capital



Source: Nomura Research Institute.

This leaves about 560 administrative staff with Toho. Mr. Ishizaka is the president of the new company. Previously he was the vice president of Toho. Mr. Michael Frazer, the president of GE Financial Assurance Holdings, also holds the position of chairman of the new company. Seven executives who undertake actual operations are from Toho (three of these also hold the position of directors). However in terms of commercial law, of the 12 directors, eight are from the GE side.

4) Field work such as procedures involving amendment and payment with Toho's existing contracts are entrusted to the new company. Regarding the formulation of statistical charts which are reported to the Ministry of Finance and the Life Insurance Association, and the formulation of basic data in the area of budgets and settlements, these are entrusted to the new company.

5) Toho will receive 50 billion yen in commissions (commissions for reinsurance receipt) from the new company. This will be accomplished by Toho's transfer to the new company of existing profitable products such as fixed-term insurance, as financial reinsurance. (Refer to the note inserted at the end of this report.) Regarding notifications, the qualification of an insurance company (In this case, GE Capital - Edison Life Insurance Company) which can accept financial reinsurance must be of AA or above rating from a designated rating company. GE Capital - Edison Life Insurance Company has been rated AA by S&P of the U.S.

6) Toho will underwrite a maximum of 50% of the new contracts obtained from the new company as co-insurance type reinsurance (refer to the note inserted at the end of this report) over a 10 year period, and will generate 90 billion yen in profits over the same period.

7) The new company will establish an investment advisory subsidiary. [4]

Table 1. Cash flow following Tied-up

Items	Toho Mutual Life Insurance Co.			GE Capital			New company		
	Investment	Earnings	Cash flow	Investment	Earnings	Cash flow	Capital subscription	Earnings	Cash flow
Providing proprietary capital	-720		-720	-720		-720	1,440		1,440
Transfer of goodwill (business rights)		700	700					-700	-700
Financial reinsurance (commission for reinsurance receipt)		500	500					-500	-500
Sub total	-720	1,200	480	-720		-720	1,440	-1,200	240
Co-insurance type reinsurance (future profits)		90 billion yen over 10 years	Same as on left					Minus 90 billion yen over 10 years	Same as on left
Operation entrustment commission		?	?					?	?
Investment return		Dividend receipt from proprietary capital and interest	Same as on left		Same as on left	Same as on left		Dividend receipt from proprietary capital and interest	Same as on left

Note: 10 years from now, earnings will have the value of 300 billion yen.
Source: Nomura Research Institute.

4 Regarding the operational assets held by Toho Investment Advisory, this is scheduled to be transferred to a new Investment Advisory firm.

2. Background of the tie-up and objectives

1) Toho's objective

Currently, many Japanese life insurance companies are facing management difficulties. This is mainly due to the current reversed-yield business environment, which was brought about by the massive sale of high yield (expected rate) guaranteed products during the bubble economy. Asset management has been on a downward trend since the early 1990s. Consequently, firms have been forced to take a profit from un-realized profits on their assets in order to maintain the expected rate. This, unfortunately, has resulted in a deterioration in the financial position of many companies, and some of them are having difficulty clearing off bad debt.

In addition to the above, such life insurance companies have experienced an increase in the cancellation of contracts and poor sales performance due to severe ratings of rating institutions and the poor evaluation of policy holders. This has led to difficulties in improving earnings through new sales.[5]

This can be said of Toho, too, with an increase in the cancellation of contracts and poor sales performance for the past several years, and it was anticipated that if this situation had continued to prevail, not only would the firm not have seen an improvement in revenues, but also it would have been compelled in engage in a full scale restructuring of operations including its sales structure. (See tables 2 and 3.)

Table 2. Proportion of repayment on cancellation and other repayment against total amount of assets at the end of the previous fiscal year

(Unit: %)

	FY 92	FY 93	FY 94	FY 95	FY 96
Nippon	2.9	2.9	3.0	3.5	5.9
Daiichi	2.7	2.8	2.9	3.4	6.3
Sumitomo	3.2	3.4	3.7	4.2	6.3
Meiji	3.4	3.2	3.2	3.8	7.0
Asahi	3.1	3.0	3.1	4.0	8.5
Mitsui	3.7	3.6	3.6	4.5	8.7
Yasuda	2.8	3.3	3.3	4.4	7.3
Chiyoda	4.8	4.2	4.7	5.7	13.4
Taiyo	3.6	3.2	2.9	3.6	4.0
Toho	15.4	12.0	9.5	9.3	13.3
Kyoei	3.4	3.5	3.3	5.0	7.3
Daido	4.3	3.8	4.0	4.9	9.2
Nippon Dantai	7.7	4.6	4.9	5.9	8.7
Fukoku	4.7	3.3	3.1	4.3	6.2
Daihyaku	4.4	4.6	4.0	5.8	10.7
Nissan	6.3	6.3	5.2	7.3	7.5
Tokyo	4.8	4.9	5.0	6.9	9.7
Total	3.9	3.6	3.6	4.3	7.3

Source: Based on data from each company.

5 As of April 19th, Toho Mutual Life Insurance's ratings were as follows: S&P - B, Moody's - Caa1.

Table 3 Growth Rate of Policies Held Over the Same Period in the Previous Term

(Unit: %)

	Private insurance			Private pension fund			Group insurance			Group pension fund		
	95.3	96.3	97.3	95.3	96.3	97.3	95.3	96.3	97.3	95.3	96.3	97.3
Nippon	2.7	1.9	1.2	8.0	15.1	-0.6	2.7	2.2	0.6	10.0	5.7	-4.5
Daiichi	3.5	2.1	1.6	5.2	10.5	-2.0	1.7	2.8	-0.7	10.8	6.2	-7.0
Sumitomo	2.8	2.1	1.1	5.5	7.9	-0.2	2.4	0.5	-5.6	8.5	1.9	-9.5
Meiji	5.7	1.9	0.5	3.6	8.4	0.1	3.1	3.0	-4.5	9.4	4.3	-8.7
Asahi	2.5	0.0	0.7	11.5	5.5	-0.2	4.4	3.8	2.4	10.3	3.5	-16.3
Mitsui	3.0	1.1	0.1	13.9	18.8	4.6	2.6	1.8	-3.3	10.8	5.3	-10.1
Yasuda	3.3	1.5	0.4	2.8	10.0	-1.5	5.1	5.6	5.1	10.6	3.9	-7.7
Chiyoda	5.6	1.3	-0.8	2.2	4.6	0.6	7.6	-1.2	-0.1	8.1	0.7	-21.9
Taiyo	0.0	1.2	3.2	5.4	9.2	4.2	3.4	6.2	1.1	9.6	4.0	-5.8
Toho	1.5	-0.3	-1.3	-3.9	0.4	-1.4	-0.4	0.2	-3.0	-3.1	-7.9	-27.3
Kyoei	6.0	5.3	2.3	3.9	10.3	10.3	3.5	-0.7	-1.1	11.9	-0.4	-18.1
Daido	2.7	3.3	3.5	-3.1	0.8	-0.9	4.0	2.9	-1.7	10.0	3.9	-8.7
Nippon Dantai	10.6	7.5	9.3	-2.3	-1.5	-2.9	2.1	1.3	0.0	0.8	0.5	-11.7
Fukoku	7.8	5.6	4.4	8.2	13.8	2.3	3.3	5.0	2.7	17.4	6.6	9.8
Daihyaku	9.6	6.6	2.5	-5.2	5.3	0.0	13.4	-7.1	-2.1	14.9	0.7	-24.2
Nissan	2.7	0.7	1.2	-3.4	-3.9	-5.4	2.8	-1.8	-1.2	6.3	-4.1	-7.1
Tokyo	2.0	2.4	1.7	-4.9	-2.1	-3.7	6.9	5.8	1.2	9.5	0.2	-12.4
Total	3.6	2.1	1.2	4.7	8.5	-0.2	3.3	2.3	-0.8	9.3	3.6	-9.6

Source: Nomura Research Institute. based on data from each company

Then, Toho took action and tied-up with GE Capital, which is recognized internationally as being a very reliable firm, in order to 1) increase new sales by making more effective use of existing management sources and 2) reduce the cancellation trend by the improvement of earnings. Toho expects to accomplish the following through this tie-up.

1) Disposition of bad debts

Toho Mutual Life Insurance Co. will be able to increase its earnings by 70 billion yen during this period by relinquishing its business rights. Toho is going to establish a reserve of at least 40.6 billion yen, and will dispose of over 80 billion yen in bad debts[6]. However, by transferring its operating assets, it will reduce future earnings because of the inability to generate profits by obtaining new contracts. Although an improvement in the redemption of bad debts is expected, it seems that it will be difficult for the firm's standing to be upgraded to "good," in comparison to other insurance companies, because Toho's reserve ratio has traditionally been low[7].

2) Building up a liability reserve

Toho intends to regain good financial health by obtaining 50 billion yen through financial

6 The details of the writing off of bad debts and the reserves during fiscal '97 were published at the extraordinary representative general meeting of March 6th. This included 2.6 billion yen owed by Crown Leasing , 1.5 billion yen owed by Yaohan Japan, 22.3 billion yen, owed by Tobishima Urban Development Group, 4.5 billion yen owed by Sanyo Securities Group, 6.5 billion yen owed by Toho Leasing and 2 billion yen owed by others.

7 As of the end of September 1997, the reserve ratio (NRI basis) stood at 20.7 %, which is the lowest level among the 16 major life insurance companies. Refer to Takeshi Inoue"Japan's Life Insurance Companies," *Capital Research Journal*, Spring 1998.

reinsurance contracts with the new company.

Financial reinsurance has the merit of generating future earnings in advance. A disadvantage is that these advance earnings that are created by the company's assumption of risk may be impacted (reduced) by the shifting of risk. In addition, according to the company, the five year Zillmer method[8] will be introduced once a 50 billion yen liability reserve is built up. However, this seems to be unfavorable compared to the companies which use the net premium method.

3) Earnings dividends from co-insurance-type reinsurance

According to Toho, they will receive total earnings of more than 90 billion yen over a 10-year period from reinsurance (co-insurance-type reinsurance) on new contracts which are to be obtained by new company. Moreover, they expect to be able to earn about 300 billion yen over a 10-year period from the underwriting of insurance contracts.

A reason that Toho is able to gain half of the new company's earnings is that a major part of Toho's financing in the new company is handled by means of a subordinated loan. Despite the fact that Toho holds only a 10% share of capital with voting rights, it is entitled to the same amount of earnings as GE.

4) Reduction of business cost

Toho is expecting a continuous earnings improvement by means of a substantial reduction in operating costs from such measures as the shift or temporary transfer of sales persons and administrative staff to the new company. The cost of Toho's company operations in FY 1996 was 84.2 billion yen, of which about half was sales related. Although Toho is to pay the new company a commission on services provided to Toho's existing policy holders, a substantial cost reduction is expected. As mentioned before, it is not denied that Toho was possibly in a position to make a full-scale restructuring of its sales sector sooner or later due a shortfall in the increase of contractors. However due to this tie-up, the sales structure has been transferred to the new company and is being effective used, and this will more or less ensure the continued employment of sales staff.

5) Investment in the new company

Toho is going to invest in the new company in the form of subordinated loan and shares, and an earnings from this investment are also anticipated.

6) Providing new products

According to Toho, policy holders will be provided highly qualified services and new products which are driven by GE's know-how and product development abilities through the new company. In concrete terms, the new company will pay more attention to products and services which have not yet been extensively provided in the Japanese market like "Healthy Body Insurance" which Toho started to sell last year, the first time in this industry.

8 The Zillmer Method is one of reserve methods of liability reserve which reserves more sales related cost from initial premium, and replenishes a shortage over years from premiums of the next period. On the other hand, a method which replenishes sufficient liability reserves from the beginning is called "Net Premium Method." The Zillmer method is called "5-year Zillmer," "10-year Zillmer," "maturity Zillmer" (same period as insurance period), etc. depending on how long it takes to cover a shortage.

2) GE's objectives

GE's objectives in this tie-up are (1) to diversify their services provided in Japan and (2) to capitalize on the investment opportunities presented by the deregulation of the insurance market due to Japan's financial "Big Bang." The reason for GE's choice of Toho as its business partner appears to be that GE thought it was the shortest route to success in this industry. Though the Japanese market has been saturated, and despite the fact that many foreign insurance companies which entered this market early on are experiencing difficulties in increasing market share, this move immediately gives GE a considerable market share[9].

GE Capital has become a large enterprise through M&As and capital investment[10]. Looking at just the past 3 years, GE has invested 118 billion dollars in M&A deals. These activities are not limited to the US: they are on a global scale, with a particular emphasis on Europe, where GE has acquired 76 companies during this period.

Since the formation in October 1994 of GE Capital Finance Corporation, a Japan entity, GE has steadily increased its M&A activities each year in this market. Currently, this company is engaged in the business fields of conditional sale, credit cards, consumer credit and car leasing, and is planning to establish a nation-wide business through the M&A of local credit sale and/or consumer credit companies. (See table 4.)

The business area which GE naturally is most expected to emphasize is life insurance. (Refer to table 7 towards the end of this report.) Among the life insurance company acquisitions of GE in 1996, The First Colony of Lynchberg Ltd. is well known for its fixed term life insurance business. GE's entry into the Japanese life insurance market seems to be based on this basic strategy of M&A.

Table 4. History of GE Capital's business development in Japan

Oct. 1994	GE Capital Finance (Japanese corporation) was established.
Nov. 1994	For 120 billion yen, obtained 350 staff, branch offices and credit card subsidiary through acquisition of installment sales load assets and goodwill of Minebea Credit Sales Corporation. Entered shopping credit business.
Apr. 1995	Obtained 250,000 members and 15,000 member shops through 10 billion yen acquisition of credit card and shopping credit operations of Shin-Kyoto Credit Sales Corporation.
Aug. 1996	Entered into car leasing business through 30 billion yen acquisition of 80% share in Marubeni Car System Corporation.
Dec. 1997	Entered into consumer credit business through acquisition of 100% share in Koe Credit Corporation of the Kofuku Bank group. Obtained 160,000 accounts and 51.7 billion yen in loan assets.
Mar. 1998	Established a new company in a tie-up with Toho Mutual Life Insurance Co. (GE holding 90%). At a cost of 70 billion yen, entered into insurance business through acquisition of Toho's sales assets and goodwill.

Notes: Other than the above, GE is engaged in the businesses of marine container and domestic container services as well as reinsurance.
Source: Based on data from each company

9 Toho has a firm client base in the medium-small company and governmental markets.

10 Refer to the Reference Section on the last page of this report for a profile of GE.

3. Evaluation of this tie-up

1) Earnings forecast for the new company

The new company, GE Capital - Edison Mutual Life Insurance Co. has taken over the operating assets of Toho Mutual Life Insurance Co. such as the sales staff. It is expected to take several years to generate a profit because of heavy operating costs and the fact that contracts are not expected to immediately increase.

Looking at life insurance subsidiaries of non-life insurance companies which have been established in previous years, they are expected to take about 8 years to generate their first annual profit and 10 years or more to clear the accumulated loss. Even in the case of Sony Insurance Co., which has shown increased performance in recent years, it took 11 years for them to generate a profit in a single fiscal year, and it still had an accumulated loss as recently as FY1996, 16 years after its founding. In the case of Prudential Insurance Co., a foreign insurance company, it took 5 years to make a profit and it still had an accumulated deficit in FY 1996, 9 years after its foundation. Toho has commented that the new company (GE Capital - Edison Mutual Life Insurance Co.) is expected to generate a surplus (loan repaid) within their first 4 to 5 years[11].

2) Toho's income from the new company

Through this tie-up, Toho is expecting earnings growth of 120 billion yen in this period. This enables Toho to write-off bad debts and streng then its policy reserve. However, it must be kept in mind that the increase of earnings in the current fiscal year brought about by assignment of goodwill and financial reinsurance is, to some extent, being achieved at the cost of future earnings which would have been obtained had goodwill been continuously retained. Toho's reversed yield cost was about 60 billion yen in the previous fiscal year. Therefore, it is difficult to increase profits dramatically unless their investment circumstances change favorably, even though there are some long term positive factors on earnings such as the decrease in operating costs resulting from the tie-up.

Regarding the 70 billion yen paid for the transfer of goodwill, as mentioned in the scheme section, if GE-Capital Edison Mutual Life Insurance Co., the new company, cannot achieve its operational plans in the period from FY 1999 to FY 2001, there is a clause which requires Toho to pay back 20 billion yen.

The majority of the board of directors is made up of people from the GE-Capital side. However, actual operations will be carried out by the Toho side people including the president and the executives. Thus, the mechanism put in place is such that the Toho side has to accept some responsibility for ensuring that the goodwill purchased by GE will actually generate sufficient value to offset the amount paid for it by GE-Capital. This is a factor representing a degree of instability in terms of Toho's future performance[12].

In this tie-up, income secured from co-reinsurance on new contracts obtained by the new company is deemed as being to Toho's merit. However, it is impossible to expect a substantial contribu-

11 Quoted from an article appearing on page 11 of the Asahi Shimbun dated Feb. 19.

12 As previously mentioned, if the new company is able to achieve its initial operational plans up to FY 2008, 20 billion yen will revert to Toho in the form of revenues from joint insurance type reinsurance.

tion at the beginning, as this profit increases in proportion to the number of new insurance contracts[13].

Moreover, whether the anticipated profits can actually be generated will depend on the new company's success. Also, the co-reinsured term is limited to 10 years, and the co-insuring rate that Toho will underwrite is also limited to 30-50 %.

As only very conservative profits are estimated, the level of capital investment in the new company will not be encouraging. Also, high returns from the subordinated loan are not likely, given that participation in profits is expected through co-reinsurance, although the detailed terms of that loan have not yet been clarified.

At the extraordinary representatives' general meeting held on March 6th, Toho announced its performance outlook. Over the next 10 years, earnings for the current term before tax are expected to be in the black. However, there are those who think Toho's forecast for insurance performance (cancellation of policies trend) and the assumption of interest rates, stock prices and the foreign exchange rate are all optimistic.

3) GE's burden

The scheme incorporating the joint subsidiary has been finally settled, and this does not directly affect either of the parent companies, despite the fact that GE initially was expected to extend equity capital to Toho in the form of funds and a subordinated loan[15]. Additionally, the funds that GE will bear the burden for via the new company (GE Capital -Edison) are not regarded as being in support of Toho itself.

Indeed, it is planned that funds will be injected into Toho in the form of (1) payment of a commission of 50 billion yen for underwriting of financial re-insurance and (2) transfer over a 10 year period of over 90 billion yen in profits from the issuance of co-reinsurance. However, some return will be expected through this structure, since (1) terms of the financial re-insurance seem to be arranged so that the underwriter of the re-insurance is ensured a profit and (2) the new company benefits from the co-reinsurance as well because it may spread the risks arising from the relative smallness of the newly founded insurance group. And it has been clearly declared in a press conference and press release that the new company will not take responsibility for existing insurance contracts held by Toho. As a result, GE is protected from a possible negative effect caused by high yield contracts and bad debts.

After all, it might be said that GE will obtain all things required in this industry, including the well trained sales staff of the 12th ranking Japanese insurance company[17], a sales network and the necessary know-how required to operate in the Japanese market. This is at the cost of indirectly injecting 35 billion yen for the acquisition of goodwill by the new company[16].

---

13 Toho also commented that it would take 10 years or more for this profit to reach its maximum level.

14 The long-term prime rate will rise by 0.1% every year. The Nikkei average will rise by 5% every year. The exchange rate will be stable at 125 yen to the dollar.

15 Quoted from *Nikkei Shimbun* on Feb. 4.

16 The investment amount is divided equally between Toho and GE Capital, and so this represents 35 billion yen, half of the amount of 70 billion yen.

17 Toho stood 12th in terms of asset size in Japan, 12th in amount of personal insurance contracts, 11th in amount of personal pension contracts, 12th in amount of group insurance contracts, and 12th in amount of group pension contracts at the end of September, 1997.

Moreover, if good performance is not forthcoming, an option exists through which the payment made for the acquisition of goodwill can be reduced.

4. Conclusion

Through this tie-up GE obtained all the infrastructure which is necessary to develop a life insurance business in Japan. On the other hand, it may be said that Toho obtained limited-period benefits such as an increase in profits for the current fiscal year and profits that will be earned through underwriting of co-reinsurance for the next 10 years[18].

For Toho, the profit forecast depends on the success of the new company GE Capital - Edison Mutual Life Insurance Co. since Toho is not going to sell any new contracts. Additionally, there is still the issue of Toho having to clear off bad debts within limited period.

Regarding this tie-up, some positive comments are given here: "Presidents of middle-tier insurance companies now have a new management alternative." (President Matsudo, Nippon Dantai Life Insurance)[19]; "There are many advantages because existing insurance contracts, staff, and relationships developed over a long period of time will be maintained; this is in comparison to Nissan Mutual Life Insurance which had no such alternative and went bankrupt last year."[20], "The negative image of the Toho brand will be improved by GE's credit insurance." (Mr. Matsumura, Japan Credit Rating Agency, Ltd.) [21]. On the other hand, there are some negative comments as follows. "Most insurance company actuaries suspect this tie-up will have a negative impact[22], "If the present pace of cancellation of insurance contracts continues, a shortfall in the policy reserve for insurance payments will occur, and the possibility of having to enter bankruptcy proceedings cannot be denied, in the worst case."[23], "The Toho restructuring plan might just be theoretical planning and it might fail."[24], "This tie-up is not acceptable for the reason that, once Toho goes bankrupt, it will not be able to avoid a situation in which utilization of an insurance benefit guarantee will be applied, the insurance sector will help GE."[25] (Comments from the insurance sector.) Thus, the success of this project is not at all a clear-cut issue.

However, due to the effect of the tie-up between Toho and GE Capital, there has been a rapid increase in reports of tie-ups between Japanese life insurance firms and foreign firms from the end of last fiscal year to this fiscal year (Table 5). The climate surrounding Japan's life insurance sector is adverse. However, with the advent of deregulation in line with Japan's Big Bang, there are many firms such as foreign firms and Japanese firms from other sectors which wish to enter the Japanese

18 Although it will be able to receive profits for over 10 years from reinsurance that has been underwritten before, this profit will be amortized as the original insurance policies mature.

19 Quoted from an article on page 4 of the Feb. 21 *Nikkei Shimbun.*

20 Quoted from an article on page 11 of the Feb. 19 *Asahi Shimbun.*

21 Quoted from an article on page 1 of the Feb. 19 *Nikkei Financial Daily*

22 Quoted from an article on page 4 of the Feb. 21 *Nihon Keizai Shimbun*.

23 Quoted from an article on page 7 of the Feb. 20 *Nihon Keizai Shimbun*.

24 Quoted from an article on page 10 of the Feb. 19 *Mainichi Shimbun.*

25 Quoted from an article on page 5 of the Feb. 19 *Nihon Keizai Shimbun*.

insurance market, one of the largest in the world. It is expected that tie-ups and acquisitions will continue to take place.

Table 5. Recent examples of tie-ups etc. between Japanese mutual life insurance companies and foreign financial institutions

Date of Report	Content
March 16th	A tie-up between Capital Group, a US investment trust and investment advisory company, and Dai-ichi Mutual Life Insurance in the area of product development and asset management in investment trust operations.
March 20th	"Nihon Investors Securities" was established (April 22nd.) with capital invesment by Jardine Fleming of the UK, and 11 Japanese companies such as Yasuda Mutual Life Insurance, Yasuda Fire & Marine Insurance and Fuji Bank. This new company specializes in the sale of investment trusts. Operations are scheduled to commence from June 1st.
March 20th	A tie-up between the Dresdner Bank of Germany and Meiji Mutual Life Insurance in the area of asset management in the Japanese market. It is intended to bring about a merger between subsidiaries of these two firms, namely Meisei Investment Trust and Dresdner RCN Investment Trust in the first half of 1998. They will then engage in joint investment trust operations.
March 31st.	Westdeutsche Landesbank of Germany provided a subordinated loan of about 10 billion yen to Daihyaku Mutual Life Insurance.A contract for financial reinsurance was entered into by RGA of the US, a reinsurance firm, and Daihyaku Mutual Life Insurance.
April 15th	A sales tie-up was formed by UNUM Corporation, a US nonlife insurance firm, Chiyoda Mutual Life Insurance and Dai-Ichi Kangyo Bank. The reinsurance of UNUM Japan Nonlife Insurance Co.'s policies by Chiyoda Mutual Life Insurance is under consideration.
April 16th.	American International Group, a US Insurance firm is considering the acquisition of Aoba Mutual Life Insurance.
April 18th.	Goldman Sachs, a US investment trust bank acquired the securitized head office building and land of Yamato Mutual Life Insurance.

Source: From various reports.

(Note 1)

Insurance companies usually prepare estimates on mortality rates for specific age groups, the expense ratio for costs incurred through insurance contracts and expected investment yield for received premiums in order to calculate premiums. Since these are only estimates, there is a possibility that real and expected results may vary. Therefore, this amounts to a risk to be borne by the insurance company. (For example, currently, there is a loss in yields with contracts signed in the bubble economy era, as expected returns were over-estimated.) However, as this rate is usually estimated conservatively, profits will normally be gained from insurance contracts (mortal profit, expense profit and yield profit).

In the case of finance reinsurance, the insurance company which originally obtained the insurance contracts (Underwriter:in this case, this is Toho), will transfer to another insurance company (Receiptor of reinsurance company: In this case, this is the new established company) all insurance risk accompanying the reinsurance contract as well as all future profits (mortal profit, expense profit and yield profit). On the other hand, the insurance company will receive in advance a lump sum payment for future profits resulting from the insurance contract (as an acceptance charge for the offered reinsurance). At this stage, the policy reserve for the offered insurance contracts will be transferred by cash payment to the receiptor of the reinsurance.

This was introduced in a revision of the Ministry of Finance’s directive dated December 25.

(Note 2)

Regarding this co-reinsurance, by underwriting a specific portion (30-50%) of the risk for new insurance contracts, Toho receives profit in line with this portion. Trading of the reinsurance acceptance charge and transfer of the policy reserve are not included in this co-reinsurance, which is different from financial reinsurance.

<Reference> Profile of GE Capital

GE Capital is a finance company owned by General Electric Company (GE) of the U.S. The parent company, GE, is one of the largest companies in the U.S., with earnings of $ 79.1 billion (5th largest in the U.S.), total assets of $ 272.4 billion (4th in the U.S.) and 239,000 employees (10th in the U.S.) (Refer to table 6). GE has 12 business lines, one of which, the financial business, is the domain of GE Capital.

Table 6. GE as seen in Fortune 500 Ranking

[Unit: $100 million/employees]

Sales			Total Assets			No. of Employees		
1	GENERAL MOTORS	1,683	1	FANNY MAE	3,510	1	WAL-MART STORES	675,000
2	FORD MOTOR	1,469	2	CHASE MANHATTAN	3,360	2	GENERAL MOTORS	647,000
3	EXXON	1,194	3	CITICORP	2,810	3	PEPSICO	486,000
4	WAL-MART STORES	1,061	4	GE	2,724	4	FORD MOTOR	371,702
5	GE	791	5	FORD MOTOR	2,628	5	UPS	336,000
6	IBM	759	6	BANK OF AMERICA	2,507	6	SEARS ROEBUCK	335,000
7	AT&T	745	7	GENERAL MOTORS	2,221	7	COLUMBIA HCA HEALTHCARE	285,000
8	MOBIL	722	8	J.P. MORGAN	2,220	8	KMART	275,000
9	CHRYSLER	613	9	PRUDENTIAL	2,190	9	IBM	268,648
10	PHILIP MORRIS	545	10	MERRILL LYNCH	2,130	10	GE	239,000

Source: Fortune.

The predecessor to GE Capital, GE Contract, was originally established in 1932 as a captive financial company to finance the purchase of GE electrical products. However, with repeated increases in business size through M&A and other developments, it now focuses on specialized insurance, consumer service, management of utilities and machinery, specialized finance and finance for the intermediate market. GE Capital currently has a total of 27 departments and is generating about 40% of the entire GE group’s profits. (The net profit of GE Capital in 1997 was $3.25 billion, while that of GE was $ 8.23 billion.)

Table 7. Summary of GE and GE Capital

	GE	GE Capital
Headquarters:	Fairfield, Connecticut U.S.A.	Stanford, Connecticut U.S.A.
Employees:	2,700,000	66,000
Net operating income:	$79.17 billion (FY1996)	$32.71 billion (FY1996)
Net profit:	$8.23 billion (FY1997)	$3.25 billion (FY1997)
Total assets:	$272.4 billion (FY1996)	$200.81 billion (FY1996)
Rating:		
S&P	AAA/A-1+	AAA/A-1+
Moody's	Aaa/p-1	Aaa/p-1

Source: Nomura Research Institute.