JAPAN RISES

Atsushi Gamo, chief representative, Japan representative office at Asia Capital Re, explains how Japan's non-life industry is emerging stronger from recent challenges

The past three years have been particularly challenging for Japan's non-life insurers. Since the financial year 2010 (1 April 2010 to 31 March 2011), the industry has had to contend with three annual underwriting losses in a row, caused by the 2011 Great East Japan Earthquake, the 2011 Thai floods and a string of mid-size natural disasters.

However, with annual premium growth of about 3% in 2011 and 2012, Japan looks set for a strong recovery for its non-life market, even though the country's non-life premiums in 2012 still fell short of the pre-crisis (2007) level of JPY11.03trn.

Atsushi Gamo

Leading the transformation in Japan is Abenomics, an ambitious new policy framework announced for Japan in December 2012. Abenomics has been widely credited with an immediate financial market impact, with the Nikkei equity price index rising sharply and the yen depreciating strongly.

The total effect of the package on real GDP growth for 2013 as a whole is expected to be in excess of one percentage point, the International Monetary Fund estimates. However, observers will be watching closely whether the effects of these policies will be sustainable.

The non-life insurance industry, of course, benefits directly from renewed economic growth, in particular through increased purchases of homes and durable goods. In addition, rising stock markets have bolstered balance sheets and solvency margins while the depreciation of the yen has boosted the contribution of foreign operations to profitability.

Nat-cat exposure

One key area being enhanced in the Japanese market is that of natural catastrophe exposures. This is especially so after Japanese insurers took a heavy toll from the Great East Japan Earthquake and the flooding in Thailand in 2011. Natural disasters also resulted in above-average significant claims payments in 2012.

Since then, non-life insurance companies have been drastically reducing their natural catastrophe exposure in domestic and international commercial risks, by increasing rates and deductibles and reducing sub-limits for earthquake and flood. However, Japanese insurers will need to carefully manage this amid an increasing confluence of supply and demand side factors.

Demand from corporate insureds, for example, is growing on the back of increased awareness of disaster risks affecting their business operations at home and abroad. The industry's response is also influenced by global property catastrophe reinsurance markets, which are notoriously volatile.

In response to the market's protracted stagnation and associated profitability pressures, the Japanese insurance industry has undergone a dramatic consolidation.

Today, three of the biggest insurance groups together account for about 85% of the market. The largest player, MS&AD Group, generates about one third of the total market premium volume, while NKSJ Group and Tokio Marine Group command market shares of approximately 26% each.

Such mergers enable insurers to benefit from economies of scale and scope, which should translate into lower combined ratios.

They also facilitate the strategic objective of growing premium income from overseas. For example, in the financial year 2012, Tokio Marine Group generated higher profits from its overseas operations than it did from its domestic non-life insurance business.

A more recent remarkable development is Sompo Japan's acquisition of Canopius, a top 10 Lloyd's insurer. For this Japanese insurance group, it represents the biggest foreign acquisition ever.

Japan's recovery story is not without its challenges. A consumption tax hike in April 2014, for example, is set to adversely affect insurers through higher loss and acquisition costs. ■

COMBINED RATIOS FOR NON-LIFE INSURANCE COMPANIES IN JAPAN 2004-2011 [FINANCIAL YEAR]

SOURCE: THE TOA REINSURANCE COMPANY