

AAJI-OLIS Life Insurance Seminar 2013

Life Insurance-Private Sector Roles in Social Security System Program

Demographic challenges and opportunities for Japanese life insurers

Jakarta, Indonesia

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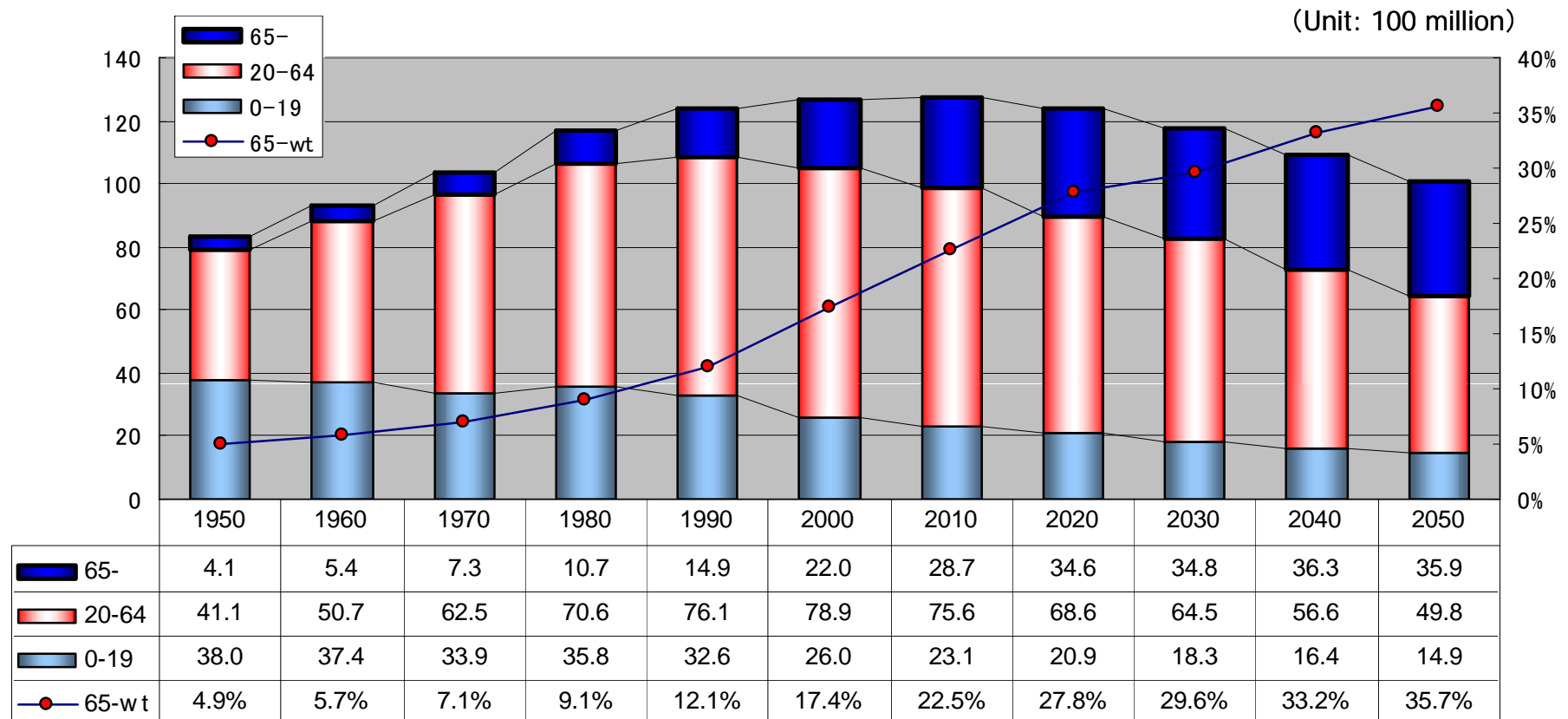
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Japanese population demographics

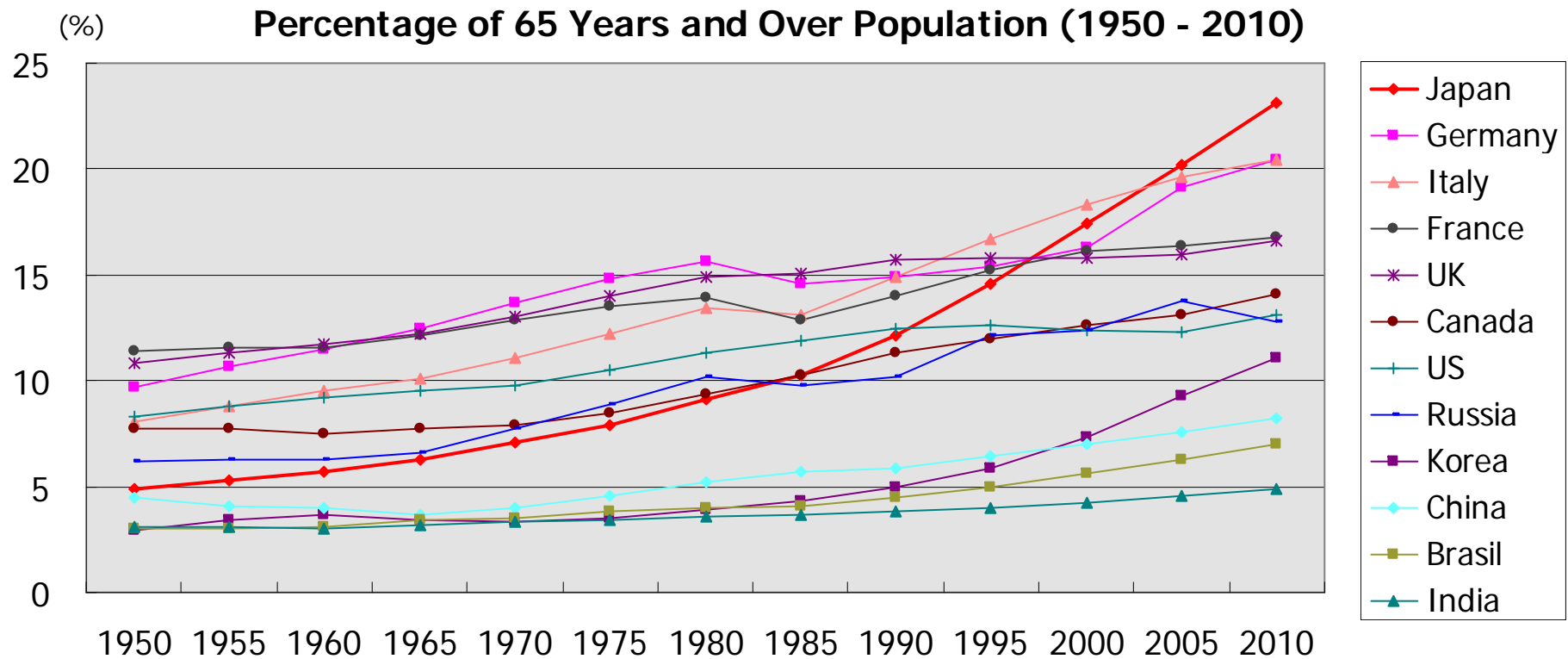
- Japanese population: 127 million 760 thousand as of 1 October, 2005, a drop of 0.02% from the previous year and decreasing since then
- Aged 65 and older reached 25.6 million, which exceeded for the first time 20% of total population and increasing since then



(Source: National Institute of Population and Social Security Research "Japan's projected population")

Rapid aging

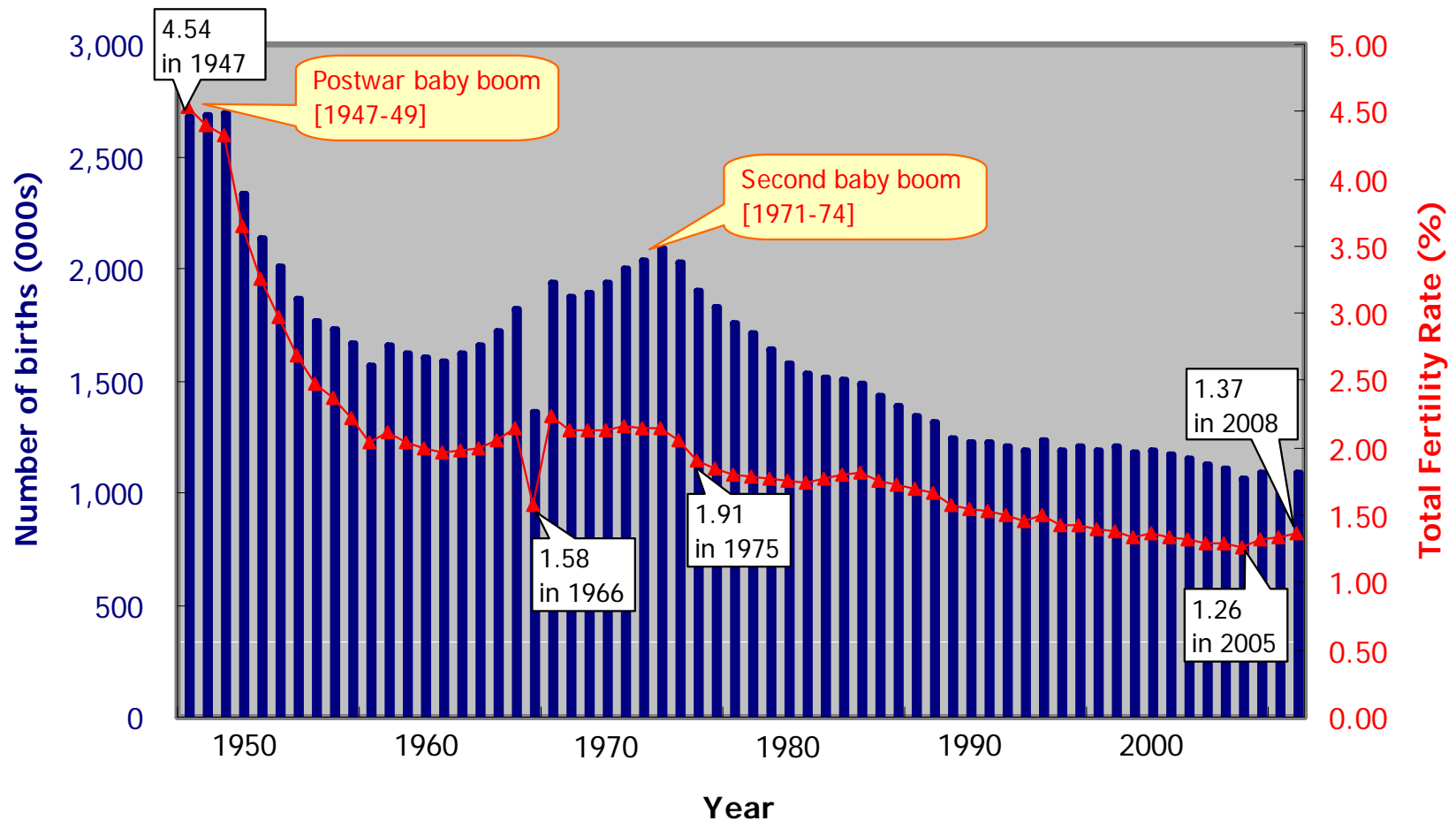
- Japan was in the lower-rankings until the 1980s, in the middle in the 1990s, and is already the highest in the early 21st century



(Source: Statistic Bureau, Data is based on United Nations, "World Population Prospects," The 2010 Revision
Note: Data for Japan is based on "Population Census of Japan")

Lower fertility rate - Trends in number of births

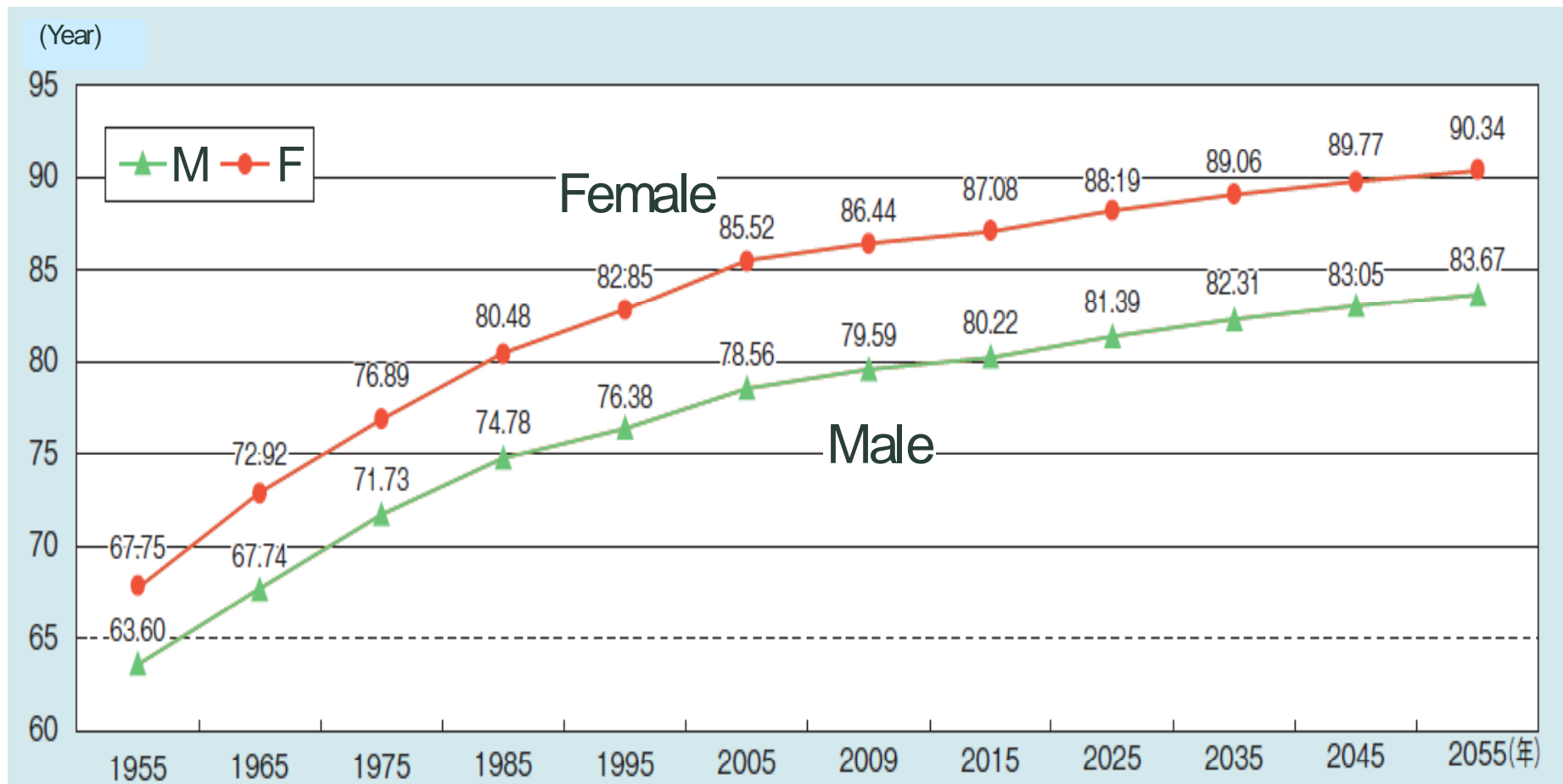
- Total fertility rate has dropped from 4.54 in 1947, to 1.91 in 1975, and to 1.26 in 2005



(Source: Ministry of Health, Labor and Welfare, Vital Statistics)

Longer lifespan

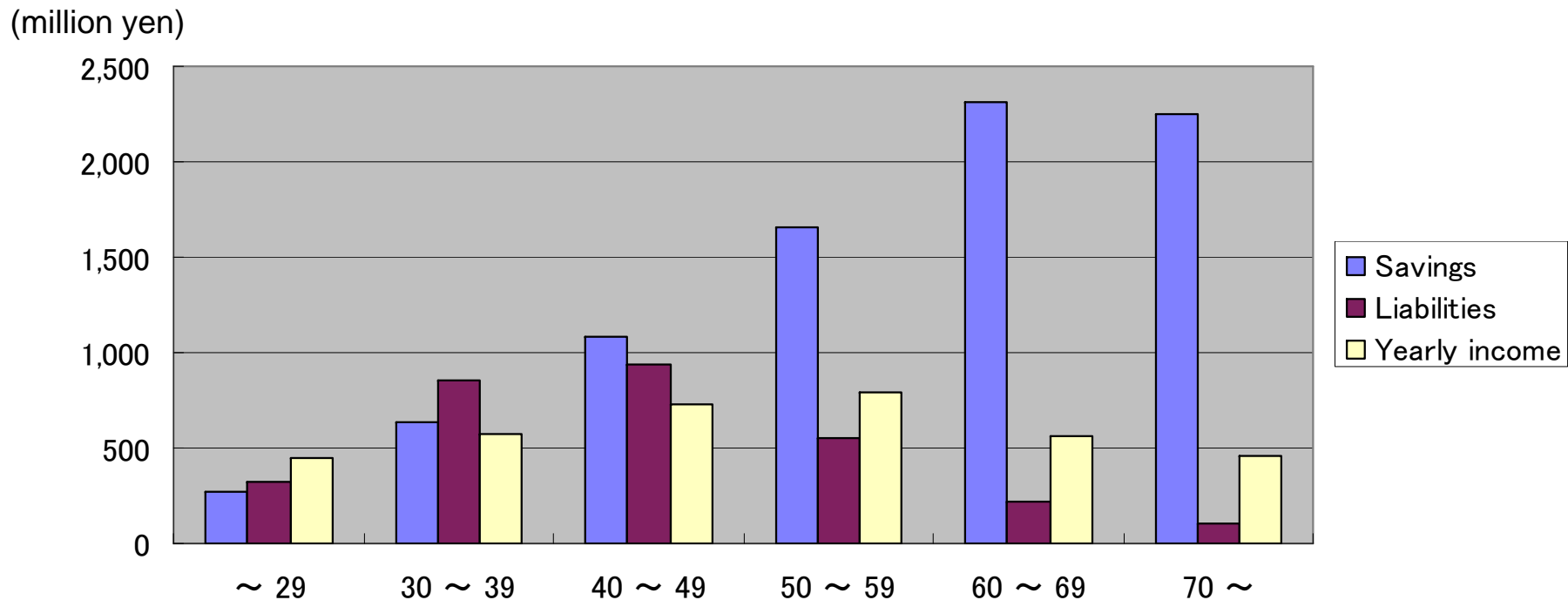
- Japanese life expectancy is among the highest in the world.
- Many Japanese women live alone for around 10 years after their husbands pass away.



Source: Ministry of Health, Labour and Welfare and National Institute of Population and Social Security Research ; courtesy of Swiss Re Japan.

Savings higher as age increases

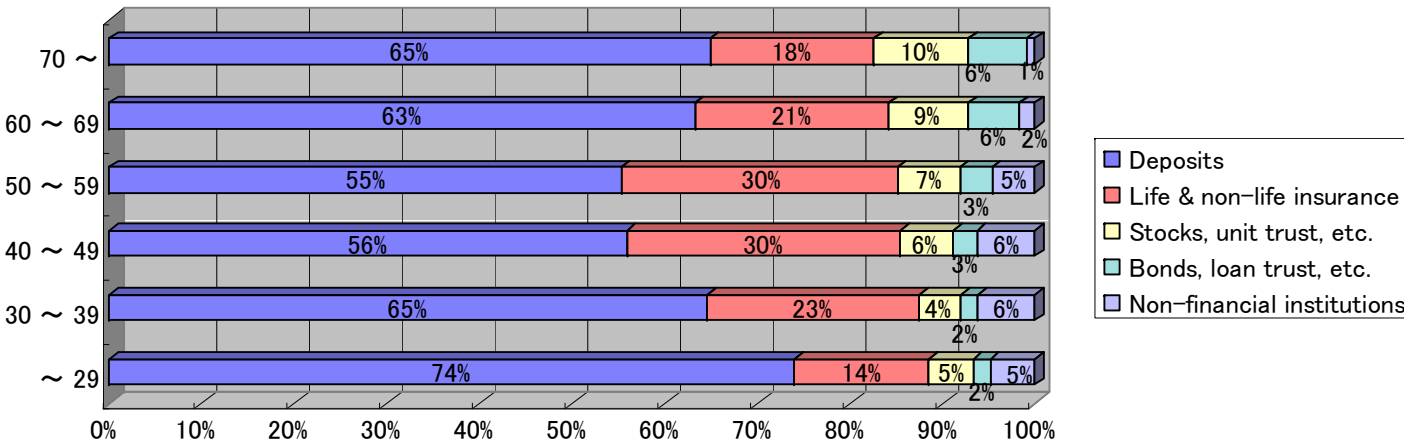
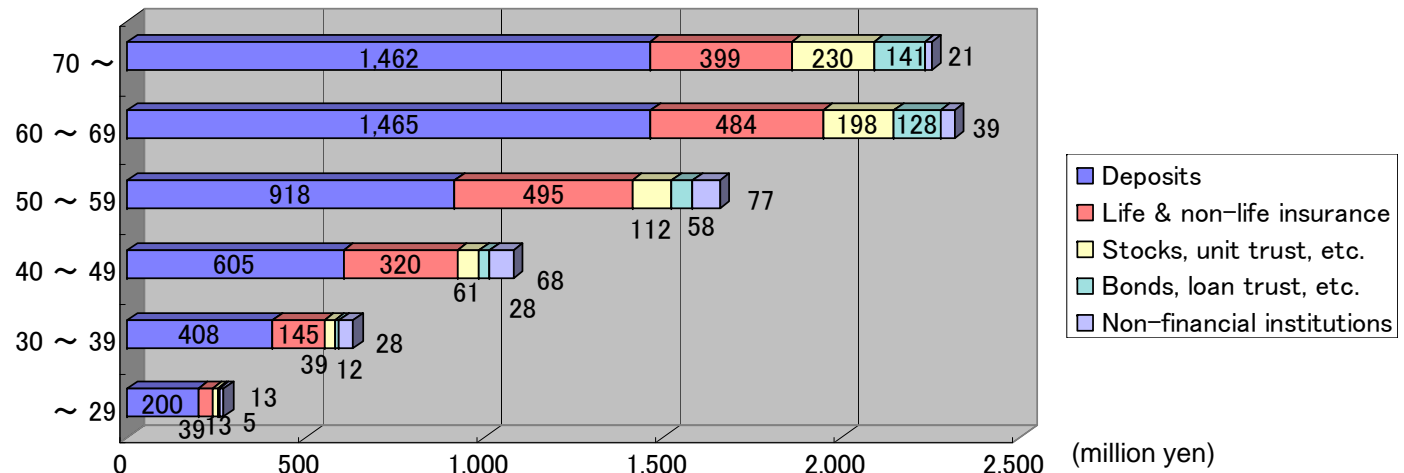
- Savings per household by age in 2010
 - ▣ Savings are 2.7 million yen for a householder under age 30
 - ▣ 8.5 times larger at 23.14 million yen for a householder age 60 or older
 - ▣ Liabilities to be higher as age increases up to the ages 40 to 49, at which age they peak and begin to decrease



(Source: Annual report on the family income and expenditure survey. Income and expenditure, Statistics Bureau, Ministry of Internal Affairs and communications 2010)

Financial profile of elderly

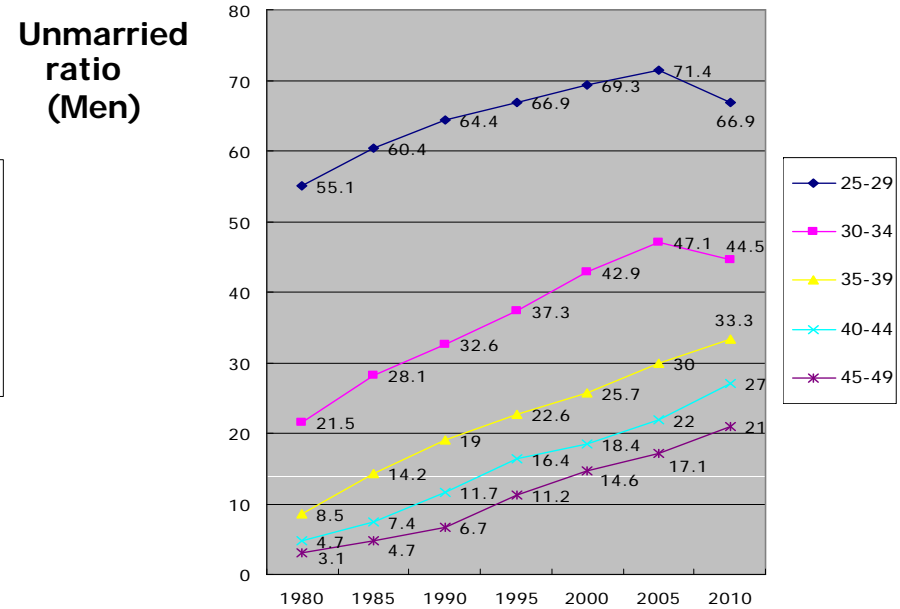
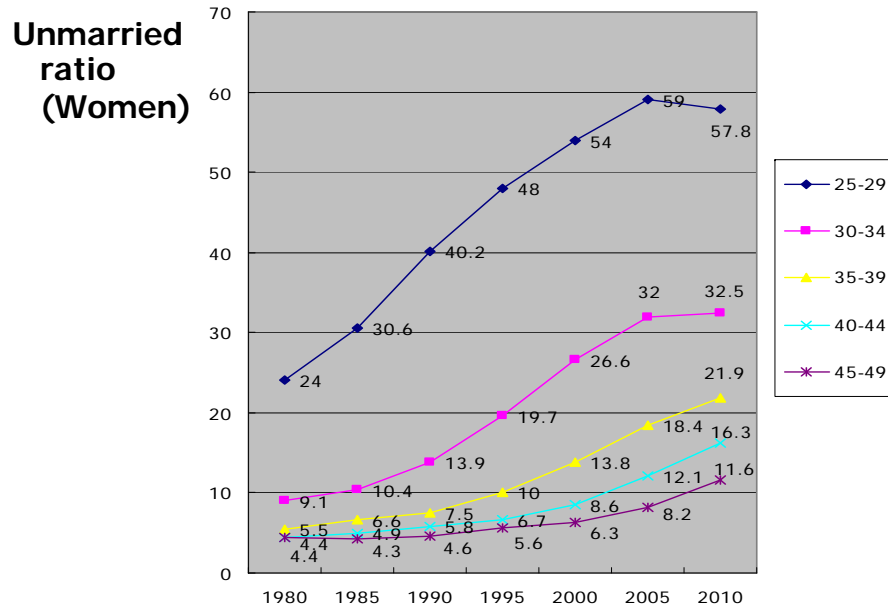
- As people get older, the portion of assets with risk increases.
- Younger generation prefer bank deposits. Those over age 50 tend to invest more in securities and less in insurance than those below age 40



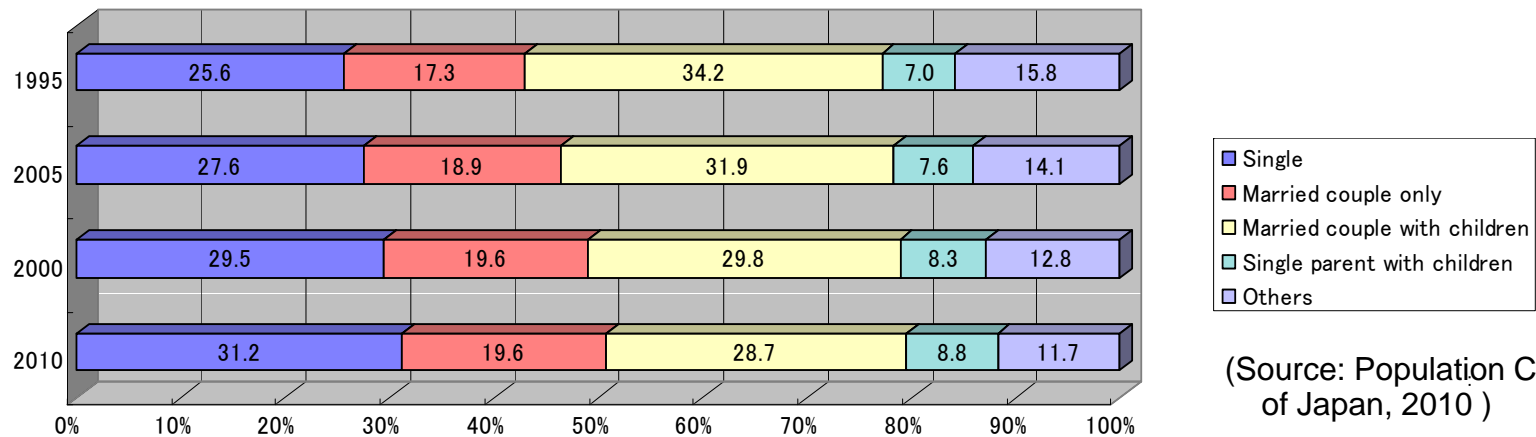
(Source: Annual report on the family income and expenditure survey. Income and expenditure, Statistics Bureau, Ministry of Internal Affairs and communications 2010)

Life style change

■ People tend to be unmarried or married late



■ Among the married, those without children are increasing

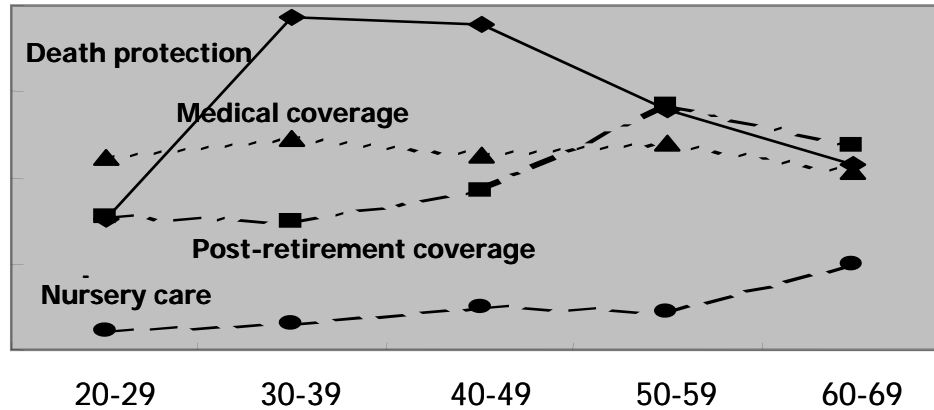


(Source: Population Census of Japan, 2010)

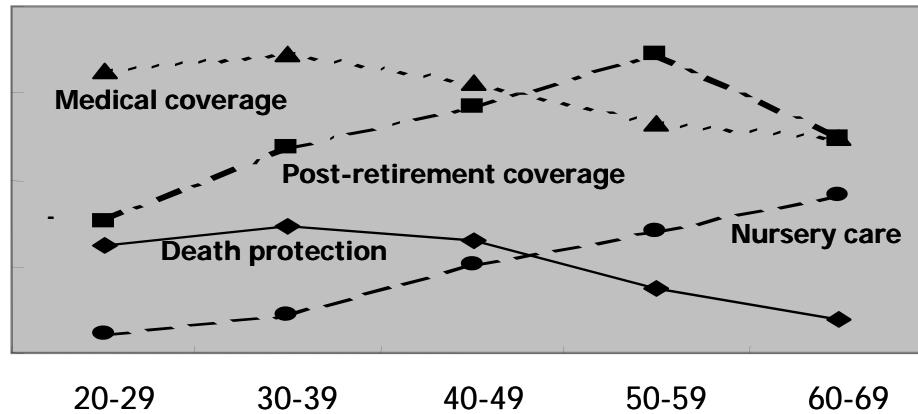
Changing life insurance needs

- In recent years, the baby boomers became aged over 50 with independent children, and needs are shifting from death protection to medical and post-retirement coverage

[Men]



[Women]



(Source: Japan Institute of Life Insurance "Survey on coverage")

1 Demographic and social changes



2 Market environment -Low interest rates and share prices

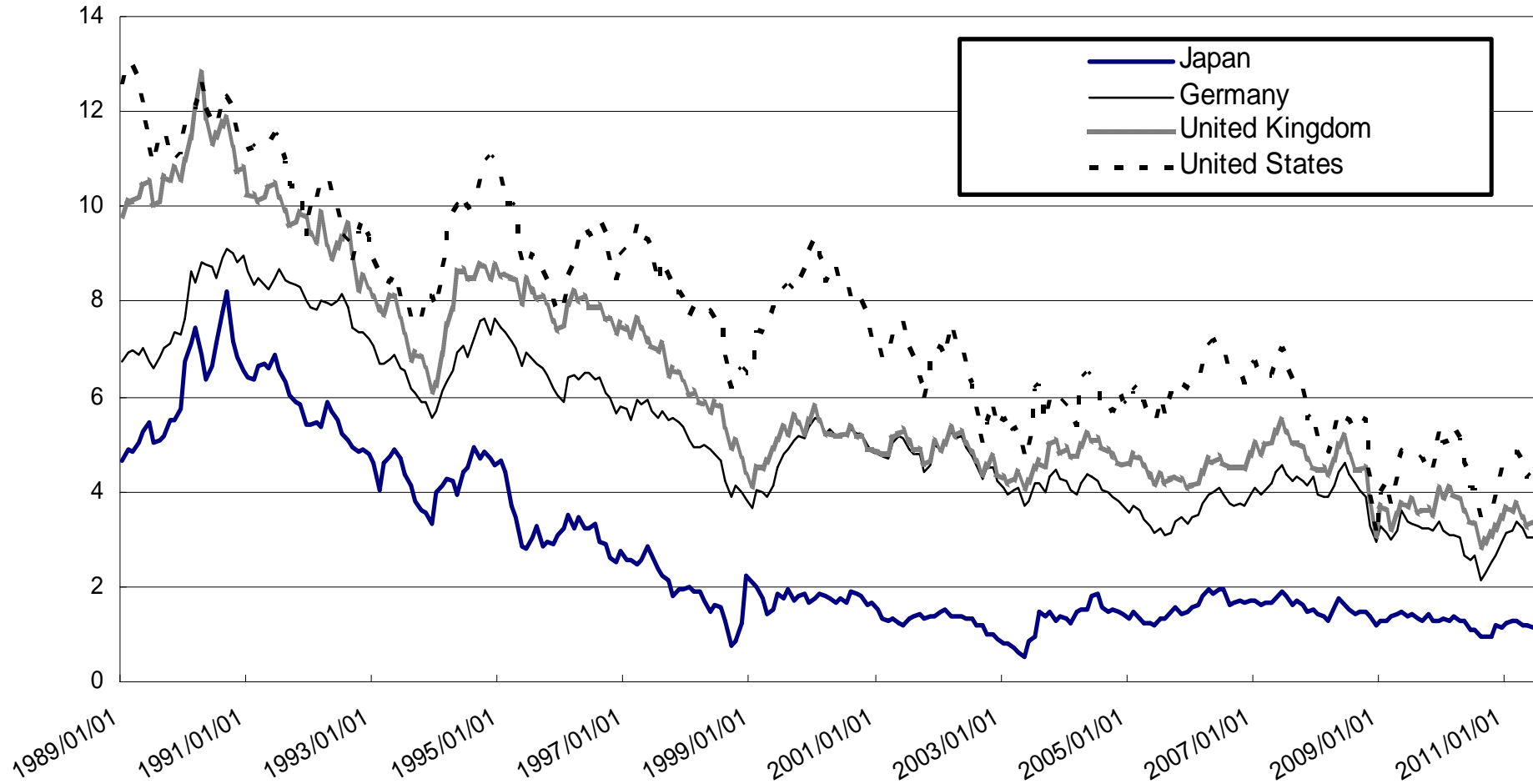
3 Aging and longevity – implications for social security and life insurers

4 Tao of supervision and risk management – Yin and Yang

Japan experienced a low interest rate environment

- Low interest rates becoming a worldwide trend

Government / Treasury Bonds (10 year) Interest Rate



Stock market has been also disappointing

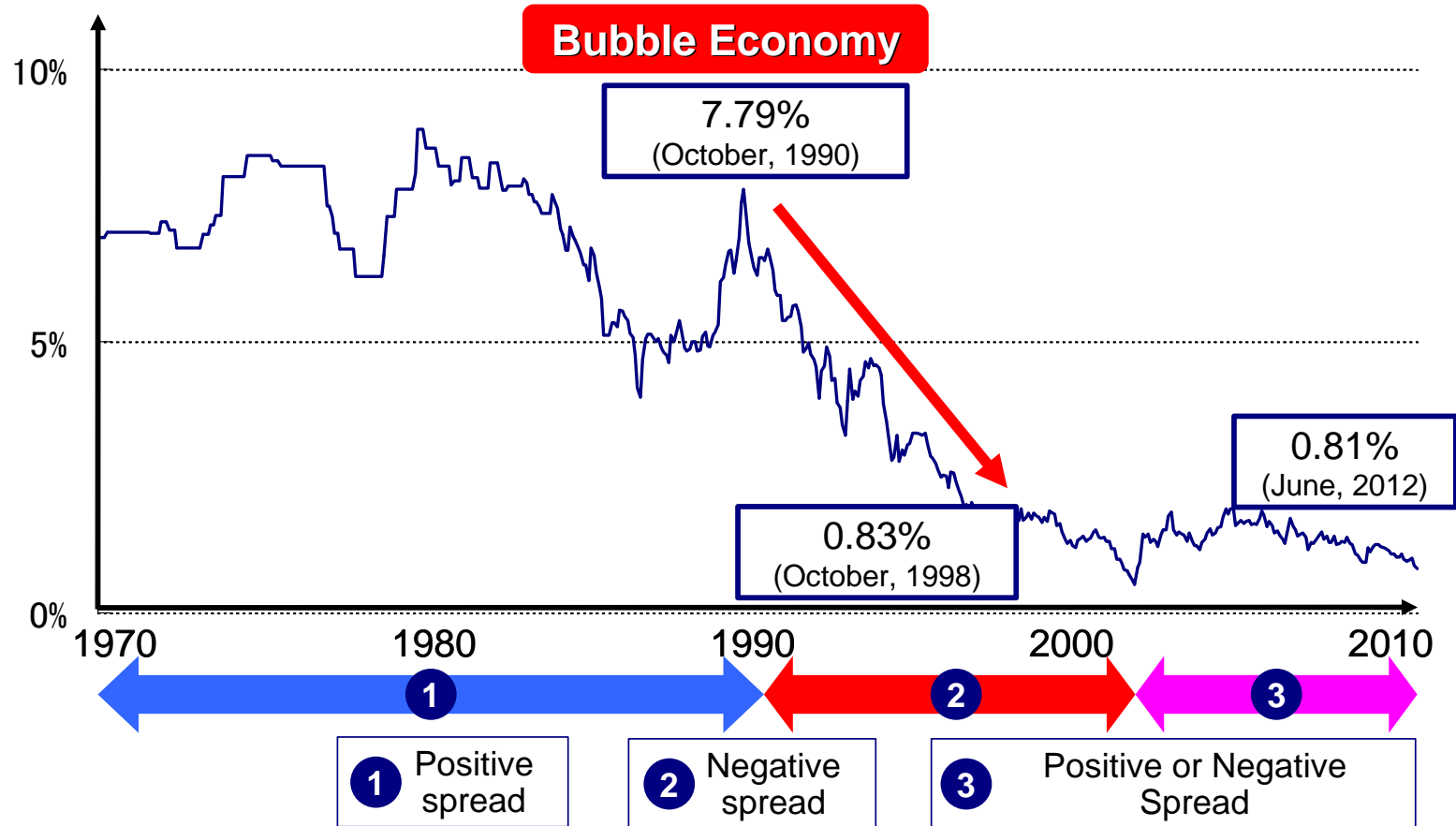
- Low interest rate coincided with poorly-performing stock prices



Negative spread problems in 1990s

■ After the collapse of the bubble economy, Japan experienced a long-lasting, severe investment environment with low interest rates and poor performing stock prices. This, combined with a market dominated by long-term insurance products with high guaranteed returns, led to negative spread problems in the mid 1990s, although most Japanese life insurers endured the severe business environment.

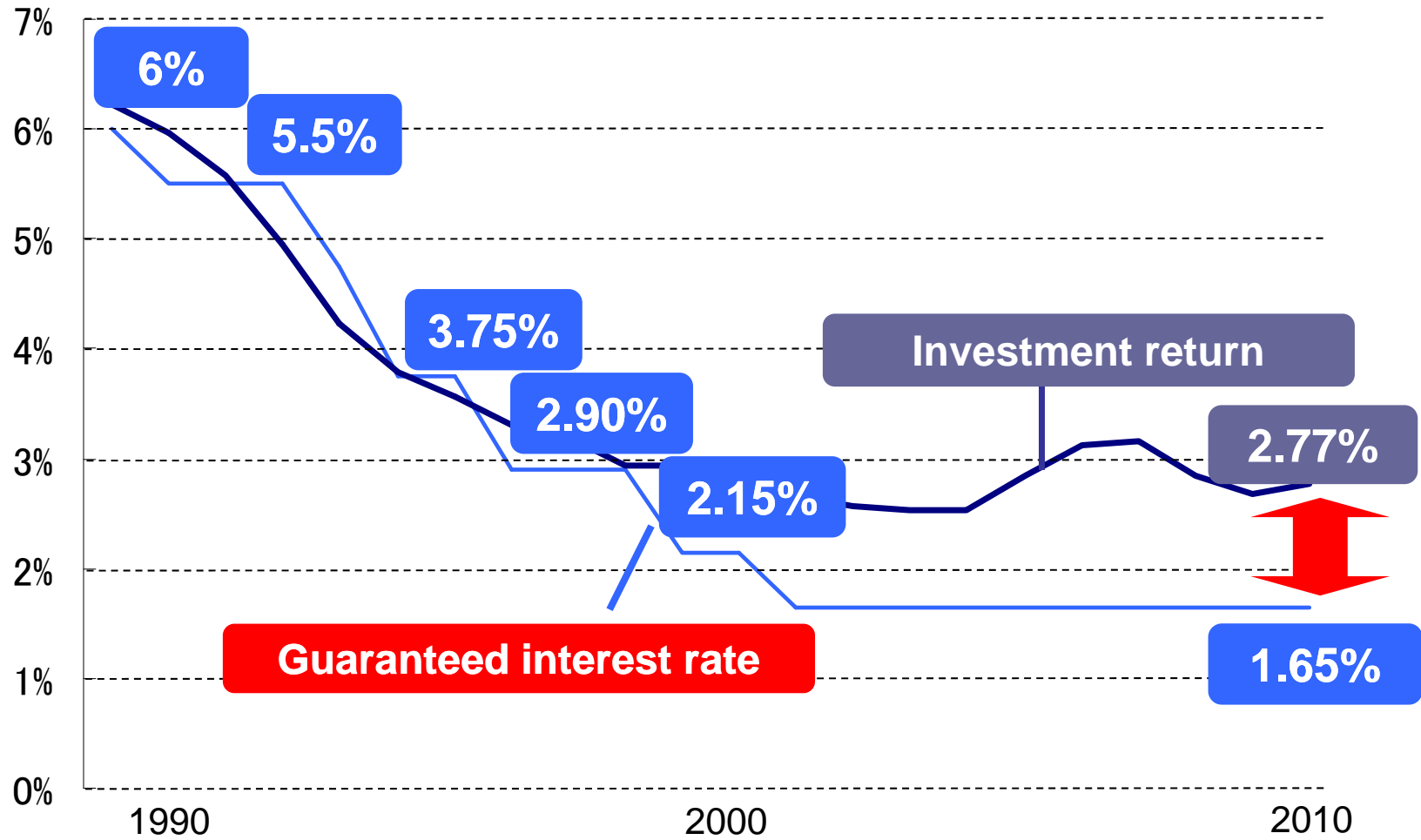
10-year Interest Rate in Japan



Lowering guaranteed interest rate

■ Reducing the guaranteed interest rate gradually for new policies

Lowered guaranteed interest rate

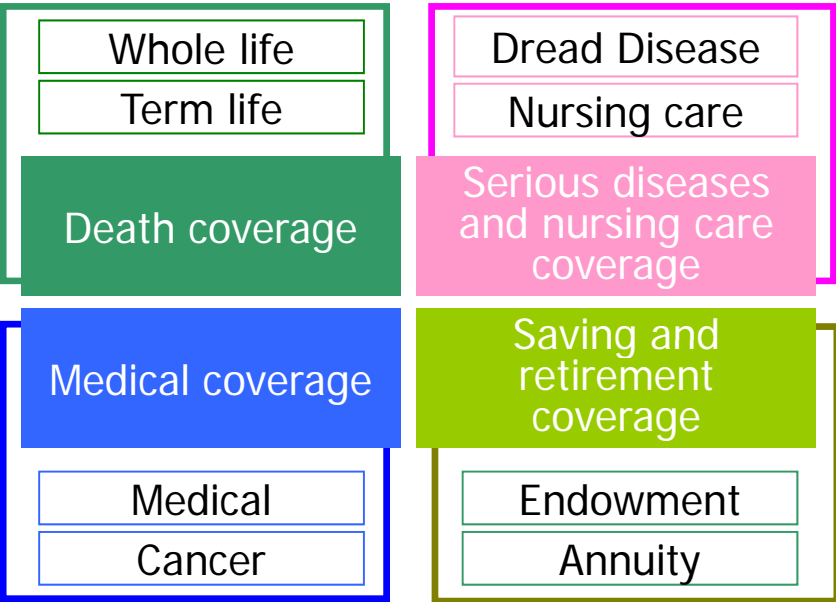


Providing protection-oriented products

- Developing a wide range of products
- Securing stable mortality profit
- Adding non-monetary values for customers

Protection-oriented products

Customers can select insurance products from a well-balanced product portfolio

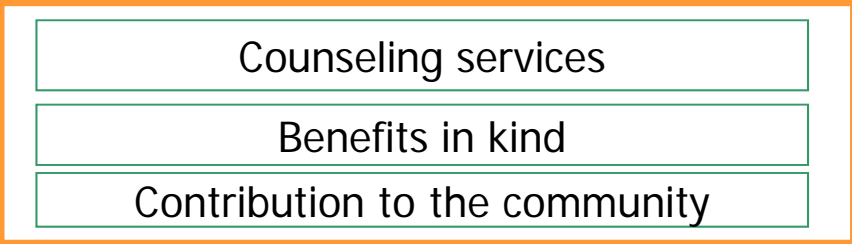


Stable mortality profit

(Billions of Yen)

	2005	2010
Mortality profit	540	437.4
Undistributed earnings	236.8	231.2

Value added for customers





Demographic and social changes



Market environment -Low interest rates and share prices



Aging and longevity – implications for social security and life insurers



Tao of supervision and risk management – Yin and Yang

Issues for discussions: social security and pensions

- The following issues may arise under these circumstances

- **What are the roles of life insurers in social security?**

Life insurers vs. Public Pensions/Healthcare

- **How to report pension and insurance liabilities?**

IFRS: Fair value accounting for pension/insurance liabilities

- **How to secure retirement income? Who are taking risks?**

Defined benefit plans vs. Defined contributions plans

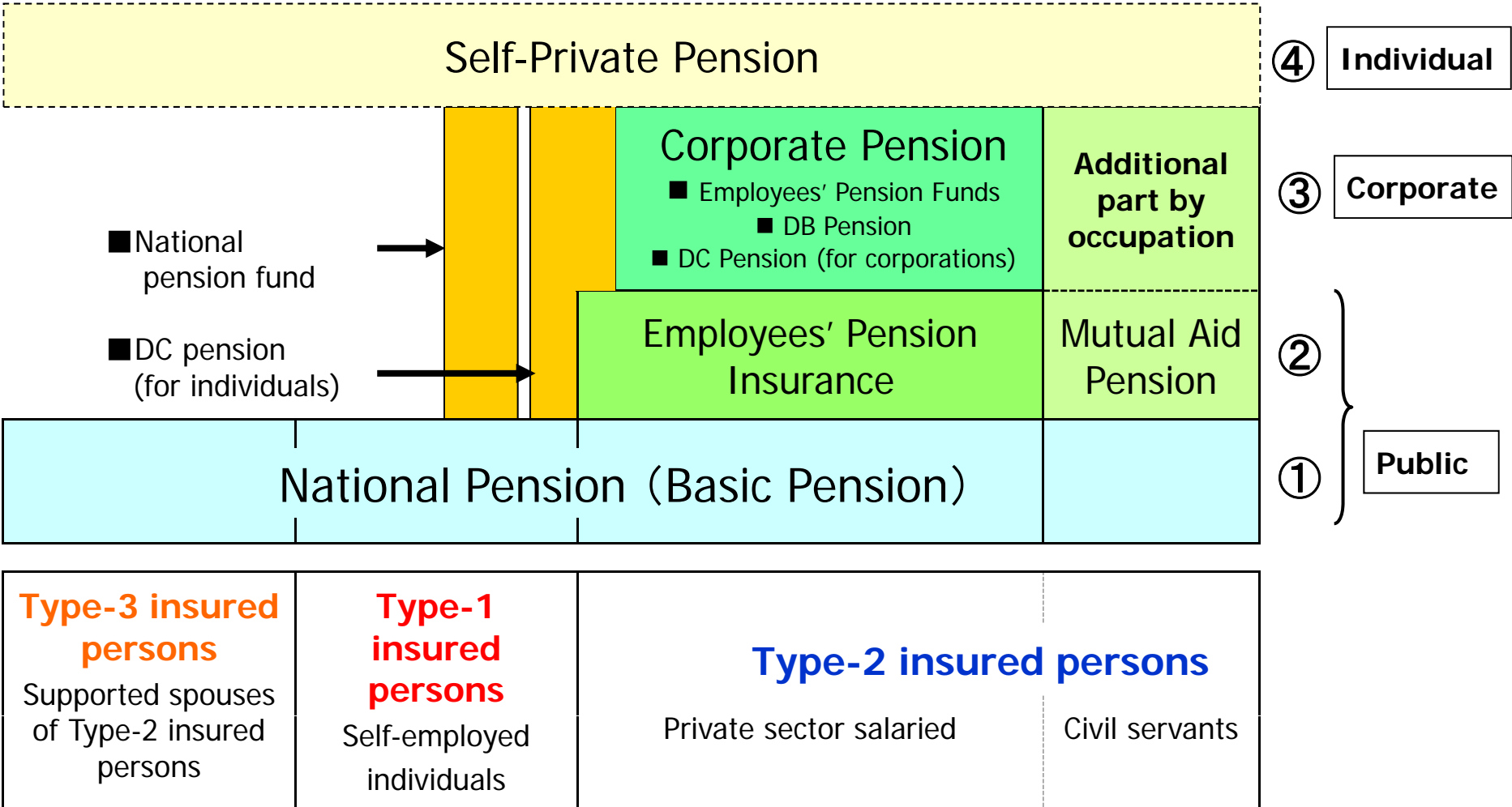
Long-term protection products vs. Investment products

- **How to deal with longevity risk?**

Joint Forum is now looking at this issue

Structure of the pension system in Japan

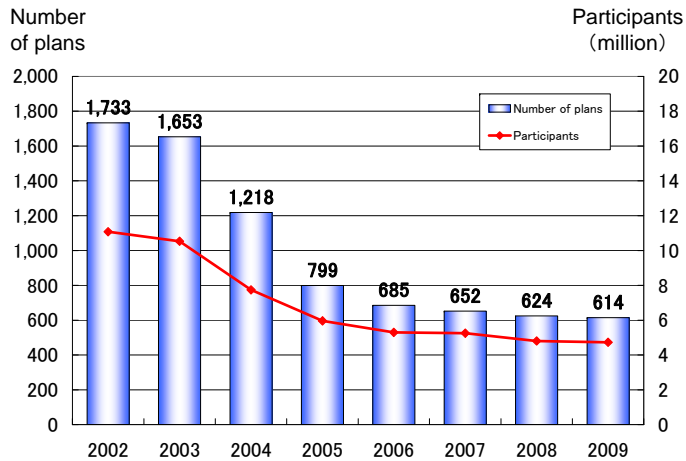
- The Japanese pension system is made up of 4 tiers including “private pension”
- The public pension provides a national minimum protection for all individuals and private pension provides additional protection tailored to the needs of each individual.



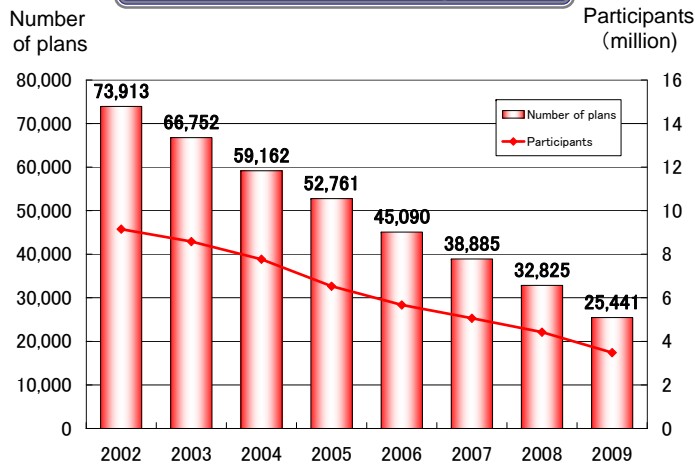
Trends for corporate pensions market

- Corporate pension system was restructured in the context of increased unfunded plans after the collapse of bubble economy and the introduction of post-employment accounting

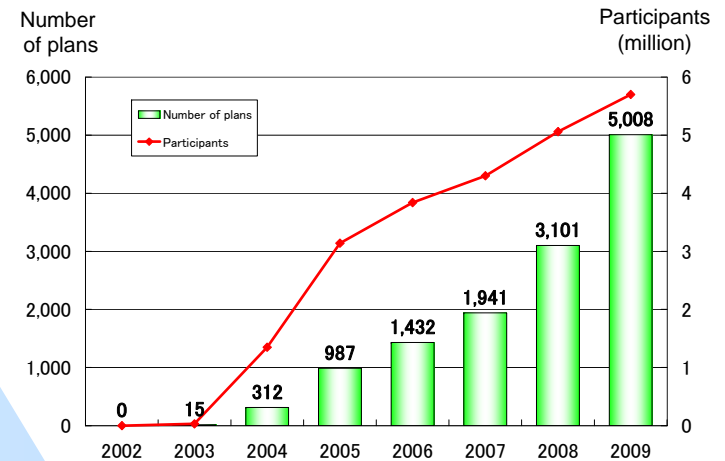
① Employees' pension funds



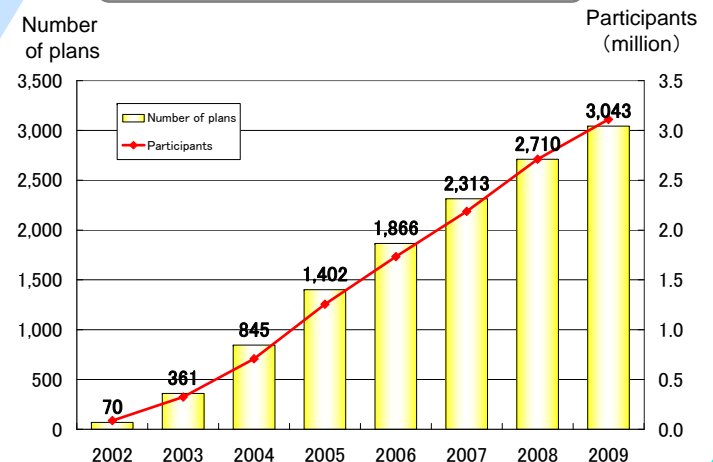
② Qualified retirement pensions



③ Defined benefit corporate pensions



④ Defined contribution pensions



□ Employees' pension funds

- "Daiko Henjo" started in 2002 (※the cessation of employee retirement benefit payments on behalf of the government)

□ Qualified retirement pensions to be discontinued in 2012

□ Defined benefit corporate pensions started in 2002

□ Defined contribution pensions started in 2001

The pension system in Japan and longevity risk

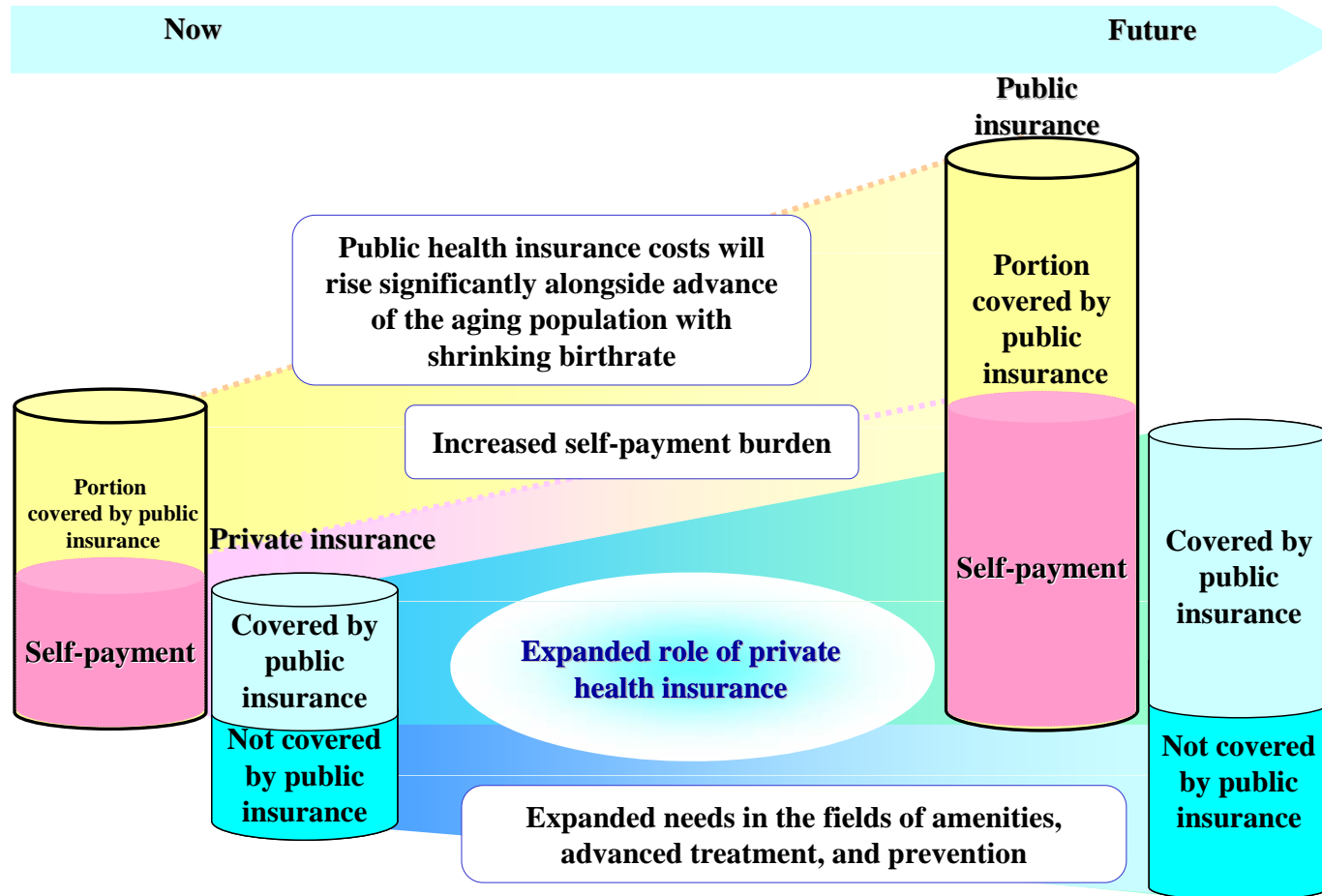
- The public pension provides a whole life annuity and the corporate pension provides a supplement in the form of a lump sum retirement payment or fixed-term annuity

Pension system	Typical form of payment	Other features
① National Pension	whole life annuity	-
② Employees' Pension Insurance	whole life annuity	survivor's pension
③ Corporate Pension	lump-sum retirement allowance or fixed-term annuity	some companies provide whole life annuities with a guaranteed term
④ Self-Private Pension	fixed-term annuity	options for whole life annuity with guaranteed term and lump-sum are available

- Longevity risk is mainly borne by government and individuals.
- Life insurers are subject to longevity risk, in case where the option for whole life annuity is chosen by policyholders for self-private pension.

Evolving roles of public and private health insurance

- Separate roles of public and private health insurance are evolving to respond to the aging population

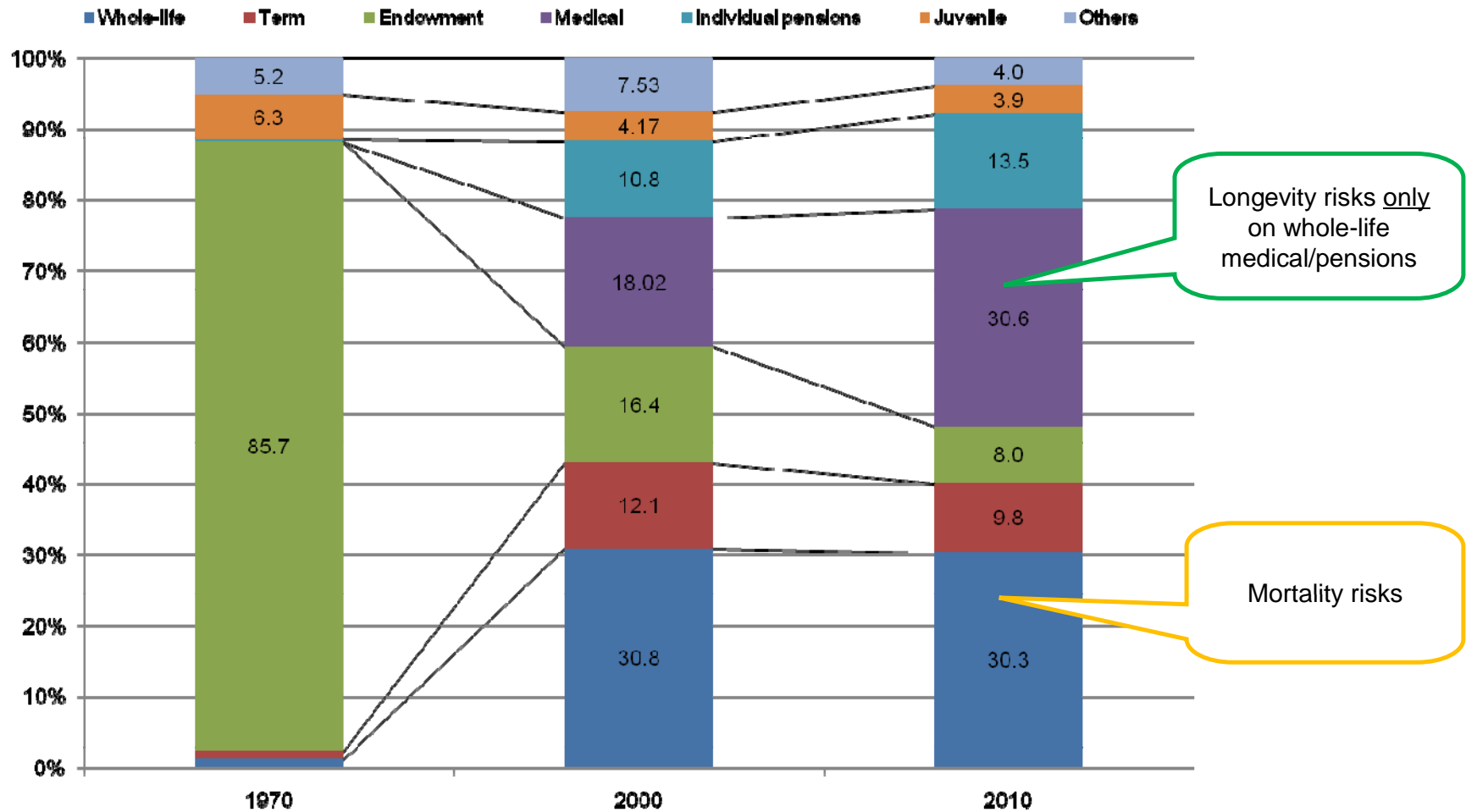


- Life insurers are subject to longevity risk, in case where the option for whole life medical insurance is chosen by policyholders.

Offsetting between longevity risk and mortality risk

- Japanese life insurers' exposure to longevity risk is limited but gradually increasing

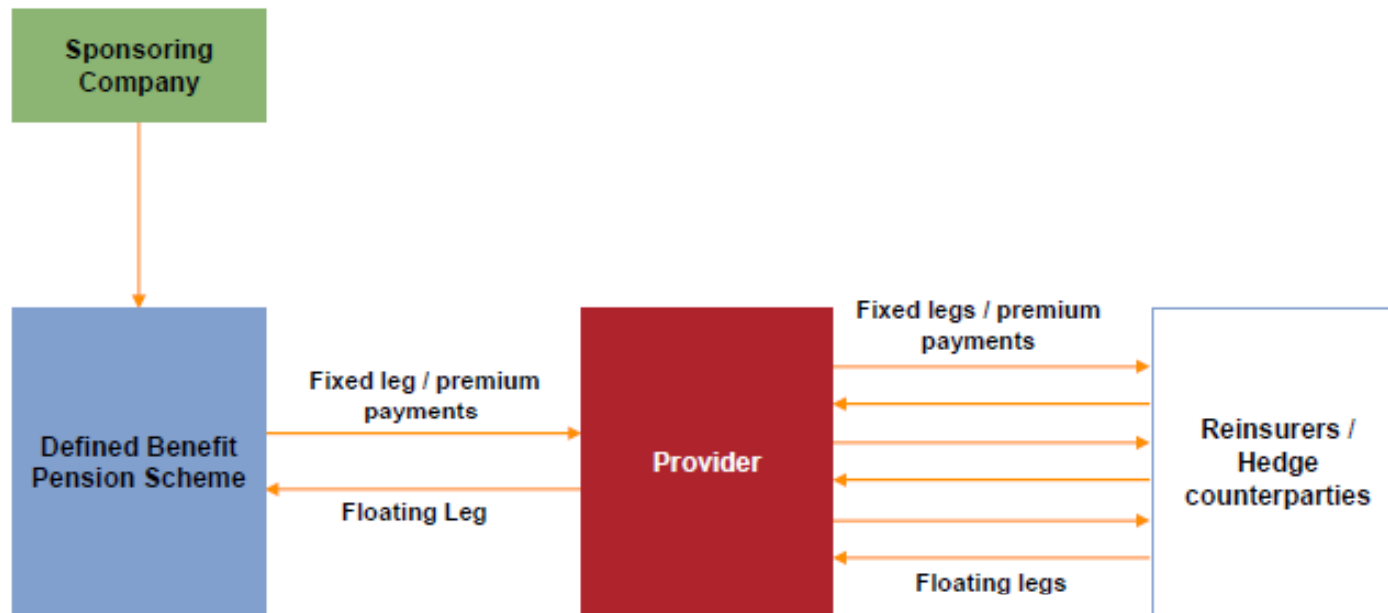
Changes in Product Portfolio (Number of Policies in Force)



Other measures to mitigate longevity risk

- Longevity Risk Transfer
 - Buy-out & Buy-in
 - Longevity Swaps
- Longevity as asset class for investors?

Longevity Hedge Transaction Structure



(Source: Deutsche Bank AG)

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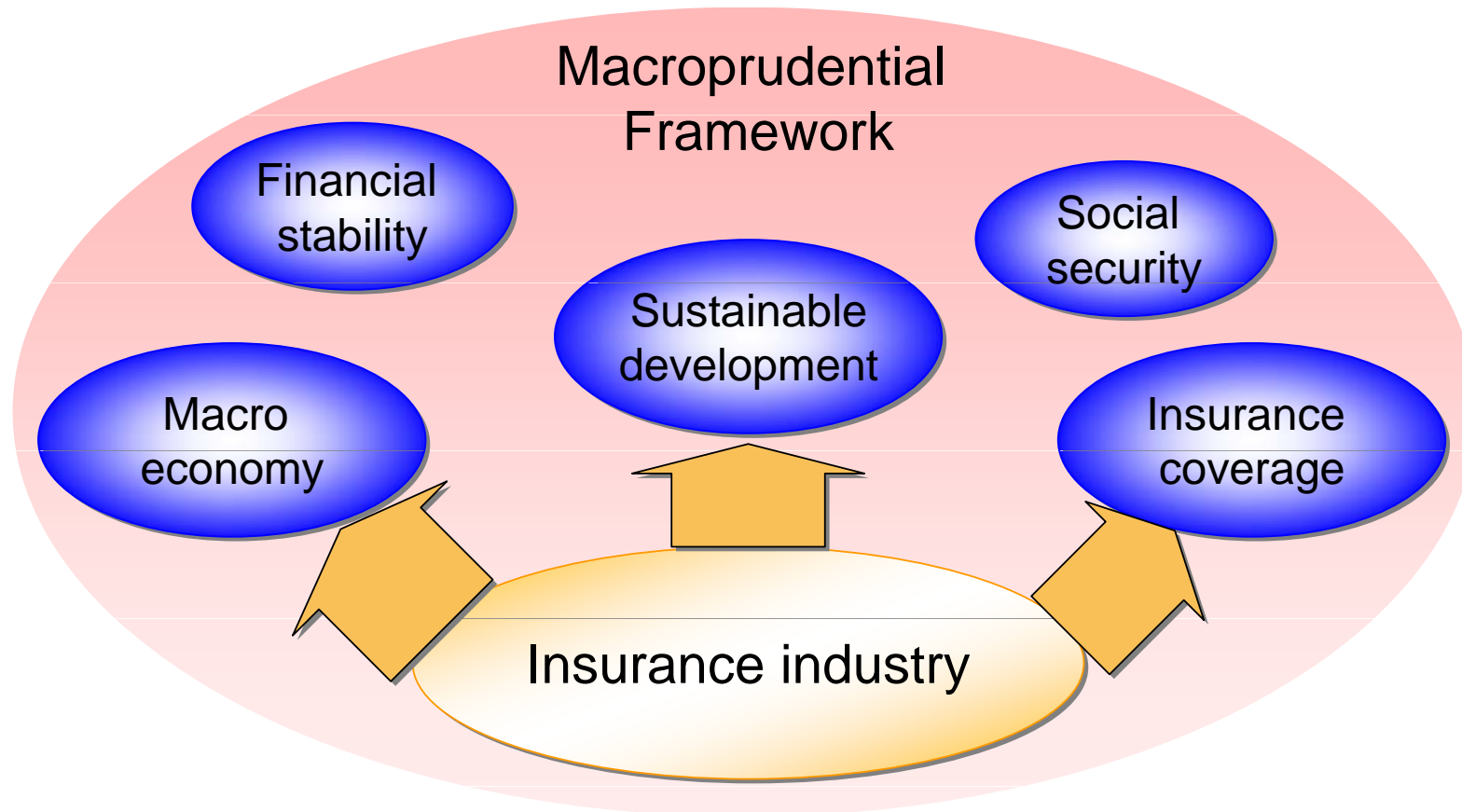
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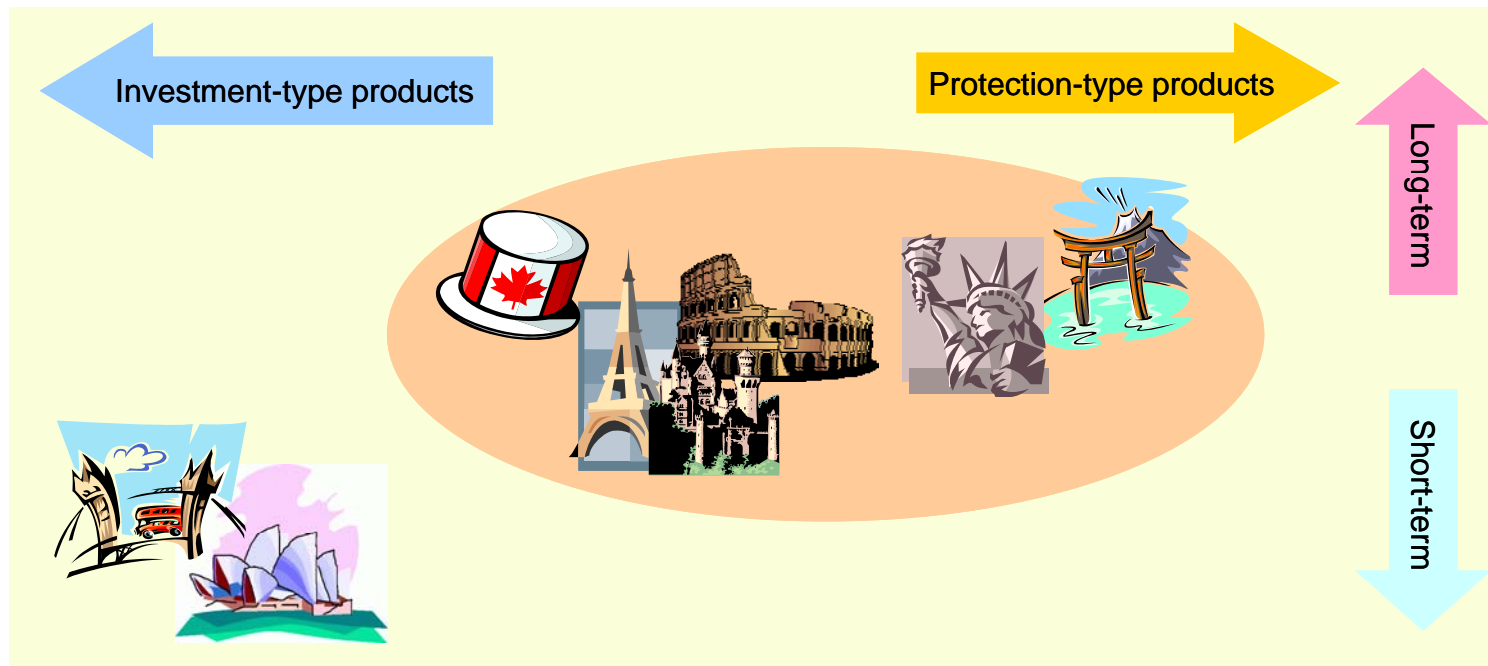
Macroprudential Framework

- Macroprudential Framework would not mean merely monitoring of systemic risks, but should holistically cover all the key dimensions



Insurance business models and consumers

- Different business models by jurisdiction that reflect:
 - Different risk preference
 - Expected roles of the insurers
 - State of development of financial markets



Regulatory implications

- **Economic-based regime should have a long-term vision**
- **If a short-term-minded solvency regime were implemented**
 - **Significant volatility** for long term products
 - Driven to transfer risks over to customers
 - Refrain from investing in non-fixed income assets
- **Unintended consequences might occur if banking regulations were copied for insurers**
 - Insurers play an important role as long term investors
 - Life insurers play an increasing role in the social security system
 - **Diversity** needed to support a sound development of the environment



(Photo – Buenos Aires, Argentina)



(Photo – Sydney, Australia)

Conclusion: yin and yang

- **Tao of supervision and risk management with a holistic framework**
- **Some words from Taoism**
 - **Be aware that the world is cyclical**
 - **Don't go to the extreme, otherwise you will fall**
 - Bring the balance of yin and yang to the universe
 - **In order to manage the world, you should control yourself**
 - In order to implement international standards, you should first know your own country

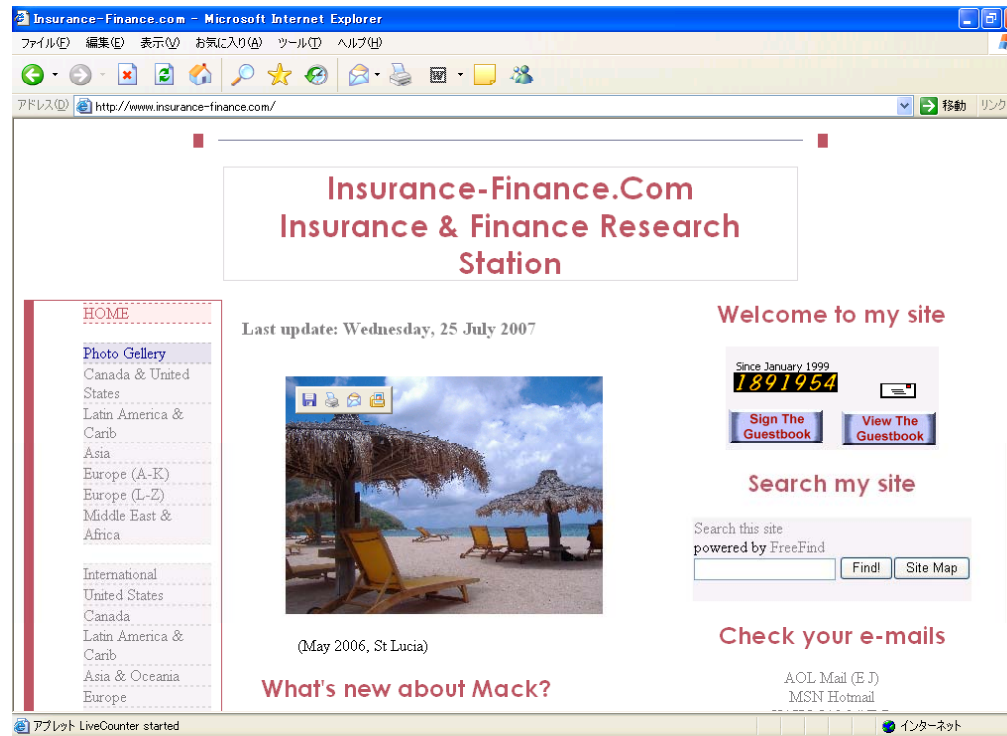


(Photo – Tao Garden, Chang Mai, Thailand)

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Demographic challenges and opportunities for Japanese life insurers

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