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EVOLUTION OF LIFE INSURANCE INDUSTRY THROUGHOUT THE WORLD

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- o What does the industry look like in various regions of the world: Western Europe, Eastern Europe, Far East and Latin America.
- o Why has the industry evolved so differently in different places?
  - -- Regulation
  - -- Taxation
  - -- Political climate
  - -- Demographics
  - -- Culture
- o What is the prognosis? Will the life industry ever globalize? Where are the areas of greatest opportunity?

MR. ROBERT L. COLLETT: Our first panelist is Demos Papasavvas. Demos was born in Cyprus in 1956. He went to the U.K. in 1974 to study at the London School of Economics. He graduated in 1977 and joined Mercantile & General Reinsurance Company (M&G) as an actuarial trainee. He planned to stay in the U.K. temporarily, but on receiving his Fellowship in the Institute, he decided to reside permanently in the U.K. During his time at the M&G, he gained experience in all types of individual and group life and health benefits, in both the U.K. and overseas. He had actuarial responsibility at M&G for U.K. clients outside the home countries, as well as for clients in Greece, Cyprus, and the Middle East. He is a partner in Bacon and Woodrow Consulting Actuaries. He is a member of their European team, specializing in Spain, Portugal, Greece, and Switzerland. Since joining Bacon and Woodrow, Demos has carried out a number of appraisals of European companies and has participated in the development of products and many other projects for companies on the continent. Demos will talk about the U.K. and southern Europe.

The second panelist is Ed Bonach. Ed is Vice President and Chief Actuary of North American Life & Casualty Company. Since 1979, that company has been a part of the worldwide insurance family of Allianz, one of Europe's leading insurers. Ed has been with North American during the entire period of Allianz ownership and has worked for three years for Allianz in Germany as a senior staff person for Allianz's director of foreign life insurance operations. That assignment, along with his continued involvement in Allianz international affairs, has provided Ed with first-hand experience of insurance

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operations in most European countries and other parts of the world as well. After Demos, Ed will speak to us about the balance of Western Europe and also about Eastern Europe. He will also share with us some of the very recent expansion activities of Allianz.

The third panelist is Noel Abkemeier. Noel first got immersed internationally in 1975 and 1976 when he was stationed in Japan for the licensing and establishment of a 50/50 joint venture company, Saison Life, formerly Seibu Allstate Life Insurance Company. He continued as the actuarial consultant to operations in Japan, Germany, and Mexico for nine years. He returned to Japan in 1985 as senior advisor and director and the sole Allstate representative at Saison Life. He has been involved in preparatory work for the Korean joint venture of Allstate and other Far Eastern research. He returned to this country and to Allstate only last month after five years in Japan. Noel will be talking about Asian challenges and opportunities.

MR. DEMOS K. PAPASAVVAS: I would like to start by looking at some statistics concerning life insurance sales. The market leader up until very recently used to be North America, with a nearly 40% share in 1986, but more recently, Japan has been increasing its share and by 1988 this was more than a third of the total. If we concentrate on the European Community countries, the market is really dominated by three countries, Great Britain, West Germany, and France, and between them, account for about 80% of the total life business sold in the European Community countries.

If we now consider life premiums per capita in 1988, Japan was well ahead of the rest of the field with Switzerland a clear second. Concentrating on the European Community countries shown in Table 1, the U.K. is at the top of the list with the Netherlands and Ireland high up the scale. The countries I will be concentrating on are Great Britain, which is at the top of the list, and Spain, Italy, Portugal, and Greece, which appear at the bottom of the list.

TABLE 1
1988 Premiums per Capita (U.S. Dollars)

	Life Premiums
Great Britain	715.7
West Germany	597.6
Ireland	526.8
Netherlands	483.9
France	456.8
Denmark	386.0
Belgium	187.7
Luxembourg	186.5
Spain	183.2
Italy	84.0
Greece	23.6
Portugal	20.7

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EVOLUTION OF LIFE INSURANCE INDUSTRY THROUGHOUT THE WORLD

Before I discuss these markets in more detail, I would like to consider the growth of life insurance in these countries over the last few years. It is interesting to note that the countries which appear at the bottom of the life premium per capita list are exhibiting some fairly high growth rates.

We will now look at the U.K. market in a bit more detail. Life insurance started back in the 16th century when people were taking out life insurance contracts, mainly on a one-year basis, to cover funeral expenses. At the time there were no restrictions on who you could take out the insurance contract on and, as a result, a number of people were using it as gambling. They saw the opportunity to gamble that a well-known person would die within the next 12 months or so and make some money. Towards the end of the 18th century, there were a number of people with quite high income but no assets who saw the need for taking out cover to protect their dependents. By this time the insurance industry was also getting itself organized and the Life Insurance Act of 1774 put an end to gambling in that it stipulated a person had to have an insurable interest if he was to take out a life insurance contract on somebody else.

Towards the end of the 19th century, the ordinary endowment contract as we know it appeared in the U.K. market and people started taking out life insurance contracts to save money. People gradually realized the need for life insurance as a means for saving for their retirement as well. The U.K. government was quite keen to promote this and in 1956 introduced legislation that provided tax relief for contracts that were used to pay pensions.

During the 1960s, single premium bonds flourished in the U.K.. A lot of money was switched from banks because people saw they could get very high returns by investing their money with insurance companies. Even though tax relief on nonpension contracts was abolished in the U.K. in the early 1980s, the increase in the need for insured pension provisions has meant that the life insurance market in the U.K. is still prospering. However, the recent Financial Services Act is making life rather difficult, especially for the smaller companies.

The U.K. life insurance market is certainly one of the most sophisticated in Europe. Several factors have contributed towards this. Firstly, liberal controls. The authorities in the U.K. realized early on that insurance was a good thing for the country and the people. They allowed a lot of flexibility to the insurance companies and allowed them to write a lot of business which, as far as the government was concerned, meant increased prosperity for the economy of the country. Insurance companies invested that money wisely in the country and helped the overall development of the economy. The government was also keen to provide good tax incentives. Some of the tax incentives we had in the U.K. were very good indeed. We have now lost tax relief on nonpension contracts, but we still have quite substantial tax incentives on pension business.

Another factor that has helped the development of life insurance in the U.K. is very well-trained sales forces and independent intermediaries. I do not think there is any secret in the fact that life insurance is not bought but sold, and it is therefore very important to have very well-trained people who can sell the products.

Another factor that has helped has been the reputation of life insurance companies. They were set up a long time ago and very well done. As a result, they managed to build up a very good reputation among the people who saw them as quite acceptable bodies with which to invest money. This is something that is quite different in some of the other countries that I will talk about later.

A great contribution towards life insurance company reputations has been made by the actuarial profession. Actuaries in the U.K. have traditionally been very conservative. As a result, companies were always very secure. Although not providing particularly good returns in early periods, policyholders at that time were interested only in security. That they certainly got.

The actuarial profession can also take some credit for product innovation in the U.K. In a number of other countries, there has been very little product innovation, mainly because their actuarial profession was not so well developed.

The wealthy economy of the U.K. has also helped in the development of life insurance because most people have money to spend on life insurance. Also, since we had funded pension schemes, people had to save money within pension funds to be able to provide for the pension benefits that were being promised. One way of doing that was to purchase insurance contracts.

If we now turn to the characteristics of the markets in Southern Europe, the picture is completely different. The first factor is the family unit. In most Southern European countries, family is a very close unit. In the past, though not so much now, whenever there were financial problems, the rest of the family would get together and help other members of the family. If, for example, a husband died and left a widow with not much money to support herself, either her parents or his parents or the brothers and sisters would come in and help. As a result, people did not see the need to take out life insurance. If something did go wrong, other members of the family would help.

Another factor that has not helped is superstition. When I was at school in Cyprus, my school had an arrangement with the local insurance company. They provided personal accident cover, where you could get a lump sum if you lost your leg or arm. A lot of people resisted this particular contract. They did not want to take out such cover, not because of the cost, but because they saw it as bad luck.

Most of the countries in Southern Europe have also suffered from low incomes. They have not been particularly wealthy and, without much money, it is difficult to encourage people to take out life insurance contracts.

Another factor that has not helped has been if the people had any money, they wanted to save that money in cash. They did not trust an insurance company. They did not even trust banks. Only a few years ago there were a lot of people in Cyprus, Greece, and Portugal who were very reluctant to give their money to a bank. They felt much happier keeping the money at home.

In a lot of these countries, people are not used to borrowing money. In the U.K. it is very common to borrow money to buy a house. This does not happen in Greece and certainly this did not happen in Cyprus or Portugal. People would only buy a house once they had accumulated enough money to do so. After that, there was no need to have any cover.

Another factor that has not helped has been the unfavorable legislation and taxation in these countries. The life insurance industry was very underdeveloped. The government did not see the need to encourage sales of life insurance and was not particularly keen to introduce advantageous terms for insurance companies.

Something else that did not help was the poor value for money that policyholders received in these countries. Premium rates in most of these countries were fixed by the authorities and they wanted them to be on a very conservative basis. As a result, premium rates were very high and policyholders received very poor value for money.

Finally, there were pay-as-you-go pension schemes. Unlike in the U.K., in most countries in Southern Europe all pension benefits were provided on a pay-as-you-go basis. As a result, there was no need to accumulate money and, hence, no need for insurance contracts.

Having said this, things are changing and have been changing for about 10-15 years in Southern Europe. The markets are becoming similar to those in Northern Europe.

Family unit -- This is still very important, especially in places like Italy, Greece, and Cyprus. That is changing. People now appreciate the need for having some insurance cover that would get them money in case one of the family policyholders dies.

Superstition -- Not so important nowadays. People are accepting the fact that it is not such a bad thing having insurance cover and they are prepared to buy it.

Low incomes -- The economies of the countries in Southern Europe are certainly improving and a lot of that is due to financial help they are receiving from the European Community. It should not really be that long before all the countries within the European Community enjoy similar levels of prosperity, and it should not be that long before the income of people in these poorer countries improves enabling them to buy life insurance.

Savings -- People are becoming used to the idea of investing their money. Stock markets have developed in Southern European countries and are doing quite well. Within the European Community, it should be a lot easier to invest money across borders. People are quite keen to do so. An insurance product would be one way of doing it.

Low borrowings -- Again, this is changing. People are now getting used to the idea of borrowing money to purchase a car or a house, and it is quite common for the lender to insist on some sort of life cover.

Legislation and taxation -- We have seen changes here. It is intended, although I am not quite sure whether it will happen, that across the whole of the European Community there will be common legislation and, possibly, common taxation. There are very great differences at present between the legislation and taxation rules that apply in various European Community countries. I think it is going to be very difficult to get uniformity. But, we are certainly moving towards it, and things are getting better in these Southern European countries.

Poor value for money -- With more freedom within the European Community, it will be easier for companies in countries like the U.K., where you have very sophisticated and competitive products, to sell their products to markets in other countries. As a result, local companies will be forced to improve the terms they are offering. They would only be able to do that in some cases with the approval of the government, because, as I said earlier, the governments fix premium rates in some of these countries. That should change.

Pay-as-you-go pension schemes -- I think this is the factor that is going to be the most important in the development of life insurance in these countries. Most of the countries have been offering quite substantial pension benefits -- benefits that the governments have not really been able to support. They are now realizing that and are quite keen for insurance companies to take over some of the pension liabilities the states have been providing or have been promising to provide over the past few years.

If you look at the distribution of elderly people, you see that there is quite a big difference between 1950 and 1980 in just about all the countries within the European Community. Things are going to get a lot worse by year 2025. Many governments have realized that and are introducing new legislation whereby they reduce the benefits the state is providing, hoping that the insurance companies will come in and supplement those benefits. This is something that is not going down particularly well among the people. They are used to being promised very high benefits by the state and do not see now that they should have to pay insurance premiums to get those high benefits. There is not much they can do about it. The countries do not have the money to provide these very high benefits. Something has to be done. It is expected that a lot of governments will be offering tax incentives to people to purchase life insurance contracts and that should be good for the life insurance industry.

There are a lot of changes happening. Things are improving in Southern Europe allowing it to catch up with what is happening further north. But, it is very important to remember that we are dealing with people from different cultures and different attitudes, and even though they are getting closer to what is happening in the Northern European countries, I think things will always be different.

I will try to illustrate the differences in culture by giving you some examples of what is happening in some of these countries. If we take Italy, for example, we have a problem of not just differences between the Italians and the rest of Europe, but differences between the Italians in Northern Italy and those in the south. Traditionally, Southern Europe has been poorer than the north. As a result, people in the south did not necessarily get along with people from the north. People in the south have been very

anti-insurance. It is going to take a while for them to be convinced otherwise, because they see insurance as a way of making the rich people richer. They pay money to buy insurance products from insurance companies that are usually owned by rich people from the north.

One or two more examples of differences in culture will help you understand why it will be difficult to get uniformity across Europe. In Greece, insurance companies have a very bad name indeed. One of the reasons for this has been the motor insurance industry. Motor insurance premium rates in Greece have traditionally been fixed by the state. Each successive government, not wanting to be unpopular with the public, fixed premium rates at levels that were not high enough. As a result, insurance companies did not collect enough money to cover claims. If you are not going to collect enough money to cover claims, the only things you can do to make sure you stay solvent and continue writing business are to either delay paying or refuse to pay the claims. As a result, the people were getting very poor service. As far as they were concerned, motor insurance and life insurance were both insurance covers they did not want anything to do with.

It is now law in Greece, although not enforced yet, that life insurance companies have to operate as separate entities from nonlife insurance companies. I think that will help the market quite a bit. People will concentrate on the fact that life insurance benefits are quite different from benefits provided by other types of nonlife insurance.

Finally, we can look at Spain. Companies there tried to introduce equity-linked contracts back in the 1970s. Companies in the U.K. were doing that very successfully, so the Spaniards thought, "Why not try this here?" Unfortunately, the stock market in Spain had a very bad time in the 1970s. As a result, people who took out equity-linked contracts had very poor performance and, if you talk to Spaniards today about equity-linked products, nobody wants to know. The results in the 1970s were so bad that it certainly put off everybody from taking out such contracts. Things will change, but I think it will take some time.

About four or five years ago, the insurance companies in Spain managed to get themselves very unpopular with the authorities there. In Spain there is a lot of black money, money that is owned by the people but not declared to the authorities. As a result, the income tax that the government was collecting was not particularly high. One way the government saw of putting that right was to insist that all banks in Spain declare the investment income they were paying on deposit accounts so the government could collect the income tax on that income, make further inquiries as to where the money had come from in the first place, and try to get some tax that way as well. When this happened, insurance companies saw a good opportunity to get some advantage out of it. They started selling what were effectively banking products -- life insurance contracts with little effective life cover. They gave a very high interest return to the policyholders on the basis that people would no longer be happy to have their money in banks, because banks had to tell the authorities where the money was. People switched money to insurance contracts, and the insurance companies gave it back to the policyholders in the form of interest. There were even banks that set up special insurance companies to do that. They effectively transferred money in the bank to their own insurance company and did not declare anything to the authorities.

Not surprisingly, the authorities were not particularly happy about that and insisted that insurance companies give them details of all their policyholders. Insurance companies were not happy with that and, to date, no agreement has been reached on what will happen. Such contracts are no longer being sold by companies in Spain. As a result of what has happened, insurance companies do not necessarily get along with the authorities in Spain. And the government there is not going to be so willing to give tax incentives to Spaniards that will help life insurance companies.

MR. EDWARD JOHN BONACH: My comments are going to focus on non-Southern Europe, including Eastern Europe, with a special focus on the new Germany. Even though there is considerable activity in bringing Eastern and Western Europe together, significant differences still exist and my comments are going to separate the two for the time being.

The Western European life insurance market can be characterized as a complex, provincial, and quite difficult market to enter for foreign companies. Additionally, the market is not homogenous, due to differences in culture, language, economic and political environments. Of the Western European countries, the most significant life insurance markets are Great Britain, France, and Germany. The life insurance industry in Western Europe is currently undergoing substantial changes as a result of the 1992 initiatives within the European Economic Community or EEC. The intention is to achieve a free internal insurance market within the EEC by facilitating the freedom of establishment and the freedom to provide services for insurance companies. This would allow companies to set up a branch in other member states that could operate under the same conditions as those applicable to local undertakings, and companies could operate across country borders without having to have a physical presence there.

In the future, it is planned that an insurance company will only be subject to home country control, whereby the company is able to sell its whole range of products in any other EEC member country. This liberalization or deregulation will increase competition and thereby the consumer's opportunity to choose among a greater variety of products at different prices.

This will be balanced by increased consumer risk, as consumer protection will inevitably decrease. The demand for protection is particularly higher in life insurance as our product is an invisible commodity whereby the occurrence of a specific event, such as a claim, is the first time the true quality of the contract is allowed to show through. The alternative to home country control is host country control, which is an issue that is currently receiving a lot of attention in Europe. Proponents of host country control argue that it is the host country that is familiar with the way of thinking of the customers of its own country, as well as the legal, economic, and social systems of that country. The issue of home or host country control characterizes the before-mentioned differences, compounded by very strict premium, nonforfeiture, and valuation requirements in countries such as Germany on the one hand, and Great Britain on the other hand with considerable flexibility.

The tax structures of the countries also add to the challenge, with France imposing a premium tax that is nonexistent in other countries for life insurance. Death and maturity

proceeds in Germany are income tax free. In a unified market, a country imposing no tax would be reluctant to institute a new tax and thereby make its life insurance products less competitive. On the other hand, a country such as France may be reluctant to eliminate its tax and thereby forego important tax revenues.

Politically, one has to also remember that many of these countries have had differences that have been so substantial that they have been at war. Even though the climate has improved somewhat, there are many scars that will take years to heal.

Also, there is a dichotomy between countries with the wealthier, more developed EEC members confronted with rapidly aging, and in some cases, shrinking populations. The Southern EEC populations are younger and growing.

Another major factor in bringing the European life insurance marketplace together is that the six largest EEC countries have their insurance markets dominated by a few large national companies. My company's ultimate parent, Allianz, for example, is Germany's largest insurer on both the life and the nonlife sides, with market shares in each sector of more than 10%. This domestic market dominance has led many insurers to increase market presence via acquisition. Group Victoria, one of Europe's largest insurance groups, acquired a controlling interest in Germany's second largest insurer, the Colonia. Allianz continues to establish strategic footholds in all of the major European countries through acquisitions such as the RAS Group in Italy a few years ago and a 50% share of France's Compagnie De Navigation Mixte, to name a few. Cross ownership of banks and insurers has been commonplace for years in many European countries, and especially in Germany. Joint ventures with financial institutions, and in particular banks, are also occurring. Europe's largest bank, Deutsche Bank, has formed its own life insurance company. Allianz is cooperating with Germany's second largest bank, Dresdner Bank, and other banks in European countries to distribute insurance products.

To confuse the matter further, German reunification has made some European nations more cautious about a unified European market. The crumbling of the Berlin Wall, German reunification, and the new openness of the Eastern bloc constitute some of the most significant developments in the world in recent history. Eastern European life insurance markets are quite underdeveloped due to the effects of the socialistic state that they have lived under for years. In the Eastern bloc, the U.S.S.R. is the largest market. It is also quite underdeveloped on a per capita basis. At the center of this melding of East and West is the Germany reunification. While West Germany will bring with it its strong Deutsche Mark, its investment, economic and social systems, East Germany's citizens will be hit hard by unemployment, inflation, and continuance of poor social conditions for many years. Many East Germans are also quickly learning that a hard currency is coupled with hard work. Productivity in East Germany is less than half that of West Germany. Wages are bound to rise and bring some parity, which will make many industries noncompetitive. An initial positive sign, however, is that despite the recent reunification, the German Mark has held its value, and inflation has not yet been ignited.

East Germany has adopted West German legislation regarding stock corporations, limited liability companies, partnerships, and mutual companies, as well as legislation for

free market pricing based on supply and demand. This legislation, however, will limit free market principles during a brief transitional period by enabling the government to set prices for contingent, economic, or ecologic reasons. Allowing immediate market determination of prices in sensitive areas, in a country used to a climate of heavy subsidies, might cause some undesirable political tension. Most of the sensitive items should not directly affect the life insurance industry, but they will impact some of the operating costs, such as for leases, energy, postal services, and telephone charges.

Life insurance is quite heavily regulated in West Germany, so the reunification should not result in a significant regulatory change. Premium rate assumptions are essentially mandated on quite conservative assumptions, with competition occurring at the dividend level. Almost all of the policies sold are participating. Furthermore, at least 90% of company gains must be distributed as dividends, with competition forcing this percentage towards 98% currently. An interesting note to this regulated environment is that there is no equivalent to the SOA, no actuarial body, and no exam process.

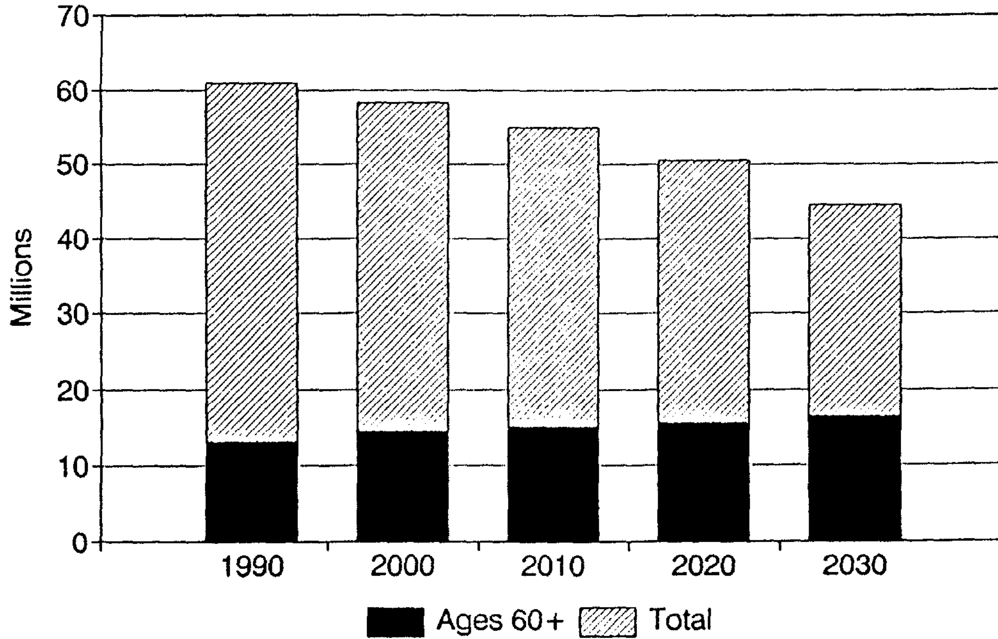
East Germany is also planning to charge a variety of duties on imports to protect its economy. The aim is to allow East Germany's industry to have a grace period to adapt itself to world market competition. Demographic changes that we have in the U.S. affecting our Social Security system are even more pronounced in West Germany due to the shrinking and rapidly aging population. Chart 1 shows this trend. East Germany's population of about 17 million should help somewhat, in that their population is slightly younger, but it will not correct this aging of the population or its rather rapid decline.

East Germany's social security system is not adequately funded and will not be able to satisfy the needs of retired people if they immediately adopt the West German system. Merging of the two systems will have detrimental effects on West Germany's system. To address this, a pension, health, accident, and unemployment insurance system corresponding to the West German system is being developed and adopted in East Germany. To finance this, West Germany will be providing 55 billion Deutsche Marks or more than $30 billion over the next year and a half.

This highlights some of the major economic issues and other issues that are facing reunification. The insurance market is rapidly changing, primarily as a result of cooperative ventures between the East and West. In this regard, Allianz has secured a 51% stake of East Germany's previously state-owned insurance company, Deutsche Versicherungs-AG or DVAG, in East Berlin. Allianz's participation will call for a considerable investment above and beyond its initial capital or cash contribution, especially in data processing and developing, training, and supporting the staff at DVAG. I recently returned from a visit there, and was quite appalled to see that, in many cases, things that we take for granted are not present there, such as each employee having a telephone or access to a telephone. You can imagine what the state of any electronic data processing or personal computing is.

The marketplace in East Germany is now open for other competitors with a large number of companies already setting up representative offices in East Berlin and East Germany. The West German Cartel, or antitrust, law has been adopted by East Germany in its entirety, including its merger control provisions. The East-West Treaty,

CHART 1



Source: Data from Statistisches Bundesamt

however, does allow for more liberal merger control for an interim period to accelerate investments in East Germany. Acquisitions and joint ventures are also occurring in other East European countries. Included in this have been some acquisitions and joint ventures in Hungary as well as Yugoslavia.

It is my opinion that the melding of the worldwide financial markets will inevitably lead to the globalization of life insurance as well. Change will continue to occur, although most likely at a slower pace than in the past couple of years. I believe it is unrealistic to think that decades of protectionism rivalry among European countries will quickly be eliminated, so some major obstacles should still be expected to exist. The melding of the markets in both East and West certainly will provide additional opportunities for life insurers. In my opinion, over the long term, joint ventures and other cooperative affiliations will emerge as the most successful way to penetrate and be successful in the various European marketplaces. The opening of borders and deregulation will most likely be followed by a period of realignment and consolidation. Specialty-niche players, however, should also have ample opportunity. In any case, the need for innovation and efficiency while providing products and services that are customer oriented and appropriate to the respective local markets, cultures, and needs constitute the key success factors for a life insurer trying to operate in Eastern and Western Europe.

MR. NOEL J. ABKEMEIER: You have just heard how the insurance industries in Europe are a combination of mature industries and developing industries. The same is true in the Far East, where Japan is the world leader in insurance premium at 35%, Korea is emerging and represents about 2%, and the other countries are varying degrees behind. I would like to comment on the factors that are influencing their future development.

Heavy regulation is a characteristic of all the markets. Invariably, there is a single supervisory authority, usually the Ministry of Finance, which grants licenses for the performance of any activity in which you wish to engage. This includes licensing for products, premium levels, dividends, and perhaps even marketing methods. Often these items are virtually standardized within the industry, and this makes differentiation difficult. Another problem is that understaffing by the regulator leads to a severe limitation on the number of approvals that could be obtained, often imposing limitation on the range of your operations.

The regulation under which you operate is not necessarily published, but it may also be conveyed in an informal manner via unwritten communication or partially conveyed through a close working relationship among the regulators, the industry association, and leading companies.

Taxation provides a mild influence toward the purchase of insurance. The inside buildup is protected, and there may be a moderate deduction of premium for tax purposes.

The political climate has considerable influence on operations in these markets. Virtually all of the markets have been closed to outside penetration until external pressure created an opening. Generally, countries have tried to protect their markets for local investment as much as possible. This may be in the form of total closure or the

requirement of local ownership participation. The speed of deregulation within the insurance industry is also politically sensitive insofar as deregulation is generally not favored by leading companies, which benefit from the status quo. Finally, it is not uncommon to find life insurance as a tool for helping to implement social and economic policy. This can be particularly true in investment guidance and dividend directives.

In many countries, the industries are in their infant stages, and demographics have not yet been able to demonstrate an influence. However, in Japan, where the population is aging most rapidly in the world, a clear return to savings-type products is emerging. The main determinant of market growth and insurance spending in any of the markets is per capita GNP, and the goal for anyone entering the market is to gain a foothold before this begins its rapid growth.

Culture has a major influence on the buying process. Women, as the family financial managers in Japan and Korea, have a significant role in the purchase decision. The cultural emphasis on personal relationships makes the sale on the basis of product differentiation more difficult. Nationalism is strong, and this can impede the growth of market share, defer entry into the market, or even require the sharing of ownership with local partners. A cultural acceptance of gambling in the Chinese cultural areas seems to lead to loose attitudes about asset management.

These influences lead to a number of characteristics that differentiate these markets from American markets. The market structure is generally concentrated in a very few companies. It is not uncommon for the leader to hold a third of the market and the top two or three companies to have a 75% share. The leading company in Taiwan holds a 51% market share. New entrants are not freely admitted. Entry requirements may demand an initial or ultimate local partner. Also, you may wish to use a local partner to achieve market penetration.

Markets generally evolve from debit-type savings products to a broader spectrum of more risk-oriented products as the economic status of the national economy improves. Selling is heavily done by women in male-oriented societies and thus has a low status. One result is a heavy turnover of sales personnel which in turn leads to the usage of simple products. Sales success is heavily dependent on personal relationships rather than product and price competition. This may be reflected in numerous sales visits by the agent while a relationship is being built.

It is imperative for an insurer to think differently about the method of business management, particularly in the investment area. A willingness to take higher risks on investment creates some belief among local company management that insurance operations exist to provide a cash flow for profitable investment operations. In most markets, inflated real estate and stock values have created large unrealized gains that are believed to be a cushion for adverse investment experience. One result is that asset liability management is not a concern. Of course, it should be. Regulatory action may be viewed as a safety net for otherwise risky activities.

These various factors lead to operational challenges as a company is being established and then continues operations. At the time of formation, you may need a partner either

to gain entry or to create a method to gain market share. Start-up is difficult because of a shortage of experienced specialists and the unavailability of ready-to-use computer systems. American computer systems vendors are adapting to the various Oriental languages and local reporting requirements, but there are still no easy off-the-shelf systems. Marketing methods that you may consider standard may be difficult to install. In general, there is strong pressure from within the organization to conform to the standard local method of operation rather than trying to differentiate with approaches that are new to the market.

Ongoing operations provide less flexibility because regulation is by permission rather than proscription. Conceptually this is limiting, and functionally it may be a bottleneck. The investment culture is relatively high risk; thus, it is necessary to use a less conservative than usual investment policy to stay in touch with the market. Sales force retention is an enormous challenge with 40% total annual turnover not unusual. The high level of turnover is generally reflected in policy lapses, which can be equally high. This area can produce enormous rewards if it is solved. Complicating these various issues is the strong position of the market leaders, who have not only a commanding market share, but also considerable surplus accumulated in prior years. In the event of deregulation, this could provide a tremendous advantage.

Many of these problems might normally fall within the realm of an actuary; however, the role of the actuary is narrowly defined as that of a valuation actuary in most cases. This limits the local support the actuary from the parent organization might have and also may reduce the perceived range of his competence.

Finally, I would like to review the situation in the various markets in the region. The leading market, of course, is Japan. It is rapidly maturing and would not appear attractive for entry for various reasons. The 20 traditional companies still retain a 97% market share, despite the entrance of 10 foreign capital companies over the last 17 years. Deregulation is beginning, and the resultant realignments within the financial services industry and the increased differentiation within the life insurance industry are likely to put pressure on profit margins. While the traditional companies have ample surplus to meet the challenge, the newer companies will be in a much weaker position. The final deterrent is an entry capital requirement of about $70 million.

Korea has been the most attractive market for foreign entrants in the last four years as the doors were opened for the first time. In this short period, the life insurance industry has exploded from six companies to 30 as U.S. companies were granted entry after a government-to-government agreement was reached. On the one hand, it is still not too late to enter because the GNP per capita is still less than half that of Japan or the U.S., and the appetite for insurance has enormous room to grow. On the other hand, the prior entry of many newcomers has already captured many of the desirable partners, so a new entrant will have difficulty establishing a market presence.

The next country on most lists of desired countries is Taiwan, which has allowed U.S. companies to establish branches as a result of government-to-government negotiations. For several years, two new entrants have been allowed each year, and there is expected to be a general liberalization within the net year. The industry has relied heavily on

skyrocketing stock market and real estate values for its profitability and is shaken as the stock market has fallen 70% since February of this year. Although the foreign capitalized operations have been precluded by regulations from some of the higher-yielding investments, they nevertheless must be prepared to acclimate themselves to operating in a high-risk investment climate. Aside from evaluating the opportunities of selling to the 20 million population of Taiwan, another question is whether this provides an entry to the market of the Peoples Republic of China. While relations have been thawing slowly, it is not clear that an insurance business would be easily transplanted or expanded.

Hong Kong has been an active insurance market as a result of its history as a British Colony and its geographic position as a crossroads. The two significant impediments to a positive evaluation of the market are its size of 6 million persons and the uncertainties of the economic status after it reverts to the Peoples Republic of China in 1997. Although there is a stated guarantee of a continuation of the current capitalistic economic system for 50 years, there is much doubt about the reality of this. The cost of entry to the Hong Kong market is low, and it probably should be viewed as a bet that it will become the doorway to Southern China.

Thailand is the most rapidly growing economy in Asia, and thus has a prime characteristic of an attractive insurance market. Unfortunately, the government is trying to limit foreign influence in the market and is not permitting new entrants at this time.

Malaysia has a population of about 17 million and thus is a moderate-sized market. The current political attitude is to protect domestic interests in the industry with the requirement that at least half of the venture be locally owned. In later years, at least 30% of the ownership must be Bumiputra, the indigenous Malaysians.

The Philippines is a sizable market of more than 50 million persons. However, the political situation over the last four years has made the direction of the economy and the attractiveness of the insurance market very uncertain. Once a clear political picture evolves, the market could become favorable if a strong economic foundation returns.

Singapore has been marked by a stable government and a consistently strong economy since its formation 30 years ago. However, its population of only 2 million makes it a low potential market. Its strength as a financial center does not translate into its insurance potential.

Indonesia, with a population of more than 180 million people, certainly is of a size to look attractive. However, a very low GNP per capita does not provide much current opportunity for insurance sales, and its diversity presents a challenge to any insurance operation. It is spread over more than 13,000 islands, is populated by more than 300 ethnic groups speaking 250 dialects, and relies on five major languages. By most standards, this is a market that still will have a long period before it shows attractive growth potential.

The Peoples Republic of China is always the dream market in which to gain a foothold for its long term potential. Of course, the per capita GNP of less than $300 per year makes this market unproductive at this time and for an extremely long period into the

future. For this reason, many persons find it best to hedge their bets via Hong Kong or Taiwan where the investment might pay a current return while keeping open the potential for expansion to the Peoples Republic of China.

In summary, the markets in the Far East do not show clear potential in the short term, but they could be attractive over the very long run. Success, however, requires a clear regional commitment and a strong internationally oriented culture in the home office.

MR. COLLETT: I am going to talk about one other part of the world that we certainly cannot afford to overlook, namely, Latin America. As is true in so many other ways when one is talking about Latin America, it is a land of contrast when we try to evaluate its insurance potential. As Tables 2 and 3 show, it is a very large market in terms of population, but quite a small market in terms of insurance presently in force.

TABLE 2
Population (in millions)

	Estimated 1990 Projected
Argentina	32.3
Brazil	153.8
Chile	13.0
Columbia	32.6
Mexico	88.3
All Latin America	450.0
United States	250.4
World	5,332.8

Source: U.S. Bureau of the Census, *World Population Profile*, 1989.

TABLE 3
Size of Insurance Market (in millions)

	Life Premiums	Total Insurance Premiums	Total Insurance as a % of GDP
Argentina	$ 126	$ 1,575	2.6%
Brazil	132	1,046	0.9
Chile	244	481	2.2
Columbia	93	601	1.7
Mexico	722	1,989	1.2
Venezuela	125	1,735	2.7
United States	176,809	431,399	8.9

All figures are as of 1988.
Source: Reprinted with permission from sigma, *Economic Studies 4/90*, Swiss Reinsurance Company, Zurich, Switzerland.

Latin America taken as a whole is considerably larger than the U.S. However, there is a lack of penetration of insurance into the lives of individuals -- 1-2% of gross domestic

product versus a much larger percentage for the U.S. average income is quite modest throughout most of Latin America, and most Latin countries lack a middle class of significant size that could form the bulk of insurance purchases.

A couple of the largest countries, Argentina and Brazil, have so many financial problems today that it is difficult to be optimistic or enthusiastic about them. Brazil had an inflation rate well over 1000% per annum the last time I looked. Argentina is really an amazing country. It is so rich in natural resources and potential. The proof of that is: how otherwise could it have survived 150 years of political mismanagement? It is amazing to realize that only a couple of generations ago, it ranked as high as it did in the world in terms of productivity and per capita income, but has slipped so far by 1990.

I would like to focus on just a couple of countries -- two Latin countries that I know best -- Mexico and Chile. They also happen to be two bright spots in the Americas -- ones that offer significant potential for gains by the insurance industry both domestically and internationally.

Family units have traditionally been quite strong with family obligations to family members and to servants and supporting employees. However, we see it breaking down there as families become less cohesive with moves to the cities and changes in the economy. In case you might not know it, Mexico City is the largest city in the world with a population somewhere between 17 and 20 million people, and growing.

Inflation in Mexico during the 1980s had a significant and detrimental effect on the insurance industry. Inflation was quite high in the mid-1980s and exceeded 100% per annum for a time. During that period, inflation washed out most of the traditional life policy values in Mexican companies. Nearly all Mexican companies are composite companies, both nonlife and life products being offered. Those companies were also damaged by inflation in replacement coverage benefits on the nonlife side.

Coming back to life insurance in Mexico, universal life insurance was introduced in Mexico in the 1980s. We should never underestimate the influence of the U.S. on Mexico due to proximity and the many financial ties. Universal life insurance in Mexico is a somewhat different form with products typically being index-linked with respect to both benefits and premiums.

Inflation has moderated significantly in Mexico in the last couple of years. This moderating has partly been artificial, due to government lids on wages and prices, but in part it has been real, achieved through other positive government actions. Traditional life insurance has not made a comeback in Mexico, but cash value universal life contracts are selling well, and term products are a significant factor in the market, also.

There has been quite a remarkable shift in the political and regulatory climate in Mexico with the change in government. Although the political party in power has not changed, the government of Carlos Salinas Gortari is very much to the economic right of previous administrations. Perhaps in fairness to De La Madrid, although his term in office was considered an economic disaster, in fact some of the programs that he began have paid dividends during the term of Salinas.

In any event, what is going on now is quite remarkable. The negotiations concerning free trade and open borders for Mexico, Canada, and the U.S. are proceeding rapidly by historical standards. Also, we are hearing somewhat more about the possibilities for a Latin American common market. That, I see as farther down the road. As far as insurance is concerned, the Mexican market has been open for foreign investment up to 49%, a percentage that constitutes effective control in many cases. There seems to be every likelihood that larger ownership percentages will be permitted in the near future. As a result, most Mexican companies are scrambling for foreign partners. Nearly all have been in need of additional capital, and now it seems within their reach. It also seems likely to me that as this process continues, there will be a contraction in the number of companies in Mexico, approximately 40 at this time. Some predict that the number might shrink by a third or more.

It is also possible that Mexico may permit direct selling in its market to its nationals by foreign companies. This is probably a couple of years away, but I see it as a real possibility. We also see Mexican companies seeking entry into the U.S., primarily to sell to Hispanics in the U.S. If a company has yet been admitted, I am not aware of it, but I am aware of discussions in both California and Texas.

Within Mexico, the regulatory climate is much friendlier today than it has been in the past. The Department of Banking and Insurance has been split into a Department of Banking and a Department of Insurance. Banking, which was nationalized in the 1970s, is now being reprivatized. I think this phenomenon will have important implications for insurance in Mexico, since prior to nationalization of the banks, many Mexican insurance companies were directly aligned with banks and had interlocking ownership.

There also have been important developments in pensions in Mexico. Previously, pension assets could be invested only with the nationalized banks. It is now possible to invest pension assets with insurance companies. This change should lead to a significant growth in assets of the insurance companies.

Pensions are dealt with favorably from a tax standpoint in Mexico. Within broad limits, contributions are deductible as made and the benefits paid are nontaxable. The market for penetration is quite large and relatively untapped. One set of figures I have seen suggests that only a couple of thousand out of the several hundred thousand or so registered Mexican companies now have retirement plans in place. It also is of interest that in Mexico, companies and the Mexican government are actively examining the Chilean privatized pension system and have sent missions to Chile to study that program.

Chile has a very different situation for insurance from all of the other Latin countries. Although it is a small country, about 13 million people, insurance companies there are growing very rapidly in terms of assets under management. There is a particular reason for that growth. After Allende's Marxist government was overthrown in the 1970s and General Pinochet took over, there was a dramatic shift to the right politically and economically.

The shift included a scheme of privatizing the country's social security system. The private scheme created private funding vehicles to handle preretirement accumulations.

The system mandated contributions into the system from all workers and required conversion into insurance annuities at retirement. The result of the change has been a rapid asset growth, first in private funding vehicles, and then in the insurance companies that participate in the system.

The government in Chile also brought inflation under control. It has been less than 15% in recent years, so it was also possible for cash value life insurance to survive, if not prosper. Life insurance lags far behind in its contribution to insurance company growth in relation to pensions. In fact, companies that are active in the annuity system may not market other lines of business to a significant degree.

Mexico and perhaps some other countries are taking a hard look at the Chilean system as a way out of some long-term problems that are inevitable in their social security systems.

Insurance regulation in Chile is very extensive. The regulatory code tries to dictate all elements of reserving, including formulas, interest rates, mortality, and whatever else might be a factor. In 1989, a mandatory asset/liability match testing scheme was adopted. It requires extra reserves to the extent that there is an asset/liability mismatch by their reckoning. I would characterize the industry in Chile as overregulated.

In terms of impact of the culture on the industry in Chile, maybe the most interesting illustration relates to the fact that divorce is not permitted in Chile. As a result, it is very common in Chile to find a man or woman living with someone other than his or her spouse. The pension scheme explicitly recognizes the legitimacy of those relationships. If a man by document acknowledges a woman other than his wife as his partner, she, as well as the wife, can receive survivor benefits, as can her children. All of this leads to some very interesting valuation records, as I found when reviewing the reserves of one of the largest companies. The string of beneficiaries in several cases included not only a wife, but several "significant others" and many children belonging to the various relationships. It was a very interesting puzzle since survivor benefits differ under different circumstances. In some cases the children receive benefits directly, while in other cases the children receive benefits indirectly, and the woman's benefit will be a function of the ages of her children. Underlying policy information contained all that was needed to sort it out, but the electronic records and valuation extracts certainly did not.

I think that selective opportunities in Latin America are excellent when viewed as niche markets. I think one must choose one's partners very carefully, of course, as would be true anywhere in the world. One should not make the mistake of assuming that Latin America, or Latin American countries of North, Central, and South America are all alike, just because the languages are similar. Political climates, economic situations, even the cultures are so diverse that one has to treat them individually.

We would now like to talk about the outlook for the future and see what the prospects are. As a first question: What are the outlooks for globalization and what are the primary impediments to globalization?

PANEL DISCUSSION

MR. ABKEMEIER: We have been talking about running an insurance company around the world, but I think there are two other aspects to look at: globalization of investments and globalization of insurance management. My belief is that companies who become global in the area of investment management will have opportunities to get good yields in other parts of the world or to arbitrage investments. I think it is inevitable that companies will think globally in relation to investments. In the corporate management area or in setting up operations around the world, I think some initial opportunities will occur as countries need capital and expertise that we can share. However, after starting up that way, I believe nationalism is going to reign strongly and that subsequent growth is going to be difficult.

The biggest hurdle or impediment is that there are certain inefficiencies in operating around the world. You use a different system everywhere and you do everything at arm's length -- uncomfortable and inconvenient and not efficient. The second thing is companies have to develop and maintain a corporate global vision and global culture. Those are few and far between, and I do not think that too many companies are going to develop a real global vision.

MR. BONACH: I would like to echo a lot of what Noel said and also emphasize that cultural differences are very important. I think U.S. insurers operate in an environment where English is the international business language. I do not see that changing. Yet, if we become pompous in the luxury that we have in being able to operate in English around the world and forget about foreign cultures and languages, we will be at a disadvantage. I think that having people who understand those cultures and people who can speak those languages is the way you will get insights into those markets and populations and into what is really needed to be successful and to do business in those countries.

MR. KEVIN M. LAW: Is there a particular product or perhaps a category of products that might be considered the most viable from an international perspective in the sense that it fits very well with the tax, regulatory, and economic environments of many different countries?

MR. PAPASAVVAS: I am not sure about any individual product as such. I think what will happen is that some ideas will be copied and adapted in various countries. There are so many differences in terms of legislation and taxation that it would be very difficult for one particular contract to be sold on a global basis. An example of a product that U.K. companies tried to introduce in other countries was a type of endowment product whereby you have a low basic sum assured and take a decreasing term cover on top of that so that by the end of the product you have enough money to repay a loan. It is called a "low cost endowment" in the U.K. I do not know if you have anything corresponding here. U.K. companies thought this was a wonderful product and tried to introduce it into other European countries. A number of companies tried this in Spain without really looking into the details as to whether it would sell there and discovered that taxation of the products was such that nobody was interested in buying them. In Spain you get tax relief on capital repayment as well as the interest you pay on a loan. Therefore, people were much better off repaying the loan, or at least the capital part of it, directly to the lender. Buying an endowment product whereby they would lose that

tax relief made no sense at all. This is a classic example of a product that companies thought they should be able to sell everywhere but, because of differences in taxation and legislation, could not. I think pure protection products may be sold on a global basis. In these you have a loan from a lender, the lender insists on some sort of cover, and you are just covering the outstanding loan. I do not think taxation would play such an important role there. But other than that, I think it would be very unlikely in the foreseeable future to see any global products.

MR. ABKEMEIER: A comment from a little different angle. The sophistication of the sales force and the clientele dictates a lot and, from that angle, I find plain vanilla endowments, term insurance, and whole life fit best in most markets and tend to fit nicely with tax situations, too.

MR. COLLETT: I see Luis Huerta who is president of one of the larger Mexican companies. I wonder if you think my optimism about Mexico is well founded, and is Mexico a country U.S. insurers should be getting into or looking at?

MR. LUIS HUERTA: Yes. There are several things that make us optimistic. What you mentioned about the Salinas administration and the opening of the Mexican economy will, of course, produce a completely new way of doing business in Mexico, bring in new players, and strengthen competition. It will also permit the market to grow. One thing that is very important is it is almost certain that the social security pension scheme is going to be privatized like that in Chile. This will be an enormous opportunity for any local or foreign carrier in Mexico.

MR. CHARLES C. MCLEOD: A question for Noel about Japan. As is the case with many other of their industries, Japanese life companies, to the best of my knowledge, have not done any business outside of Japan, either in the U.S. or other countries. I wondered if you would give us your views as to why that has been the case, and whether you think it is likely to change in future?

MR. ABKEMEIER: On your question of why they have not done business outside of Japan, the market itself has been in rapid growth in my 15 years of familiarity with it. I think they were just reinvesting the gains that they had and doing what they could to maximize their domestic growth. I did not catch your last question.

MR. MCLEOD: If they have not expanded outside of Japan up to now, would you expect, say in 10 years, the Japanese to have entered the U.S. market in the way they have in cars or other manufacturing industries?

MR. ABKEMEIER: Yes. I am sure they are looking very hard at the U.S. market and as you are aware, they have made an investment in Lincoln National. I know the largest companies have money coming out of their ears and would love to come into the U.S. market. I think various temporary frictions between the U.S. and Japan are delaying it. I would say with a time frame of 10 years from now, every major Japanese company will have some kind of operation in the U.S.

MR. PAPASAVVAS: If I could just add to that. I have had very limited exposure to Japanese companies, but there certainly are a lot of Japanese companies looking very closely at Europe at the moment, and the impression I get is that they are taking their time in deciding what to do. Once they decide what they will do, they have plenty of money, and they will be able to buy any company they like in no time at all.

MR. BONACH: I think the influence of the Japanese highlights the whole issue of globalization of the life insurance marketplace, and I think that as you see these companies with excess capital entering the foreign and world life insurance markets, there will be an increased competition for high-quality companies for strategic alliances and for capital and talent in general. That is going to pose some interesting challenges and opportunities for all of us, including the companies here that think they will not be international in their scope. I think they will be impacted by foreign entrants into our market as well.

MR. COLLETT: Ed, you said something about the international actuary. Do you think it is necessary for actuaries to become more international? Is it possible to be unaffected by all of that?

MR. BONACH: I think it is fairly difficult to be totally insulated from the occurrences in the world insurance market. I see an increasing demand for the so-called international actuary. I think a lot of you have seen the different management recruiting advertisements. I think that there is a lot to be gained by looking at what is happening in the different marketplaces as far as actuarial work. Our friends in the U.K. have done a lot of work with unit-linked products, the valuation actuary concept, and the whole idea of the investment actuary. There has been a lot of work in some of the other countries as far as analyzing the impact of AIDS, and I think those are the kinds of things that we can also learn from. I challenge everyone to be international in their perspective, even if it is only to be cognizant of the fact that there will be more competition for the actuarial talent that we are all trying to obtain for ourselves and for our companies.

MR. PAPASAVVAS: I would certainly go along with that. As I said earlier, I cannot see a product that will globalize and be sold all over the world. But having said that, we can certainly learn a lot from products being sold in other countries and adapt them to make sure we can sell them in every market. It is very important to make sure that we do not just copy those products. A number of companies have made that mistake, and it would be very naive to think a product that is selling in a particular country should sell in other countries as well. We should always be prepared to adapt any products we have.