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INTERNATIONAL REINSURANCE

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The panel will discuss life, accident and health reinsurance markets in Europe, Central and South America, and the Far East. The following areas will be discussed:

- *Growth potential in these different markets*
- *Where to go to find the reinsurers*
- *Assistance with sales, reporting, etc.*
- *Currency risk issues, political and economic risk issues*
- *Type of reinsurance YRT, coinsurance, modified coinsurance*
- *Regulation (U.S. and others)*
- *Tax issues*
- *Licensing issues*

MR. A. GREIG WOODRING: James Sweeney, executive vice president of Munich Re, will talk about reinsurance in Europe. Richard Wang, managing director of international reinsurance for Transamerica, will talk about the Asian market. Peter Bondy, senior vice president, Spain/Portugal/Latin American division of RGA, will talk about South America. Kathryn Hyland, vice president of operations, New York Life Worldwide Bermuda Limited, will talk about a U.S. company expanding to foreign markets and the considerations and approaches that come into play in that process.

I am from RGA and I am the moderator of this discussion. I will admit that I had almost nothing to do with the organization of this session—the credit for that should go to Paul Schuster. Our first speaker will be Jim Sweeney of Munich American; he'll talk about the European market.

MR. JAMES L. SWEENEY: I'm going to keep my comments rather short because I think that when we talk about worldwide reinsurance, other marketplaces are much more appealing to North Americans than those in Europe. It's an old marketplace, and companies have been well established for a long period of time.

However, it's hard to talk about reinsurance in any marketplace without at least covering briefly the direct marketplace. There are 29 countries that I counted in Europe. There may be fewer or more, depending on how many countries you count in the breakup of the Soviet Union and Yugoslavia. The marketplace in its entirety is just about equivalent to that in North America. I think Mr. Wang's comments later will, of course, correspond to these. The life premiums are approximately $250 billion (U.S. dollars). The premium per capita, however, in Europe is slightly less than what we see in North America.

We really see in Europe two different Europes. Western Europe is where the predominance of life business is—a mature market. The population is aging. The population is similar to that of North America's. It has lost some sense of faith in the federal government to provide all social needs, so we expect even that mature market to be a growth market. The eastern market is just emerging. The companies there have dealt with Communism for a number of years, and the business of insurance is somewhat new.

What we've seen in Europe is that there are different products for each of those countries, many of them old countries. The U.K. is highlighted by the single-premium marketplace. Much of it is unit-linked, similar to our variable products. In France, the big growth is in open groups and bank assurance business, whereas Germany issues mostly endowments. Those are the three largest marketplaces. Other countries' products fall in between.

In 1994 there was a third life directive, which was issued by the European community, that in theory opens up the European market. A licensed insurance company in one European market or country is eligible to write anywhere in Europe. However, that has not been fully implemented. Many factors regarding restrictions, legal environments, and taxes must still be worked out.

According to the statistics that I have received, Europe is the fastest growing in terms of real premium dollars in the world. The percentage growth between 1992 and 1993 was slightly better than 10%; North America's growth was 7.4%, about the world average, and Asia followed at 5.5%. Some of these figures are misleading. You have to convert numerous currencies to U.S. dollars, and that may have an effect.

However, within Europe, the fastest growing areas are France with the bankassurance, and Austria, Ireland, and Denmark. The U.K. marketplace is now suffering because of a consolidation of life companies, similar to what we see here in North America, and the disclosure of commissions that has been now required.

I will give a brief overview of the life premium in Europe by country. I've converted these to U.S. dollars. The U.K. is the largest at $71,263 billion; France is next at $57,252 billion; Germany is at $45,898 billion. The Netherlands at $13,731 billion and Switzerland at $12,817 billion comes next. Eastern Europe has a very small share. We could only uncover a little more than $1.5 billion. Some of the eastern European countries have premium income that is actually less than most of the companies in the more established countries.

Because the reinsurance marketplace has to necessarily follow the direct marketplace, the products we offer as reinsurers follow those in the services. I wanted to briefly touch on the direct marketplace but spend most of the time on the reinsurance marketplace. So although the direct marketplace is just about to North America, we find that the reinsurance marketplace is much smaller. I cannot fully explain that, but there are a number of very large direct writing companies in Europe, and the market is very well established there. Also, perhaps the average size of policies written, particularly endowments and things, are much lower than here in the U.S.

Like North America, there are many established reinsurers. Some of the world's oldest and largest reinsurance companies have their home offices in Europe. I found in asking questions that even within Europe the reinsurance practices vary. The sales forces and how reinsurers reach their customers vary in the marketplace. The reinsurance coverages offered also vary. Pricing and the treaty terms also vary from country to country within Europe.

Table 1 shows best guess of the size of the reinsurance marketplace by country. One country that's missing here is the U.K. I did not get its total premiums. This is total ceded gross premiums, before commissions. We can see that the largest market in Europe for reinsurance is Germany with about $3.7 billion in reinsurance premium. France follows with about $1.8 billion.

TABLE 1
SIZE OF REINSURANCE MARKET
1993 CEDED GROSS PREMIUMS IN $US MILLIONS

Country	Premiums
France	1,844
Germany	3,758
Spain	198
Switzerland	350
Netherlands	1,250
Italy	267
U.S.	17,300

Source: Munich Re & A.M. Best's.

The Netherlands, although it was fifth in the size in the direct marketplace, would be third at $1.2 billion, if the U.K. is excluded. The Italian market is remarkably small here. We have excluded inter-Italian company transactions. This is what would be "available" to a professional reinsurer out of that marketplace.

As I mentioned before, there are a number of established European reinsurers—Munich Re, Swiss Re, Mercantile & General (M&G), Scor Group, Frankona Re, Employers, Skandia, Gerling Global, Hannover Re, Union Re, Unione Italiana, Aachen Re, Bavarian Re, and Worldwide. These are just a few and you'll recognize most of those names. They're almost as familiar here in North America as they are in Europe. These companies have life reinsurance premiums in excess of $1–2 billion.

Reinsurers in Europe have been international since the 1960s. The direct market is just now getting there and reinsurers often compete on services, as they do in North America. Typical services a reinsurer is expected to offer include: publications, seminars, expert underwriting system, actuarial services, underwriting assessment and a manual, and claims and administration support. That list would probably look familiar to anybody dealing with reinsurance in North America. Expert underwriting systems are beginning to be sold in Europe now. I get many calls here about how we handle things actuarially as products are being developed there.

I want to contrast the U.K. reinsurance marketplace, which is most like North America, with that here in North America and with the German marketplace so that you get a little flavor of how reinsurance is conducted. The reinsurers generally have actuaries or other technical people as their sales force. The buyers of insurance typically are actuaries and other technical people as well. That should be a very common practice for those here in North America. Often, committees are chosen to make the actual reinsurance decision at the ceding company. Again, that's a very common approach to what we see here. There is severe price competition. Anybody here who works in a reinsurance marketplace has heard that kind of concern, and it's a similar one echoed in the U.K.

Some things are different. Experience rating is very common. You see that both YRT and coinsurance contracts typically have an experience rating provision that result in a sharing of profits with the ceding company. Self-administration is the norm. As I mentioned, in the U.K. companies coinsure the single-premium business.

In examining the reinsurance treaties, the currency is specified. U.K. direct companies operate, particularly in Ireland, and you'll see reinsurance premiums specified in British pounds or pounds sterling or Irish pounds. One of the unusual things that you will see in a reinsurance treaty in the U.K. is that the treaty requires that you must submit your facultative business to your automatic. You are then bound by the decision of your reinsurer, unless the reinsurer has declined the case and then you can submit it facultatively to another carrier.

It's unusual to find anywhere on the European continent a recapture provision. However, errors and omissions and arbitration clauses are typically found in the U.K. The set-off provision allows a ceding company and a reinsurer to set off amounts due one another, premiums due versus claims. Even though it's in British common law, it's not in any of the British reinsurance treaties that I've seen.

Typically, like in North America, product development is quick, and reinsurers have to give quotes on quick turnaround time. There is a surplus strain on the new business written, and the reinsurers are expected to participate in that strain. Pricing is based upon insurance mortality. Reinsurers will use ceding companies' experience often, when it's provided. They do make variations from company to company in the reinsurance pricing. Again, it's a competitive marketplace and this contrasts dramatically with how it's done in Germany.

Smoker/nonsmoker products are part of the landscape in the U.K., and reinsurance is done on a smoker or nonsmoker basis. The expected assets earning rate of the reinsured assets is used in pricing. When I contrast that to how it's done in Germany, although it may sound very familiar to those operating here in North America, it's a little different in Germany.

Services are very important in the German marketplace. Often, in Germany, direct writing companies offer both property and casualty, as well as life business. They want one reinsurer to take some of the very difficult property and casualty covers, and the life business will be given as a sweetener to the pot. There's a certain mind-set that reinsurers are long-term partners in the business and they discuss more general business topics and themes than individual quotes.

That leads me to the reinsurance sales representatives or generally to senior management executive-level types, where the reinsurance is bought and sold. At our company, it's at the managing director level—two senior levels within the company. The buyers tend to be at the same level. They agree in principle, and then the details are left to the professionals. (That doesn't mean senior managers are not professional, but that only unless there's a large dispute will they go back to senior management.)

As we've seen in the U.K. market, experience refunds in the German market are very common and will cover up much of the pricing conservatism that I'll show you in a few minutes. Modified coinsurance is the most common form of reinsurance in Germany. The product that is issued is mostly an endowment type of coverage and modified coinsurance fits well there. Also, by law, it has to be participating business, with 90% of the profits going back to the policyholders. In practice, it's a much higher percentage. That's where the German insurers compete. Again, like North America and the U.K., the business is done on a self-administered basis.

The pricing in Germany uses population mortality for direct business, and reinsurance is done on the same basis. The valuation interest rate, instead of the actual asset earnings rate, is used in the calculations. It is also used in the experience refund calculations that I've seen on modified coinsurance. The interest rate on the modified coinsurance reserves is also the valuation interest rate, for which the latest rate I had is 3.5%.

Even though the direct business has to be participating, reinsurance on modified coinsurance does not reimburse the dividends. That would be clearly illegal here in the state of New York. However, again, the experienced refund formulas tend to help reimburse the company indirectly for its dividends. The business is not smoker-distinct because it's based on the population mortality.

The German reinsurance treaties have the same type of provisions, although wording is slightly different. The facultative must be sent to the automatic, and the automatic company is bound by it. There's no recapture provision. The currency is specified in the treaty. An interesting AIDS clause is in the typical German treaty and says that if the ceding company makes changes on in-force policies, whether it be premiums or dividend scales, because of deteriorating experience, the reinsurer must share in that change or all reinsurance can be terminated. It's a very interesting difference that you see between Germany and North America; the U.K. is silent on that issue.

Also what's very unusual, at least for those operating in North America is upon termination, it allows the reinsurer to terminate all business that's in force, as well as new business, in case of the insolvency of the ceding company. Also, if the ceding company has a change in ownership or if it's merged to another company, the reinsurer has the right to get off the risk entirely. Again, state regulators here would love that kind of provision on reinsurance treaties.

I hope this gives a little flavor of how reinsurance is done in Europe. In many ways it's very similar to what we do here in the states, and in many ways it's quite different. Most companies here do not view Europe as an attractive place for setting up offshore or expanding operations because it's been a solid marketplace for a long time.

MR. WOODRING: Next we'll hear from Richard Wang about the Asian market.

MR. RICHARD T. WANG: I'm glad to have this opportunity to participate in this panel discussion and to share with you my experiences in the Asian market.

I believe the Asian market currently is the most dynamic and exciting marketplace in the world. Although Transamerica Reinsurance is the leading life reinsurer in the U.S., our international operations started just about three years ago and so we are relatively young in the international market. Our key emphasis is in Asia and in the Latin American market, to a lesser degree we are in the European market. Currently, all our business is conducted out of our Charlotte home office, but we will set up a customer service center in Asia by the end of this year.

In my presentation, I would like to share with you from my own experience an overview of insurance and the reinsurance market in Asia. Because reinsurance is the second tier of the insurance transaction, and the reinsurance industry tends to react to both conditions and movements of the direct insurance market, I therefore will address the direct insurance market first and then lead into the reinsurance environment in the region.

I would like to start with a quote from Robert Rubin, Treasurer/Secretary and a former National Economic Council director. He once said, "Asia will probably be the most dynamic part of the world in the decades ahead, and we want to be there." Indeed, the surging financial power of Asia in the last decade has been creating new markets, industries, cities, and individual wealth. To put it simply, it has changed the world.

The combination of its vast population and economic boom has produced tremendous business opportunities for the life insurance industry and thus reinsurance. In recent years, the life insurance market in Asia, with only the exception of Japan, has been experiencing double-digit growth rates between 18% and 30% annually. The licensing of the American International Group (AIG) in China in 1992 further magnified the business potential for this region. With a population of 1.2 billion, China has expanded the market size for this region by almost threefold.

Moreover, the recent normalization of diplomatic relationships between the U.S. and Vietnam and the pending privatization of the insurance market in India will significantly amplify the life insurance market in this region to a greater degree. This emerging free market environment is particularly appealing for U.S. companies. An open market atmosphere promotes competition and creates a demand for advanced knowledge and technology in underwriting, product design, market strategies, and information management systems.

Now, let's take a closer look at this market. I also included Japan and India, but both areas will be just sort of mentioned in the map. Most of my discussion actually will cover mainly the emerging market section. Basically, based on the socioeconomic structure of the country, I divided the Asian market into five different groups. Japan, by itself, is the most advanced industrial country, and so the market is by itself; it stands alone.

The next tier market is the so-called new industrialist countries: South Korea, Taiwan, Hong Kong, and Singapore, also called the Four Dragons. The next is the so-called Four Tigers, mainly the Asian countries of Thailand, Malaysia, Indonesia, and the Philippines. China and Vietnam are the so-called totalitarian regimes. They are the newcomers for the marketplace, and the potential is justified by the population and future economic growth. They will generate a substantial business for the future. India, with 900 million people and an economy that is doing well, will again provide further market expansion for the western insurance companies.

The advanced industrial country is Japan. The new industrial countries are Taiwan, Hong Kong, Korea, and Singapore. Developing countries include Malaysia, Indonesia, Thailand, and the Phillippines. China and Vietnam are the totalitarian regimes. The nationalized market covers both India and Pakistan. I understand Pakistan will open up for private sectors in the Asian market, but I hear there are not too many takers yet. I think the problem with China and Vietnam is that policy is very hard to predict because of the Communist regime. I think some of you probably share the same feelings regarding getting a license to do business in China.

As we indicated earlier, the life reinsurance market in Asia, with only the exception of Japan, has been experiencing tremendous growth in recent years. Let's look at some of the statistics that I collected based on different publications. Table 2 shows the three emerging markets in the world—Africa, Asia, and Latin America. The purpose is to show you the magnitude of the Asian market and the premium size in comparison with the two other markets. The statistics are perhaps slightly out of date, but I think the size of the Asian market is clearly illustrated.

TABLE 2
LIFE PREMIUMS IN EMERGING MARKETS

	1989		1991		1989–91
	Premium	Percentage of World Share	Premium	Percentage of World Share	Percentage of Increase
Africa	$ 614	0.09%	$ 651	0.09%	6.03%
Asia	11,730	1.84	15,649	2.11	33.41
Latin America	1,716	0.27	3,233	0.43	88.40
Total	$ 14,060	2.20	$ 19,533	2.63	38.93
United States	$244,454	38.25%	$263,791	35.52%	7.91%

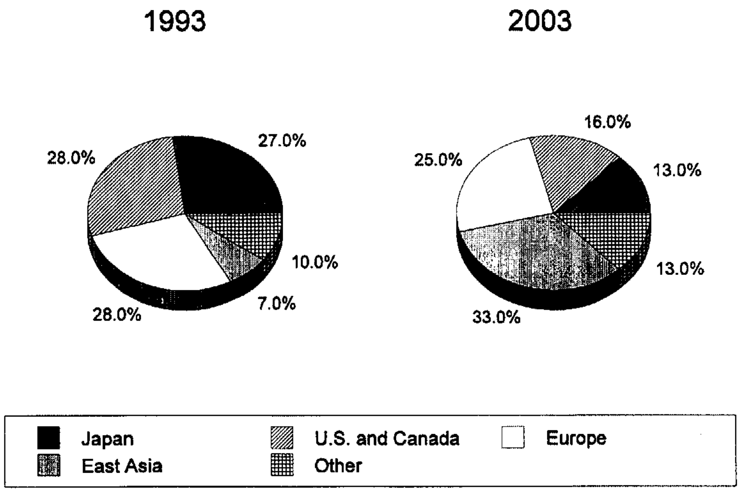
Table 3 shows some 1993 key statistics related to most of the countries in Asia. (China is based on the 1992 number.) This will give you an idea of the population, the gross domestic product (GDP) in U.S. dollar terms, and the number of life insurance companies in each country. I want to point out that Taiwan and Indonesia have the fastest growth of companies. Before 1987, there were only eight life insurance companies in Taiwan and there were about the same number in Indonesia. By 1993 there were 30 life insurance companies in Taiwan, and I think, as of today, 49 or maybe many more new companies are forming in Indonesia. You can see they are still relatively small premium-wise in comparison with Japan and the U.S. Again, that is a 1993 number, of course, but any production would show a substantial growth performance there. Also, as a percentage of GDP, they are relatively smaller in comparison with Japan and the U.S. Korea may have the highest per-capita premium among all the emerging markets there, only because most companies in the Korean market are in pension/savings types of businesses and so they have a high-premium product. But in the other countries the premiums are relatively small.

Chart 1 shows the projected growth of the distribution of life premiums in different parts of the world. You can see that for the east Asian market in 1993, the life premium is about 7% of the total. That's based on about $900 billion of premium. The ten years of growth will push the Far East or east Asian market share to 33%, so you can see the growth. That's 250% of growth over the ten-year period.

TABLE 3
FAR EAST MARKET
KEY LIFE INSURANCE STATISTICS (1993)

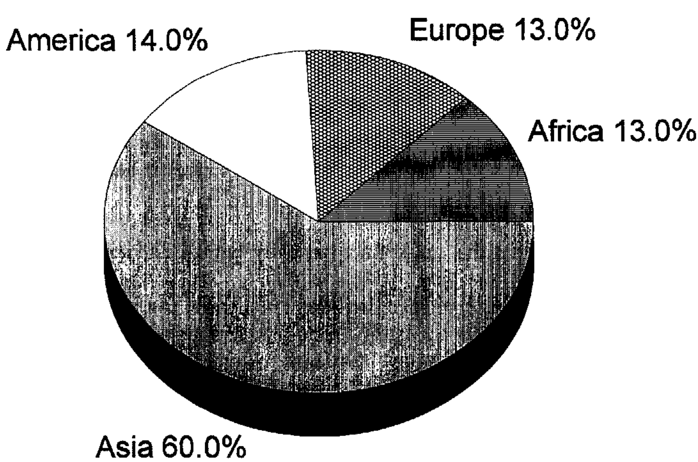
Country	Population (MM)	GDP (US$ MM)	Number of Companies	Premium (US $MM)	Percentage Over 1992	Percentage GDP	Per Capita (US$)
China*(1992)	1,205.0	$ 658,000	4	$ 1,031	71%	0.16%	$ 1
Korea	44.1	329,250	30	31,237	6	9.49	708
Singapore	2.9	60,130	14	1,380	21	2.30	475
Hong Kong	5.7	94,690	63	1,400	56	1.48	246
Taiwan	20.9	220,100	30	8,938	17	4.06	427
Indonesia	188.2	121,467	49	489	52	0.40	3
Malaysia	19.1	59,700	18	1,180	21	1.98	62
Phillippines	65.0	49,344	26	338	19	0.69	5
Thailand	57.8	109,000	12	1,382	18	1.26	24
India (estimated)	879.5	245,277	1	2,693	66	1.10	3
Total	2,488.2	$1,946,958	247	$ 50,068	n/a	2.37%	$ 20
Japan	124.5	4,292,929	30	294,000	3	6.85	2,361
United States	235.0	$6,200,000	1,840	$319,551	13	5.15%	$1,360

CHART 1
WORLD LIFE PREMIUMS



We have seen all these impressive statistics. Let's look at what makes the life insurance industry in Asia grow (Chart 2). Currently, Asia has about 60% of the world population, and it will have about two-thirds by the year 2000; that's current. The 1993 statistics show about 60% of the population in Asia, and that's including Japan, India, and all Asian countries.

CHART 2
WORLD POPULATION DISTRIBUTION 1993
TOTAL POPULATION: 5.7 BILLION



Since the 1960s, Asia has emerged as one of the world's most lucrative marketplaces. The average GNP growth rate has been approximately three times that of the U.S. Table 4 was published by the International Monetary Fund. It shows that in the 1970s, 1980s, and also into the 1990s, the so-called east Asian emerging market had an average between 6% and 8% or 9% of growth rates. The combined world growth rate is only 2.5–3.6%, so you can see the magnitude of the growth in this region.

TABLE 4
FAR EAST MARKETS ECONOMIC OUTLOOK

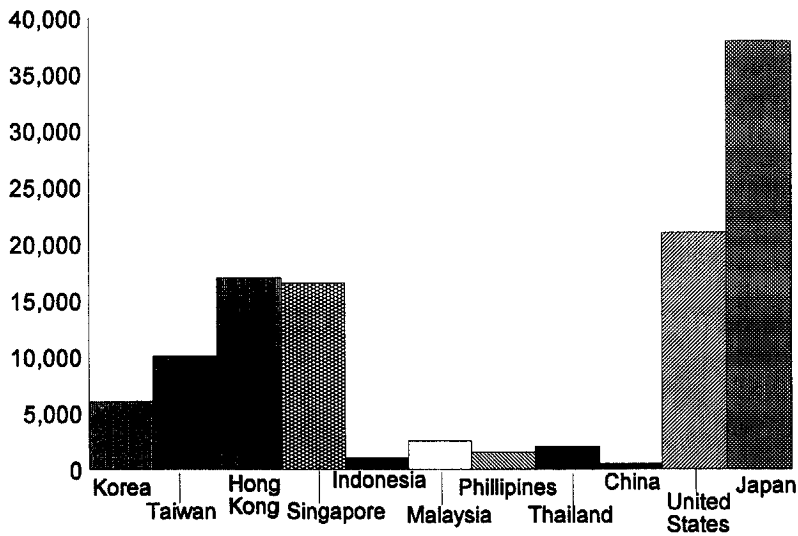
	1970s (Percentage)	1980s (Percentage)	1990s (Percentage) Projected
Korea	7.70	9.60	7.10
Taiwan	9.70	8.00	6.50
Hong Kong	9.30	6.70	5.50
Singapore	9.10	7.10	5.80
	8.70	8.50	6.60
Indonesia	8.00	5.50	6.30
Malaysia	7.80	5.90	6.90
Phillippines	6.30	1.80	3.60
Thailand	6.80	7.70	7.40
	7.30	5.80	6.30
China	5.80	8.90	8.50
Combined	7.50	8.00	7.20
World	3.60	2.80	2.50

Source: Data from IMF "International Financial Statistics"

Because Asia is considered to be the emerging market, the per-capita income in each country is actually relatively small in comparison with that of the U.S. (Chart 3). There's still room for growth. The last one, Japan, was almost at about $35,000 per-capita income in 1993. The U.S. was at about $22,000–23,000 per capita. China is really small and it will take many years for the China market to become materially significant.

The other factors that affect this market are basically typical characteristics of a new marketplace. Most of the emerging markets in Asia are still in the infancy stage. Because of the lack of social insurance facilities, the people use insurance products to support and to supplement their needs for medical coverages and pension coverages. Asian people tend to save more money. Basically, they don't like to spend too much above their means, so there is the potential, again, of additional savings for life products as a savings or investment vehicle.

CHART 3
GNP PER CAPITA-1993
PER US$



In addition, during the last several years the economic policies of most of the Asian countries have encouraged foreign investments either through sole ownership or through joint venture with local business partners. That's another reason for the surge in the growth of the life insurance market. Some other factors also affect or stimulate the growth of the market. The U.S. treaty conditions that are put on, say, Korea and Taiwan, force both countries to open up the insurance market for U.S. companies. I think that happened somewhere in the late 1980s. Also, the recent development of the General Agreement on Tariffs and Trade (GATT) will further increase the accessibility of the local insurance market in the Pacific rim.

As a result, many western insurance companies have established their presence in the marketplace and have brought with them new product ideas and technologies. Above all, western companies have induced the open market competition concept. All these factors have contributed to the growth of the life insurance industry in Asia. During the last few years, the average growth rates have been approximately 25% a year.

Let's now take a look at some basic characteristics of the Asian market. They are young and small. The products are mainly the traditional products. During the last decade, the insurance products in the region remain relatively the same—traditional whole life. Endowment is extremely popular, and term insurance is getting some momentum. The saving elements of a product continue to outweigh the protection elements. Wraparound products are very popular in the region. The wraparound product means it's a main policy and different types of riders, including medical disability income writers, that will be used and attached to the base policy. That's very common in the marketplace.

In recent years, due to the risks associated with inflation and currency exchange, dollar-denominated products are becoming more acceptable. In Indonesia and Hong Kong you can sell dollar-denominated policies. New product ideas also start to migrate from Europe and South Africa into this region. The European reinsurance companies brought those ideas into the marketplace. One product that's getting extremely popular is the dread disease life insurance product, which is selling very well in Singapore, Malaysia, and Taiwan.

We have had a look at the direct insurance market. I want to go over some basic issues related to the reinsurance market. I believe that the evolution of the open market environment in this region creates a demand for insurers seeking reinsurance partners that have both the financial strength and the ability to provide new technologies in underwriting risk management, product design, and software systems. This market will be more receptive to a reinsurer that is both open and innovative.

The key characteristic of this market is that for reinsurance, the ceding company tends to put more emphasis on long-term relationships over price, but there are differences here because so many new companies have surfaced. A new company tends to put more emphasis on price, but local companies dominate the market. They tend to put more emphasis on long-term relationships. Price seems to be secondary to them. They like to see the services and new ideas from the insurance company. The only way local companies can gain access to the western knowledge and technology is through reinsurance. So they treasure that more than the price they receive from the reinsurer.

Most of the reinsurance products available in the marketplace currently are risk premium or what we call YRT reinsurance. Most treaties tend to have the experience refund features. I think in the U.S. today we have straight YRT without experience refund. The coinsurance concept is very foreign in Asia, I think mainly because the market is relatively young. Also, most of the local companies have sufficient financial strength and don't look at coinsurance. They consider coinsurance as showing a weakness of their financial stability.

The regulatory environment also discourages using coinsurance as leverage for sustaining a company's growth. Most of the regulators I visited tend to believe that a company should only write as much business as its capital can support. Using reinsurance to leverage is usually discouraged, but there is no rule that says you cannot do financial reinsurance. So that's something that may change in the future.

The basic reinsurance services that most ceding companies are seeking are still the typical ones. The facultative underwriting probably is the most welcome one. The product design, again, is another service that a reinsurer can provide to the ceding company, especially with the new western joint venture or branch operations in the region. They brought in the U.S. product concept or European product concept that the local companies are really seeking for support or help in product design.

Also, most of the companies, especially local companies, are weak in their administrative systems. They are seeking new ideas as to how to improve both their direct administrative system and their reinsurance administrative support. Some of the European companies will offer this for free, I think, in return for the business. That's another way of offering more value-added services to the ceding company.

Let me just address some key risks associated with doing reinsurance internationally, or in Asia, but I think this applies to all international operations. The political risk is more prominent in Asia, especially in China and in Vietnam. In those Communist regimes, you have no idea when the policy will change overnight. A country such as Indonesia, again, is still controlled by some top-level people. If the current president, Saharto, retires, or a new president comes in, the policy may change.

The squabble between Taiwan and China has created many concerns among the foreign investors and also among local people. Another risk is economic. Granted, we show a substantial and impressive growth in this region but, again, Japan shows tremendous growth in the early years, but it's all bubble economy and sometimes it may burst. I think the additional investment from the western countries into the region is very important to support the healthy growth of the economy in the region.

There is a great deal of potential for growth in China, and it's a promising market for many industries. But if you really dig into the ground for the root of the whole structure, there may be problems in China because the government would lose control of this growth.

The third risk is currency risk. As an actuary, I believe the foreign exchange perhaps is one of the most difficult risks to manage. Most companies either sell a foreign fund in each country or just convert everything into U.S. currency. There are pros and cons of how to handle the currency risk by taking either approach.

Some of the issues associated with the reinsurance industry in this region are regulatory. I think regulatory issues are less significant to reinsurers. Most of the regulators tend to be very friendly with the reinsurer. There are really not many rules or regulations that try to restrict reinsurance activities. I think Singapore may have the tightest rules, and it prefers you sell through a branch or subsidiaries to do reinsurance in the country. I met with the commissioner, Ms. Linn, before and she said that as long as you have the intention to establish a branch office, you can still do business, conduct reinsurance, or try to promote the reinsurance business in Singapore.

Basically, the countries in this region tend to be a lot more lenient to the reinsurance operation than to the direct company. The direct company must get a license to do business or establish either a branch or a subsidiary in the country. Taxation really is not an issue to a reinsurer, because currently all of Transamerica's transactions are done out of the U.S. It's not really a local company, so we're not subject to the local taxation, with the exception that we have to pay an excise tax or business tax of 1%.

As I pointed out, with the exception of Singapore, most of the countries do not require you to set up a branch. Actually, some of the commissioners encourage you to set up as an office. As long as you don't conduct the business transaction locally, I think that's OK. Most of the reinsurance companies doing business in Asia basically follow the same route.

The aspect of the reinsurance industry in the region is financial reinsurance. I believe that there's a need for financial reinsurance because of the new companies and the growth of the market. Current financial strength would not be able to sustain future growth. Financial reinsurance should play a major role in helping the market to grow. I think the main obstacle is how to convince the regulators to have financial reinsurance.

One talks about more full risk transfer type of coinsurance or a modified coinsurance structure that is acceptable for the insurance industry. The other one is new technologies. As I pointed out before, the market becomes a very competitive open market and more policies with large face amounts are being issued. The new technologies, such as advanced underwriting and financial underwriting, are really needed in the region.

The other thing is also reacting to how the direct insurance market meet its needs. Because of the open market environment and the increasing competitiveness in the marketplace, many insurance companies try to establish a different distribution system. The majority of business is sold through the career agency system, and brokerage or general agent (GA) systems are really not as popular. I think that's definitely a demand for new ideas of how to distribute insurance products and that's what reinsurance can help do.

The last item that I consider to be of significant value for the future growth of the market is to provide investment and asset management services to the ceding company. With the growth, many countries are offering annuities and privatizing the social security system. I think all that requires the concept of how to do asset/liability matching, which is currently foreign to many local companies.

Here are the key professional reinsurers in the Asian market:

European
- Cologne Re
- Hannover Re of Germany
- Mercantile & General
- Munich Re
- Skandia International
- Swiss Re

North American
- Employers Re
- Lincoln National
- Manulife
- RGA
- Transamerica

Japanese
- Daich
- Kyoei
- Meiji

Europeans have been there for a long time, especially Swiss Re and Munich Re. They've been in the Asian market for decades. Cologne Re is a strong player in the current marketplace, but I think it has been there perhaps less than ten years. It's a relative newcomer as a European. After Hannover Re purchases the NRG Victory Australia operation, it may become a key player in the region. M&G set up an office in Singapore and I think one in Hong Kong and, again, it has become very active in the marketplace.

The Japanese reinsurers used to be active mainly in Taiwan and in Indonesia, but in recent years they've become relatively invisible. I think the reason may be because the business mentality is very conservative and not very flexible and really doesn't fit into this current open market environment. They don't want to change. Usually they say, these are my terms—take it or leave it. Unfortunately, many companies now leave it rather than take it.

I think Lincoln National has been in the marketplace for a long time, maybe the longest among other North American players. It has an office in the Philippines and is also active in some other countries there. The newcomers are the rest of those on the list. Employers Re, after the purchase of Victory Re of U.K., has a sizeable existent business from the Victory. Manulife also set up an office about three years ago in Singapore. It has been active mainly in the southeast Asia market. RGA is probably the newest player in the marketplace. It has offices in Japan, Tokyo, and in Hong Kong. I think Transamerica is the only reinsurer doing business in Asia without a local presence. Again, like I said before, perhaps in two months we will have a local presence.

To compete in this market, reinsurers must offer a full line of reinsurance coverages, including life, accident and health, disability income, and catastrophe coverages. It seems that North American companies tend to separate life and nonlife, but most of the Europeans offer composite coverages. Many insurance companies in Asia are composite, which means they do both life and nonlife. I think there is a certain advantage for the European reinsurers currently dealing with the composite companies, because they provide both coverages.

In addition, due to the rapid growth and increasing open competitive market, services such as product development, advanced underwriting, and systems support have come greatly in demand. So the value-added services through those three areas can be very helpful for a reinsurer to establish its position in the marketplace. The new opportunities and promising developments continue to surface in east Asia, but the market continues to evolve and will take many years to reach maturity.

For a reinsurer to do business or to be successful in the marketplace, it must carry a very long-term commitment before deciding to move into this market. More importantly, we need to work very closely with both the insurance industry and the regulator to direct these opportunities into a healthy growth for the insurance industry and also improve the profitability for the business for both the ceding company and the reinsurer.

MR. WOODRING: Pete Bondy will talk about South America.

MR. PETER J. BONDY: It's certainly a pleasure to be here. I came to this country 33 years ago from Ecuador to become an actuary. I wound up staying, so it certainly is a pleasure to be back working in Latin America. Spanish is my first language.

Concerning focus on Latin America and RGA, it's in Latin America today because domestic and Canadian growth opportunities were leveling off. It searched for other areas, Latin America, the Far East, and eastern Europe. We set up a division in Latin America in the area that I'm involved. We now operate in seven countries, including

Argentina, Chile, and Mexico; others will follow shortly. We operate there with a long-term commitment. I think the most important part is what I would call the mental block and the perception about Latin America. I will speak quite a bit about that and then come back to the insurance industry and reinsurance. We view Latin America as being unstable, as a place with many risks, and as probably being a place that we cannot trust. I agree on the first one, to some extent; I agree on the second one; and I disagree on the third one.

The map on Chart 4 does not show Mexico. That falls within the division. Some people would classify it as North America. The map is called Central and South America. The countries of opportunity right now would be Mexico, Brazil, Argentina, and Chile to a great extent. To some lesser extent, people will talk about Bolivia, Peru, and Colombia. Then there are countries such as Panama, Ecuador, Costa Rica, and El Salvador. Costa Rica is in the process of undoing its monopoly. Then there is Paraguay and Uruguay, which is a smaller country in the process of undoing its monopoly. Venezuela will become a country of opportunity, but it needs to resolve certain issues.

CHART 4
CENTRAL AND SOUTH AMERICA

What is Latin America all about? Let's look at the population (Table 5). It's population is about twice that of the U.S.—432 million versus 258 million as of 1993. Argentina has 34 million, Brazil has 159 million, Colombia has 36 million, Mexico has 91 million, and Chile has 14 million. The growth rate, however, is an important factor here; it's 2% for the continent versus 1% for the U.S. The age pyramid shows a much younger age for the population.

TABLE 5
THE REGION—POPULATION
FIGURES IN MILLIONS

	1989	1991	1993	Four-Year Compound Annual Growth Rate
Argentina	31.93	32.70	34.00	1.6%
Bolivia	5.69	6.13	6.56	3.6
Brazil	147.40	153.30	158.98	1.9
Chile	12.96	13.39	13.81	1.6
Colombia	32.95	33.60	35.89	2.6
Ecuador	10.49	10.85	11.47	2.3
El Salvador	5.10	5.38	5.50	1.9
Guatemala	8.94	9.45	10.03	2.9
Honduras	4.60	4.92	5.25	3.3
Mexico	84.49	87.84	91.45	2.0
Panama	2.37	2.47	2.56	2.0
Paraguay	4.16	4.45	4.80	3.6
Peru	21.79	22.30	23.15	1.5
Dominican R.	6.90	7.31	7.65	2.6
Venezuela	18.00	19.79	21.24	4.2
Total	397.77	413.88	432.34	2.1%
USA	247.35	252.50	258.00	1.1%
Ratio LA/(USA+LA)	61.7%	62.1%	62.6%	

Certainly they have much lower income levels than we do, but the growth in the GNP is very impressive (Table 6). You can see the growth in Argentina's, Bolivia's, and Brazil's GNP. Chile has a 12.6% compound rate per year. The continent shows 7.3%. The U.S. shows 5.3% during the last four years. It's probably an accelerating growth rate as countries such as Ecuador, Columbia, and Bolivia go through certain processes and the situation improves there.

With regard to history, the 1950s, 1960s, and 1970s were unstable. Governments, while preferring democracy, had barriers impeding capitalism and private enterprise. I came to this country in 1962 and I can tell you that I've seen tear gas and quasi-revolutions right around where I lived in the 1950s. Some of what was seen in the 1950-1960s continued into the late 1970s, 1980s, and 1990s. But we started seeing more fiscal responsibility, government modernization, probusiness legislation, and free enterprise, to the point where now we have, in fact, almost free trade coming about in Latin America.

One of the first ones was the Andean Pact with Bolivia, Colombia, Ecuador, and Peru. There is the North American Free Trade Agreement (NAFTA) with Canada, the U.S., and Mexico. Chile will be the next partner; others will follow. A privileged country is something that is not well known. That is basically the opportunity for Latin American countries to export to the U.S. country without customs duties on certain items that are manufactured within the country with raw material from the country in many cases.

TABLE 6
THE REGION—GROSS NATIONAL PRODUCT
FIGURES IN US$ MILLIONS

	1989	1991	1993	Four-Year Compound Annual Growth Rate
Argentina	60,134	180,357	242,424	41.6%
Bolivia	5,497	6,067	6,450	4.1
Brazil	442,211	528,200	550,473	5.6
Chile	25,372	26,596	40,757	12.6
Colombia	39,704	43,653	55,300	8.6
Ecuador	10,117	11,354	11,986	4.3
El Salvador*	6,446	5,959	6,870	1.6
Guatemala	8,393	9,404	11,391	7.9
Honduras*	4,908	3,026	3,666	N.M.
Mexico	200,713	290,913	350,591	15.0
Panama	4,639	5,491	6,355	8.2
Paraguay	4,375	6,050	6,740	11.4
Peru	ND	25,841	26,523	N.M.
Dominican R.	6,687	7,313	7,939	4.4
Venezuela	42,833	53,882	59,832	
Total		1,204,106	1,387,299	7.3%†
USA	5,163,200	5,677,500	6,343,300	5.3%
Ratio LA/ (USA + LA)	NM	17.5%	17.9%	5.7%†

* Political unrest

† Two-year growth rate due to unavailability of 1991 date for Peru.

Mercosur includes Brazil, Argentina, Uruguay, and Paraguay. Chile was looking into entering. Then there is the Central American common market—Costa Rica, Nicaragua, Salvador, Guatemala, and Honduras. Ultimately, there's a master plan to have continent-free trade, including the U.S.

What about other developments? Education has improved. Many of the people are U.S.-educated. The business environment is much different from what it was before. People are serious, punctual, and professional. Government monopolies are being privatized. Chile is probably the most advanced in that. Argentina is proceeding. It affects most industries and brings an entrepreneurial atmosphere.

On the other side, there are very strong infrastructure needs in Latin America—telephones, utilities, and roads. They're to the point of privatizing, for example, the post office in order to improve it. A very strong demand exists for capital investment and likewise for growth.

I like to talk about the privatization of social security, what we actuaries would call the old-age, survivors, and disability insurance (OASDI) benefits. I consider this perhaps the single most important factor, outside of privatization and the education level, in bringing about growth and improvement in Latin America. At this point, Chile, Argentina, Peru, and Colombia have privatized the OASDI benefits. The schemes are somewhat different from most countries' schemes. The one that is the most private is Chile. Colombia might be the one that most combines the private and public element.

It has created an insurance industry or an insurance line of business. It has created fund management companies. It has provided investment funds. In time, it has increased the level of savings to the population and also the awareness of investment returns and the value of savings. It has reduced government spending and inefficiency.

I have an example using Chile: there is about $26 billion in the system. The system privatized 13 years ago. Remember, this country has 20 million people and a lower level of income. Approximately $1 billion annually is being transferred to insurance companies to purchase retirement annuities from the system. The annuities from the system are provided by private insurance companies. The system is investing abroad. It started out with the provision that up to 10% of their funds could be invested abroad. Now they can invest up to 30%.

Chile is known as the investor and the capitalist of Latin America today. Argentina owns much of the utility industry and many other industries as well, and it is moving into other countries. The system will continue to grow, I estimate, at about $2 billion per year.

Argentina privatized on July 15, 1994. Its system did not go as far into privatization as Chile. It still allows some participation in a public system, and the employer contributions go to the public system. Ultimately, all employee contributions will go into a private system. Sixty percent of the people who ultimately will be in are in at this point. Two categories are talked about: the undecided people or those in decision, and they are supposed to be into the private system by 1996. These are people who were not able to make a choice of a fund management company and who have not made one yet.

Also, there are a number of state retirement systems, and at some point, they probably will be privatized. Some, I think, are proceeding at this point. I estimate that about $5–6 billion is in the AFJPs (the retirement fund in Argentina) or in fund management companies. This is for a system that has just been in force for slightly over a year. At this point, no annuities have been purchased to speak of. My projection to 2000 or so, is that the assets will be in the order of $50 billion. That's in the fund management companies. Then at that point the annuity production will be in the order of $2–3 billion a year. Now this is only the annuities from the privatized social security system. Other annuities are coming in from private provisions. It will start producing investments out of the country. Argentina will be another Chile, another capitalist of Latin America.

The insurance industry has traditionally been multiline companies, very much along the lines of European companies. Historically, there were currency exchange controls. There were reinsurance monopolies. Life offshore business from U.S. carriers had significant growth. The products were antiquated. The products offered by offshore were up to date—universal life (UL), for example, term, and so forth.

High-inflation years ended the individual life insurance industry in Argentina and Brazil. In fact, in Argentina, just about all individual life policies disappeared either because they were surrendered or lapsed, or because their value had become so low that the companies were asking people to cancel their policies due to the fact that it would cost them too much to administer the collection of the premium. The offshore market grew. Technical knowledge suffered.

What about this decade? Insurance laws are being overhauled. They're being modernized. Likewise, investment laws are being modernized to provide guarantees to the foreign investors. There is growth in insurance. There is growth in life insurance. Foreign ownership is increasing and certainly has played a part in forming or providing growth for many individual life companies in Argentina, for example. Free currency exchange is available now in Argentina, Chile, and Mexico.

Reinsurance monopolies have been shut down. The monopoly in Argentina is in the process of being shut down. The Instituto de Reseguros de Brazil (Brazilian reinsurance monopoly company) is also in the process of being shut down within the next few years. Dollar policies were authorized and this, again, was to provide comfort to the buying public and also to compete with the offshore market.

Regarding percentage of total premiums in the local market, as of 1990, Argentina had about 9% life insurance, and 91% nonlife (Table 7). As of 1993, 17% was life and 83% is nonlife. As of 1995, another $400 million is coming into the life insurance market just from the insurance required by the privatization of social security, so this relationship has drastically changed. It's gone more from life to nonlife due to high inflation in Brazil. In Chile, the percentages remained about the same and in all these years the private social security scheme was in effect. You can see the percentages in other countries and compare them with the U.S. In most of these countries the nonlife market still has a bigger share of the total market as compared with the U.S. This will start changing due to the different steps that they are taking—the privatization, the leveling of inflation. As social security privatized and savings increased, I expect life insurance to increase significantly.

TABLE 7
THE REGION: LIFE VERSUS NONLIFE MARKET
PERCENTAGE OF TOTAL PREMIUMS

	1990		1993	
	Life	**NonLife**	**Life**	**NonLife**
Argentina	9%	91%	17%	83%
Brazil	12	88	4	96
Chile	60	40	56	44
Colombia	19	81	15	85
Mexico	35	65	34	66
Panama	42	58	25	75
Peru	1	99	7	93
USA	28	72	31	69

Table 8 shows the total insurance market in terms of total premiums. Argentina in 1989 was $2.7 billion. In 1993, it was $3.9 billion. The story here is the annual double-digit growth rates. In fact, this is an area where Argentina, Chile, Brazil, and I think most other countries will provide double-digit increases in growth in life premiums.

TABLE 8
THE REGION—TOTAL INSURANCE MARKET IN US $ MILLIONS

	1989	1991	1993	Four-Year Annual Compound Growth Rate
Argentina†	2,761	2,969	3,974	9.5%
Brazil	3,590	5,750	7,882	21.7
Chile*	572	928	1,406	25.2
Colombia†	702	669	1,168	13.6
Mexico	2,670	3,595	5,783	21.3
Panama	133	171	227	14.4
Peru†	286	287	287	Nil
USA	431,050	490,866	484,799	3.0

* A large portion of growth is due to single-premium immediate annuity sales to the national private pension system and health insurance premiums for the national private health system.

† These countries have, within the last year or so, privatized OASDI (all three) and a national health system (Columbia). Growth in insurance premiums will follow the trend in Chile.

Continued premium growth will be in the double digits. Living standards will improve. There's terrible underinsurance. The population growth is higher than in the U.S. In some countries, the average age might be 27, 28, or 30. Privatization programs of social security and savings rate growth all will provide for double-digit growth.

We're finding that the traditional reinsurance products are similar to the U.S. We have coinsurance, but it's called *quota share*. *Coinsurance* means something different in Latin America. It means that you, as a reinsurer, publicly owe the paper to the policyholder. YRT, excess of loss, and catastrophe covers are found. Lesser known products at this point would be financial reinsurance and modified coinsurance. For privatization of social security, the first year was handled via quota share or excess of loss, stop loss, and catastrophe. In renewal years, it is becoming more a stop-loss and catastrophe coverage. Nontraditional reinsurance products include technological assistance and exchange for reinsurance, products, systems, and other.

There are some differences. I find that pricing is more conservative. Exceptions do exist. There is more conservative underwriting for health and activities. Terms are somewhat more restricted. The local policies will include more exclusions, and reinsurance will follow them. There are lower retention limits and there are lower autobinding limits in most cases.

There is the casualty company mentality. Again, companies have operated on a multiline basis. The types of risks that are ceded facultatively, often, are short-term, odd benefit pattern risks. In many cases, the treaties are cancelable by the ceding company every year. When I say cancelable, this may include the in-force reinsurance ceded. Most treaties are experience-rated.

There are similarities. There are smoker and nonsmoker rates such as we have here. In Argentina, for example, there's another question. Smoker or nonsmoker rates are being offered, but a nicotine test is not widely available. I would not consider it to be as aggressive at smoker/nonsmoker rates as is this country. Most U.S. treaty conditions or provisions are accepted. There are dollar transactions in the sense that you may write the reinsurance in the local currency, but you will be paid in dollars. The products reinsured are similar—UL, term, group life, dread disease. They want to adopt U.S. standards for underwriting, pricing, administration. There's keen interest in being taught and being helped on that issue.

We face political risk. It varies by country, but I believe it to be stabilizing. Local laws are not an issue with stabilization of economies. Reinsurance follows the currency of the underlying contract. It varies by type of treaty used, by coinsurance versus YRT. The Chile peso is appreciating, the Argentina/Brazil currency is stable, and others are devaluating at slow speed.

Taxes are an issue I don't think we should discount. We compete with European reinsurers but they do not have items such as a deferred acquisition cost (DAC) tax. We have a foreign income tax in Argentina and a foreign excise tax in Chile. There is potential nonrecognition of foreign standards. Licensing requirements are not a burden. They require patience.

MR. WOODRING: Finally, we'll hear from Kathryn Hyland. Speaking as a reinsurer, RGA is expanding internationally. Some of the same considerations that Kathryn will talk about that a direct writer goes through are the exact same things we think about when a reinsurer expands internationally.

MS. KATHRYN A. HYLAND: I'm going to give you the direct writer's perspective. I'd like to talk about what prompts U.S. or Canadian companies to go abroad. This will be from the perspective of New York Life, which, of course, is 150 years old, the third largest company in the U.S. New York Life, through its worldwide operation, has operated about eight years in diversifying globally and currently operates in eight countries—Argentina, Bermuda, Hong Kong, Indonesia, Korea, Mexico, Taiwan, and the U.K.

These words will take the point of view of a U.S. company. The message basically is to be bold. Many U.S. and Canadian companies have tried going the other way. That really doesn't work in this market. Generally speaking, the point of view of the U.S. and Canadian companies moving abroad is one of being very conservative. These countries generally are quite stable. They're looking at using tried and true methods. They're quite domestic-oriented and their decisions are very steadied, so the perspective of U.S. companies in global expansion tends to be looking at foreign operations as an investment—putting a toe into the water very cautiously. By contrast, European insurers operating abroad tend to be more globally oriented and tend to be more diversified in this manner.

I guess in terms of talking about the attraction of foreign markets, there's both a push and a pull in looking at these other markets. The U.S. domestic life insurance market is very flat, very mature, and generally has bad demographics from a life insurance perspective with the aging population. The environment is very competitive. There are increasing threats from the banks, and the markets are very highly regulated.

By contrast, there's more of a growth opportunity in less-developed markets. A product that has already tired in the U.S. market could, in fact, be highly technical in some of the less-developed markets. There's the possibility of achieving better margins, as there's less entrenched competition in these markets. Also, it's a matter of corporate strategy. At New York Life, there is a corporate strategy to derive at least 10% of new premium income from non-U.S. sources by the year 2000. Of course, there are some competitive pressures, and some U.S. companies are anxious to be where their domestic competitors are elsewhere in the world.

In terms of decisions about markets to go into, the message is to be there early. Basically, the factors that we're looking at as being most important are income, income distribution, disposable income, and disposable income growth. Can the people in this market afford to pay for life insurance now and in the future? Per-capita income is growing, for example, in Mexico. We're looking at a per-capita income of about $2,500 U.S. and a household income of about $10,000.

We look at insurance penetration and here the least attractive markets are those that are already mature, which would be the markets in Japan and in western Europe. The emerging markets offer more fertile ground in terms of less-entrenched competitors. Regulatory framework is an issue here. We're looking at an environment that may be very protectionist, such as Brazil, or more open, such as Argentina. Size and demographics of the market and political stability are obviously a consideration. Other factors include growth potential, local competition, and the state of the economy.

Acquisition tended to be the earlier approach. It offers some immediate presence and some immediate control. It could be cheap or expensive, depending on the target company, but it may leave you with an inventory of bad assets and some long-term fixes that need to be done. Building tends to be a little more attractive these days than it was earlier. Here you have no heredity problems, but it's a very long-term solution.

The trend these days is toward joint venture operations, probably the most popular approach, and here the most productive blend tends to be combining U.S. product and insurance expertise with local distribution and market knowledge. There's also a trend toward marketing agreements in which there might be some technology transfer and a U.S. company could, in essence, try out the market before actually buying in.

In terms of New York Life, basically the steps that we go through are market research. The staff develops a profile of countries and highlights attractive countries that we might look at for future expansion, followed by a field trip to actually put people into that market, test some of the intangibles, and develop a feel for how we might do business in that environment. Executive commitment is critical for the long term, and this is an ongoing challenge as we compete for time with other opportunities elsewhere.

Legal representation is one of the first stages of moving into the market, to utilize our domestic lawyers only for guidance, but to seek to acquire legal counsel within the target country. We'll use advisors as required on any of the deals. Rewards are obvious.

Results tend to take a long time in any of these operations. One of the common symptoms is that of *mañana*—not necessarily tomorrow, but not today. Promises are made, particularly in joint ventures. Capabilities aren't always easy to understand. There can be decommitment on the part of one or both parties, which obviously are very detrimental to an arrangement like that. Ethics tends to be a local characteristic. Tied sales may be fine in some areas, but they're not in this country.

New ways of doing business are a continuing challenge. Basic success factors in any of these operations are human resources, cultural sensitivity, a very long-range strategy, commitment from the top and, most of all, patience.