Japanese insurance firm collapses and more could follow

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The collapse of the insurance firm Tokyo Mutual Life, Japan's 16th largest, is a further indication of the enormous crisis gripping the country's banks and financial institutions.

The 106-year-old company last week filed for court protection from creditors claiming that its debts exceeded assets by 34 billion yen and that it was saddled with some 74 billion yen in unrealised losses on stock market investments. In addition Tokyo Life is said to be holding 30 billion yen in unrealised losses on real estate and 10 billion yen in loans. In total, the insurance firm is said to have liabilities of 980 billion yen or around $7.9 billion.

The collapse is the seventh insurance company failure since 1995 and the fifth in the 2000-01 fiscal year ending on March 31. The most notable bankruptcies were those of Kyoei Life, previously Japan's 11th largest life insurance company, which collapsed in October 2000 with liabilities of 4,600 billion yen ($42.4 billion), representing Japan's largest post-war failure in the insurance sector, and the demise of Chiyoda Life with 2,940 billion yen in debts in the same month.

According to the *Japan Times*, an estimated 700,000 policyholders will be affected by the Tokyo Life collapse, with payouts on long-term insurance policies expected to be cut. The firm went down when its largest creditor, the Daiwa Bank, announced it was not prepared to provide 30 billion yen of additional capital. Daiwa has since announced that instead of making a profit of 28 billion yen for the current fiscal year it expects to incur a loss of 18 billion yen.

The collapse of Tokyo Life and other insurance firms has its roots in the dramatic decline in stock market and real estate values from the early 1990s when the financial bubble of the late 1980s burst.

As a recent *Reuters* report noted: “Tokyo Life, like many other insurers, has long been suffering from a huge gap between its promised returns to policy holders and returns it received on its investments. This negative spread has worsened as the stock market crumbled and long-term interest rates hovered at historic lows. Tokyo Life's accounts at the end of September showed its break-even point at 19,800 on the stockmarket's benchmark Nikkei average. The Nikkei closed at 13,214 on Friday.”

At the high point of the bubble economy the Nikkei hit almost 39,000. It has since fallen by two thirds, while real estate, in which many insurance firms invested, is down by 80 percent.

But the Japanese stock market rose on the news of Tokyo Life's demise on the basis that the decision by Daiwa to let it go was a sign that the country's banks are now going to recognise their bad debts and let insolvent companies go to the wall.

International financial markets have continually demanded such a policy on the grounds that it was needed to strengthen the Japanese economy, and also with an eye to their own interests.

The *Financial Times* pointed to the opportunities which might arise if the “restructuring” of the insurance industry continues.

“Foreign companies,” it noted, “are taking advantage of sector weakness to gain a foothold in the world's largest insurance market. About two third's of Japan's 1,300 billion yen in individual assets lies in bank deposits, offering overseas companies a potential pot of funds to entice into insurance products.”

Banks in trouble

In addition to insurance companies, the banks themselves are on shaky ground. Earlier this month, Fitch IBCA, the international credit rating agency, placed 19 Japanese banks on Rating Watch Negative. The move was made in response to “growing concern over the impact of falling share prices and lingering asset quality problems on the bank's capital quality, performance and prospects.”

According to a report in the *Australian Financial*

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Review: “Bad debts in the banking system total 31.8 trillion yen, according to the FSA (Financial Services Agency), but private sector analysts say the real amount is at least double that—more than 10 percent of the gross domestic product of the world's second largest economy.”

New accounting laws taking effect on April 1, the beginning of the new fiscal year, will begin to reveal the real state of health of the debt-ridden banks as they are forced to value their shareholdings at current market prices rather than the inflated values presently on their books.

Previously banks have been able to hide the extent of their bad debts and potential losses by overstating the value of their shareholdings and real estate assets as well as loans secured by share portfolios and other overvalued collateral.

In the words of US treasury secretary Paul O'Neill, who, like his predecessors, has taken up the call for “restructuring”, Japanese banks have “assets on their books that are simply not there.”

O'Neill likened the situation to the savings and loans crisis in the US in the late 1980s, and called for it to be resolved through large write-offs. But this is easier said than done. The extent of bad debt held by Japanese banks and financial institutions is believed to be six times greater than the savings and loans debt in the US.

Pointing to the consequences of debt write-down, *Guardian* journalist Jonathan Watts wrote: “Disposing of bad assets means bankruptcies and job losses on a massive scale. One European diplomat warned that Japan faced an ‘unemployment bloodbath' if it pushes ahead with financial surgery.”

According to a recent report from the Nomura Research Institute, the aggressive restructuring of all bank portfolios could cut 1.1 percent off economic growth in the latter half of fiscal 2001, accelerate deflation and push the jobless rate above 5 percent.

Even before the restructuring process has begun in earnest some of the banks have announced job cuts as part of their own reorganisation and possible mergers.

Asahi Bank, which is predicting a net loss of 10 billion yen for the current fiscal year, is set to cut 20 percent of its executive's posts, slash executive salaries and close 15 percent of its offices by the end of March 2003. It will also reduce its current workforce of 9,500 by 2,000 by March 2006 and is planning to employ more female staff who earn 3 million yen annually as opposed to male staff who make 10 million. It is also considering withdrawing from overseas operations, closing 19 offices.

United Financial of Japan will axe 7,000 jobs and close 108 branches by March 2005, an increase on an earlier plan to cut 6,000 jobs and close 68 offices. Executive posts will be cut by 20 to 30 percent and the remaining executives will have their pay reduced.

Sumitomo Mitsui Banking Corp has stated it will reduce costs by 47.6 billion yen, largely through cutting 9,300 jobs and closing 303 branches before 2005. Mizuho Financial Group will slash its workforce by 7,000 or 20 percent of its staff and close 30 percent of its domestic and overseas branches.

But the big worry in global financial circles is that the cutbacks could go further than this. What will happen if Japanese banks decide they have to liquidate their vast holdings of international assets in order to repatriate funds and shore up their balance sheets at home?

Jeffrey Garten, dean of the Yale School of Management, raised this possible scenario in an article entitled “The American Risk in Japan” in the *New York Times* earlier this month.

“Japanese entities,” he wrote, “still own some $350 billion of Treasuries, about 25 percent of all such holdings outside the United States, not to mention hundreds of billions in other marketable bonds and stocks. Japanese firms own some $150 billion in direct investments in America, more than those held by any other foreign country except Britain. And Japanese companies employ more than 550,000 Americans.

“A Japanese sell-off of American assets could mean more downward pressure on America's softening economy—more surplus, more layoffs. It could mean that the Japanese would exchange dollars for yen, weakening the dollar, which in turn would lead to increases in the price of imports. Rising prices in a no-growth economy—stagflation—may be more possible than many think.”

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