January 2017

Japan’s commercial insurance market

Swiss Re Corporate Solutions Insurance Japan
Swiss Re Economic Research & Consulting
Japanese firms face a wide array of risks, including fire and earthquakes, which can result in significant losses. In this study, we find that Japan has the world’s biggest protection gap in property. In other words, the difference between the amount of property insured and the total amount of property that should be insured is larger in Japan than anywhere else in the world.

The risk landscape for business is forever changing alongside evolving economic and legal environments, and new risks are constantly emerging (e.g., cyber security) due to developments in technology, globalisation and geopolitical events. Many large Japanese corporations operate globally, and the number of small- and medium-sized firms expanding overseas is on the rise also. As such, Japanese companies are increasingly exposed to liability and other risks in foreign markets, where they face very different regulatory and operating conditions.

How companies manage these risks has a great impact on their market value, their financial strength and their ability to fund projects. Some risks are part of a firm’s core business and can be sensibly retained, while others are better-suited for transfer to the insurance market. Commercial insurers play a key role in helping firms to manage these risks. Insurance-buying should be part of a company’s overall risk management.

Given the diversity and changing nature of risks, firms must constantly reassess whether to insure or to retain their risks. This report analyses the key risks Japanese companies are facing in light of Japan’s shifting economic structure and emerging business trends. Firms should actively engage in risk management as an integral component of their business activities. We look forward to having the chance to discuss further with you how to reduce your company’s exposure to potential losses and be best risk-protected for future growth.

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Country Manager Japan
Swiss Re Corporate Solutions

Clarence Wong
Chief Economist, Head Swiss Re Economic Research & Consulting – Asia
Executive summary

Risk exposure assessment is an ongoing process for corporates.

Commercial insurance helps firms mitigate their exposure to losses and is an essential component of risk management. In Japan as elsewhere, changing dynamics in the economic, business, regulatory, socio-political and technological conditions reshape the risk landscape, driving companies in all sectors to constantly reassess their risk exposures.

Japan is the world’s fourth largest commercial insurance market, but penetration is low relative to other advanced countries.

Japan’s commercial insurance market is the fourth largest in the world after the US, the UK and China. Commercial insurance premiums in Japan totalled USD 33.5 billion in 2015. Penetration (premiums as a percentage of gross domestic product (GDP)) has been rising in recent years; but it is still low relative to other advanced markets. In 2015, commercial insurance penetration in Japan was 0.81% of GDP, compared to 1.6% in the US and 2.4% in the UK.

Motor and property are the main lines. Japanese firms are under-insured in property risk and spend less on liability than their advanced market peers.

By line of business, motor accounted for 34.6% of premiums written in the commercial insurance sector in Japan in 2015, followed by property (17.7%) and liability1 (17.1%). Commercial property premiums resumed steady growth in 2015, following the decline that occurred after the Japan earthquake/tsunami and Thailand flood events of 2011 which led to higher rates in fire and earthquake insurance. Nevertheless, property risk (commercial and residential) remains heavily underinsured. Japan has the biggest estimated property protection gap in the world, estimated to be USD 41 billion. That’s equivalent to 242% of the property insurance premiums that were written by local non-life insurers in 2014.2 In Japan, firms also spend less on liability insurance than in other advanced countries.

Commercial premiums in Japan are forecast to grow by 1.1% in 2017, as prices are likely to stay soft.

In 2016, commercial insurance premiums in Japan are estimated to have contracted by 0.6%, reflecting weak demand and falling premium rates. Insurance demand will continue to be affected by weak economic performance. Rates have continued to soften in most lines, but the pace of reduction is slowing. Commercial insurance premiums are forecast to rise by 1.1% in 2017. Insurers will continue to face a challenging investment environment, characterised by limited yield opportunities and sustained financial market volatility.

Rising risk awareness should support growth in the commercial property insurance segment.

Economic growth is the main driver of demand for commercial insurance, but several underlying trends are shaping the longer-term outlook. Japan’s declining manufacturing activity and industrial assets do not bode well for the insurance sector. That said, increased awareness of business interruption risk will likely support demand for property insurance. Also, the growing services industry should boost demand for liability cover because services firms are more exposed to liability and financial risks.

Increasing exposure to foreign markets, as well as cyber risk, will boost demand for liability cover from Japanese firms.

Many large Japanese firms operate globally and are exposed to different liability regimes via their exports and foreign subsidiaries. The interplay of different macro, financial sector, regulatory, and physical and virtual realities, alongside societal and political dynamics in the markets in which they operate, create a complex liability risk landscape. Increasing exposure to foreign liability risks will likely generate more demand for global liability cover. Technological developments are also changing the environment. For example, cyber security represents a significant source of both reputational and business interruption risk, and has become a top item on the corporate agenda. This could be another driver of growing demand for liability cover in Japan over the long term.

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1 This includes workers compensation.
2 The property protection gap is the estimated uninsured losses from natural catastrophe and general property underinsurance (ie, the shortfall in the amount of property insurance purchased relative to the amount that would be economically beneficial to buy). See sigma 5/2015 – Underinsurance of property risks: closing the gap, September 2015, Swiss Re.
Japanese firms are underinsured relative to peers in the US and the UK.
The world’s fourth largest commercial insurance market

In 2015, direct premiums written (DPW) in Japan’s commercial insurance market were estimated to be USD 33.5 billion, equivalent of 45% of the country’s total non-life insurance premiums. Based on premium volumes, Japan’s commercial insurance market is the fourth largest in the world, after the US, the UK and China.

Table 1
The world’s 10 largest commercial insurance markets in 2015

<table>
<thead>
<tr>
<th>Rank</th>
<th>Country</th>
<th>Commercial insurance DPW (USD bn)</th>
<th>Commercial share of non-life market</th>
<th>Commercial premiums as % of GDP</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>US</td>
<td>297.5</td>
<td>50.7%</td>
<td>1.6%</td>
</tr>
<tr>
<td>2</td>
<td>UK</td>
<td>67.9</td>
<td>67.9%</td>
<td>2.4%</td>
</tr>
<tr>
<td>3</td>
<td>China</td>
<td>54.1</td>
<td>40.4%</td>
<td>0.5%</td>
</tr>
<tr>
<td>4</td>
<td>Japan</td>
<td>33.5</td>
<td>45.2%</td>
<td>0.8%</td>
</tr>
<tr>
<td>5</td>
<td>Germany</td>
<td>25.2</td>
<td>33.2%</td>
<td>0.8%</td>
</tr>
<tr>
<td>6</td>
<td>France</td>
<td>20.2</td>
<td>31.1%</td>
<td>0.8%</td>
</tr>
<tr>
<td>7</td>
<td>South Korea</td>
<td>14.0</td>
<td>24.7%</td>
<td>1.0%</td>
</tr>
<tr>
<td>8</td>
<td>Canada</td>
<td>13.1</td>
<td>30.0%</td>
<td>0.9%</td>
</tr>
<tr>
<td>9</td>
<td>Australia</td>
<td>12.1</td>
<td>45.1%</td>
<td>1.0%</td>
</tr>
<tr>
<td>10</td>
<td>Italy</td>
<td>11.8</td>
<td>35.7%</td>
<td>0.7%</td>
</tr>
<tr>
<td></td>
<td>World</td>
<td>701.7</td>
<td>45.7%</td>
<td>1.0%</td>
</tr>
</tbody>
</table>

Notes: Estimates of total non-life premium written in 2015 (excluding health). The UK figures do not include the London market business.

Source: Swiss Re Economic Research & Consulting.

Figure 1
Commercial insurance penetration in key markets (premiums as % of GDP)

Source: Swiss Re Economic Research & Consulting.

3 All Japan data refer to fiscal years. For instance, 2016 refers to FY2016/17 (year ending March 2017).
Commercial insurance penetration in Japan has been rising steadily in recent years. Corporations’ spending on commercial insurance is in line with that of many of their advanced-county peers, but Japanese firms are underinsured relative to companies in the US and UK. In 2015, penetration in Japan was 0.81% of GDP, compared to 1.6% in the US and 2.4% in the UK. In the same year, automobile risk, including compulsory automobile liability insurance (CALI), accounted for 41.4% of direct commercial insurance premiums written in Japan, followed by commercial property (17.7%), liability (17.1%), marine (5.6%) and other risks (18.2%).

**Figure 2**
The business mix of Japan’s commercial insurance market in 2015

**Table 2**
Penetration of major commercial business lines in Japan in 2015

<table>
<thead>
<tr>
<th>Premiums as % of GDP</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Property</td>
<td>0.17%</td>
</tr>
<tr>
<td>Liability (include worker’s compensation, exclude motor liability)</td>
<td>0.14%</td>
</tr>
<tr>
<td>Worker’s compensation</td>
<td>0.02%</td>
</tr>
<tr>
<td>Commercial automobile (include CALI)</td>
<td>0.33%</td>
</tr>
<tr>
<td>Marine</td>
<td>0.05%</td>
</tr>
<tr>
<td>Credit &amp; surety</td>
<td>0.01%</td>
</tr>
<tr>
<td>Others</td>
<td>0.11%</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>0.81%</strong></td>
</tr>
</tbody>
</table>

Japan has the world’s largest property protection gap, driven mainly by natural catastrophe-related losses.
Market performance

Commercial insurance in Japan

Commercial insurance premiums in Japan returned to strong growth in 2011 in the wake of the earthquake/tsunami that hit the country, and also after the Thailand flooding event of the same year. However, premium growth has moderated since 2013, as the market has softened. This is mainly due to sluggish demand alongside poor economic performance. On the supply side, ample market capacity also exerted downward pressure on premium rates. In 2015, premiums grew by 2% to JPY 4,021 billion (or USD 33.5 billion), after 4.7% growth in 2014 and more than 10% growth in 2013. In 2016, premiums are estimated to have contracted by 0.6%. Until recently, many Japanese firms had no earthquake or loss-of-profits cover/property insurance. In Japan, many industrial assets are insured on an indemnity basis, and recently more policies are going for replacement value basis. In addition – as the 2011 earthquake/tsunami and Thai floods revealed – many firms are significantly underinsured. Commercial lines’ profitability remained steady in 2015 as claims were relatively benign, but 2016 results were impacted by the Kumamoto Earthquake. Market concentration in many commercial lines in Japan is more than 90%.

Figure 3
Commercial insurance direct premiums written (in JPY billion) and growth rate (year-on-year, %)

Figure 4
Commercial insurance penetration rate (premiums as % of GDP)

Market performance

Commercial motor insurance

The share of motor in total commercial insurance business in Japan in 2015 was 41.4%. Automobile insurance protects companies against liability claims and property damage associated with the operation of the vehicles they own. Liability insurance is mandatory for all accredited vehicles. Most motor liability claims are of a high-frequency and low-severity nature. In many advanced markets, larger firms usually do not insure the property part of the risk. But many Japanese corporations still insure their motor fleet’s own damage risks. In 2015, direct premiums from commercial motor insurance rose by 2.6% to JPY 1 664 billion. Profitability of the motor segment improved after rate adjustments in April 2011 and April 2013.4

Figure 5
Commercial motor insurance direct premiums written

Figure 6
Penetration rate in commercial motor insurance (premiums as % of GDP)


4 The standard premium for CALI is determined by the Non-Life Insurance Rating Organisation of Japan on a “no-loss, no-profit” basis. All non-life insurance companies are required to adopt the standard rates.
There was strong growth in commercial property insurance premium in 2015, reflecting also front-loaded demand for long-term fire policies.

**Commercial property insurance**

In Japan, most corporate earthquake and business interruption cover is included as a rider to fire insurance policies. Many large corporations insure their property on an indemnity basis and do not buy loss-of-business or earthquake cover, while many smaller enterprises are largely uninsured. As such, while the earthquake and tsunami in 2011 caused economic losses of more than USD 210 billion, only 17% was covered by insurers (including the government’s Japanese earthquake reinsurance scheme). After 2011, in light also of the Thailand flood disaster in that same year, commercial property owners and corporates have increasingly come to see earthquake and business interruption insurance as core components of their risk management strategies. In 2015, DPW in commercial property insurance rose by 9.9% to JPY 853 billion. The strong growth reflected also the impact of front-loaded demand associated with a shortening of long-term fire insurance products from a maximum of 36 to 10 years in October 2015. The penetration rate of property insurance rose to 0.17% of GDP in 2015 from 0.13% in 2010.

**Figure 7**

Commercial property insurance direct premiums written


**Figure 8**

Penetration rate in commercial property insurance (premiums as % of GDP)

Market performance

Japanese companies spend less on liability cover than their advanced-market peers.

Liability insurance

Japan is the largest liability insurance market in Asia. Liability direct premiums rose by 4.8% to JPY 688 billion in 2015. Rates in general liability, D&O and professional liability lines have been on a declining trend since 2012 due to competition. Even so, liability lines remain profitable because claims have remained low, a reflection of the country’s benign litigation culture. In Japan, companies tend not to sue one another; they prefer to settle out of court. Moreover, Japan’s liability market is highly polarized and only a few large firms purchase global coverage. Compared with other advanced markets, Japanese companies underspend on liability insurance. In 2015, liability business accounted for 17.1% of direct commercial insurance premium written, compared to about 30% in the US. Japan’s liability insurance penetration remains very low at 0.14% of GDP (in 2015), compared with 0.49% in the US and 0.35% in UK.

Figure 9
Liability insurance direct premiums written

Figure 10
Penetration rate of liability insurance (premiums as % of GDP)


^ This excludes motor liability, workers/employee compensation and personal accidents. See Liability insurance in Asia, Swiss Re, September 2015.
Marine insurance premiums decreased in 2015.

Marine insurance

In 2015, marine premiums in Japan fell by 2% to JPY 225 billion, reflecting a weakening in world trade. The penetration rate in marine insurance was 0.045%.

Figure 11
Marine insurance direct premiums written


Figure 12
Penetration rate in marine insurance (premiums as % of GDP)

**Market performance**

Credit and surety insurance premiums continue to drop in 2015.

**Figure 13**
Credit and surety insurance direct premiums written

Credit and surety insurance

The poor trade environment has also adversely affected demand for credit insurance. In 2015, Japan’s credit insurance premiums volumes continued to contract, by 6.5% to JPY 42 billion (2014: –2.4%). Japan’s credit and surety market ranked the third largest in Asia in 2015, after China and Korea. Penetration is lower than in other advanced markets, and even in some other Asian markets. In 2015, credit and surety penetration in Japan was 0.01% of GDP, compared with 0.04% in the US, 0.1% in South Korea and 0.04% in China.

**Figure 14**
Penetration rate in credit and surety insurance (premiums as % of GDP)

Economic performance is a main driver of demand for commercial insurance.
Growth drivers

Commercial insurance premium growth eased further in 2015, reflecting sluggish economic performance and falling premium rates.

Figure 15
Commercial insurance premium and GDP growth in Japan

In a similar way, marine premiums closely track shipping volumes. As global trade continued to weaken in 2015, the growth of Japan’s marine insurance premiums contracted by 2.0%. Demand for marine insurance has continued to be affected by poor trade performance in 2016 due to weak global demand. The strengthening of the Japanese yen in 2016 has also hit exports. On a trade-weighted basis, the yen rose by about 20% in the first nine months of 2016.

Economic performance

Demand for commercial insurance, especially specialty lines, is generally linked to national economic performance. Employment growth, inventory values and building activities all translate directly into premium growth. The very strong growth of commercial insurance premiums in Japan between 2011 and 2013 reflected premium rate increases in the property and motor segments. The rate increases in property came in the wake of the earthquake and tsunami in Japan in 2011, and also the Thailand floods of the same year. Separately, non-life insurers raised motor premium rates in 2011 and 2013 due to rising claims. Commercial insurance premium growth eased to 2.0% in 2015 from 4.7% in 2014, alongside sluggish economic performance and falling premium rates.


Figure 15
Commercial insurance premium and GDP growth in Japan

In a similar way, marine premiums closely track shipping volumes. As global trade continued to weaken in 2015, the growth of Japan’s marine insurance premiums contracted by 2.0%. Demand for marine insurance has continued to be affected by poor trade performance in 2016 due to weak global demand. The strengthening of the Japanese yen in 2016 has also hit exports. On a trade-weighted basis, the yen rose by about 20% in the first nine months of 2016.

\* The standard premium for CALI is determined by the Non-Life Insurance Rating Organisation of Japan on a “no-loss, no-profit” basis. All non-life insurance companies are required to adopt the standard rates.
**Figure 16**
Growth in Japan trade volumes and marine insurance premiums

Note: *January-September 2016, trade refers to values of total imports plus total exports

**Figure 17**
Japan’s trade and exchange rate (% change year-on-year)

Note: as of September 2016.


**Growth drivers**

Demand for commercial property insurance has slowed alongside a declining share of manufacturing in overall economic activity.

**The economy’s structure matters**

Demand for commercial property insurance is also closely linked with manufacturing activity and the accumulation of industrial assets. Between 1996 and 2014, Japan’s commercial property insurance premiums declined by an annual average of 1.3%. This coincided with a decline in the manufacturing sector’s share of GDP to 18.5% from 21% in year 2000. In recent years, however, higher awareness of business disruption risk after the 2011 earthquake disaster at home, as well as the floods in Thailand in the same year, have resulted in an increase of commercial property insurance penetration.

**Figure 18**
Commercial property insurance penetration, and share of manufacturing of total GDP

<table>
<thead>
<tr>
<th>Year</th>
<th>Commercial Property Premiums as % of GDP</th>
<th>Manufacturing as % of GDP</th>
</tr>
</thead>
<tbody>
<tr>
<td>1995</td>
<td>0.17%</td>
<td>23%</td>
</tr>
<tr>
<td>1996</td>
<td>0.16%</td>
<td>22%</td>
</tr>
<tr>
<td>1997</td>
<td>0.15%</td>
<td>21%</td>
</tr>
<tr>
<td>1998</td>
<td>0.14%</td>
<td>20%</td>
</tr>
<tr>
<td>1999</td>
<td>0.13%</td>
<td>19%</td>
</tr>
<tr>
<td>2000</td>
<td>0.12%</td>
<td>18%</td>
</tr>
<tr>
<td>2001</td>
<td>0.11%</td>
<td>17%</td>
</tr>
<tr>
<td>2002</td>
<td>0.10%</td>
<td>16%</td>
</tr>
</tbody>
</table>


Liability penetration has been rising as the share of the services sector in overall economic activity has grown.

**Figure 19**
Commercial liability insurance penetration, and share of services sector of total GDP

<table>
<thead>
<tr>
<th>Year</th>
<th>Commercial Liability Premiums as % of GDP</th>
<th>Services as % of GDP</th>
</tr>
</thead>
<tbody>
<tr>
<td>1995</td>
<td>0.16%</td>
<td>76%</td>
</tr>
<tr>
<td>1996</td>
<td>0.14%</td>
<td>74%</td>
</tr>
<tr>
<td>1997</td>
<td>0.12%</td>
<td>72%</td>
</tr>
<tr>
<td>1998</td>
<td>0.10%</td>
<td>70%</td>
</tr>
<tr>
<td>1999</td>
<td>0.08%</td>
<td>68%</td>
</tr>
<tr>
<td>2000</td>
<td>0.06%</td>
<td>66%</td>
</tr>
<tr>
<td>2001</td>
<td>0.04%</td>
<td>64%</td>
</tr>
<tr>
<td>2002</td>
<td>0.02%</td>
<td>62%</td>
</tr>
<tr>
<td>2003</td>
<td>0.00%</td>
<td>60%</td>
</tr>
</tbody>
</table>


Meanwhile, penetration rates in liability have risen in recent years as the share of the services sector in total economic activity has increased. That’s because service sector companies are relatively more exposed to liability and financial risks than manufacturing organisations.
Increasing awareness of business interruption risk

Premiums in commercial property insurance returned to strong growth after the 2011 earthquake/tsunami disaster and Thai floods. Premiums per non-dwelling fire insurance contract rose by 16% to JPY 155,446 in 2014 from JPY 133,956 in 2010 (see Figure 21). After the 2011 earthquake disaster, Japanese insurers were mainly affected by commercial earthquake insurance claims. Residential earthquake insurance claims had no earnings impact due to support from the government-backed reinsurance system and the drawdown of reserves for residential earthquake insurance. Japanese insurers were actually harder hit hard by the Thai floods in the same year, given their heavy exposure to industrial all-risk policies in the affected zone. The reported net commercial insurance claims of five major Japanese insurers following the floods was USD 4.2 billion, more than double the combined USD 2 billion in claims these same five companies faced on account of the earthquake and tsunami at home, according to the Institute of Actuaries of Japan. Business interruption insurance has become a growing business line since 2011.

Figure 20
Japan non-dwelling fire insurance contracts (number of contract in millions, LHS) and premiums (JPY billion, RHS)

Figure 21
Premiums per non-dwelling fire insurance contracts (JPY, thousands)

Growth drivers

The annual property (commercial and residential) protection gap in Japan is estimated at USD 41 billion.

The world’s biggest property protection gap

Property risk (commercial and residential) remains highly underinsured in Japan. Premiums in the global property insurance market are estimated to be around USD 413 billion in 2014, with the level of global underinsurance standing at USD 221 billion. Japan has thus the world’s biggest property protection gap, with an estimated total annual uninsured loss of USD 41 billion, or 242% of the property premiums written by local non-life insurers in 2014.

Figure 22
Annual expected insured and uninsured natural catastrophe property losses (in USD billion)

Table 3
Property (commercial and residential) protection gap (in USD billion)

<table>
<thead>
<tr>
<th>Rank</th>
<th>Country</th>
<th>General property underinsurance</th>
<th>Nat cat property protection gap</th>
<th>Total property protection gap</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Japan</td>
<td>13.1</td>
<td>27.9</td>
<td>41.0</td>
</tr>
<tr>
<td>2</td>
<td>China</td>
<td>13.6</td>
<td>22.7</td>
<td>36.3</td>
</tr>
<tr>
<td>3</td>
<td>US</td>
<td>–</td>
<td>30.9</td>
<td>30.9</td>
</tr>
<tr>
<td>4</td>
<td>Germany</td>
<td>7.8</td>
<td>2.1</td>
<td>9.9</td>
</tr>
<tr>
<td>5</td>
<td>Mexico</td>
<td>2.2</td>
<td>5.2</td>
<td>7.4</td>
</tr>
<tr>
<td>World</td>
<td>68</td>
<td>153</td>
<td>221</td>
<td></td>
</tr>
</tbody>
</table>

Note: Expected losses generated by Swiss Re’s natural catastrophe risk model MultiSNAP.

Note: Expected losses generated by Swiss Re’s natural catastrophe risk model MultiSNAP. The natural catastrophe property gap measures the estimated uninsured losses from natural catastrophes, while the general property underinsurance measures the shortfall in the amount of property insurance purchased relative to the amount that would be economically beneficial to buy.
Increasing exposure to liability risk in foreign markets

Japanese corporations have wide-reaching interests globally, with manufacturing facilities in Europe, the US and many of the low-wage economies in Asia (China, Thailand, the Philippines, Indonesia and Vietnam). At the end of 2015, the total stock of Japan’s outward direct investment was USD 1 259 billion, up from USD 259 billion in 1996. The advanced markets remain the main destination for the outflows (absorbing 73.5% of the total in 2015) but the emerging markets are taking an increasing share (26.5% in 2015, up from 24.9% in 1996).

Japanese corporations face an increase in liability risks from their foreign exposures ...

... and are likely to demand more global liability cover in the coming years.

There is increasing demand for product recall insurance especially by the automobile industry following the large claims in the US in 2016. The US legal system produces most of the world’s awards of USD 1 billion or greater. As a result of situations like these and their growing exposure overseas, Japanese firms are likely to demand more global liability cover in the coming years.
Growth drivers

Evolving technologies give rise to new risks and rising demand for liability cover.

Technological advancement and new risks

Technologies and product innovation are changing the risk landscape and shaping the longer-term outlook for liability insurance demand. For instance, 3D printing presents a big challenge in tracing/determining the liability for product defects. Another example is the electronic technology involved in car manufacturing. Japanese automakers have poured billions of dollars into developing navigation systems, automatic vehicle-collision notification, automatic braking and even driverless cars in recent year. If the technology fails, the carmakers can be exposed to huge liabilities. Also, they are linking the telematics systems in the cars to smartphone apps, giving owners remote control over some aspects of their vehicles. As cars become more networked, there is growing potential for the vehicles to be hacked, adding another dimension to overall risk exposure.

There is growing awareness of cyber risk amidst the greater use of smartphones, credit cards, mobile and internet banking. Businesses that possess personal or sensitive data are increasingly exposed to cyber security breaches. In 2011, a major Japanese game developer was hacked resulting in the theft of personal data of over 1 million customers. In June 2015, Japan’s national pension system was also hacked, leading to a leak of 1.25 million sets of personal data. Cyber risk issues are at the top of the corporate agenda. In a survey by the World Economic Forum, cyber risks ranked as main concern for corporates in Japan in 2016 (see Figure 25).

In an age where information flows freely and instantly, facilitated by the use of social media, a negative incident such as product recall, or even a rumour can spread quickly. This can hit revenues in the short term and more damagingly, have a long-term impact on brand value and reputation.

Figure 25
Top risk concerns of Japan businesses in 2016


Cyber risk is the top concern for Japanese corporations.
Market outlook

Premium outlook remains challenging

Commercial insurance premiums in Japan are estimated to have declined by 0.6% in 2016 to JPY 3,996 billion (USD 37.2 billion), reflecting weak demand and continued market softening. By line of business, motor premiums remained steady but fire, casualty and marine premiums all contracted. A sharp drop in fire premiums also reflected the impact of front-loaded demand associated with a shortening of long-term fire insurance products from a maximum of 36 to 10 years in October 2015. Non-life insurers’ underwriting results were also impacted by the Kumamoto earthquake in April 2016.

Commercial insurance demand will continue to be affected by the economic outlook, which remains weak. Japan’s real GDP growth is forecast to be 0.8% in 2017, up from an estimated 0.6% in 2016. Commercial premiums volumes are expected to grow by a modest 1.1% in 2017. Premium rates have continued to soften in most lines, but the pace of reduction is slowing. Nevertheless, insurers will continue to face a challenging investment environment, characterised by limited yield opportunities and sustained financial market volatility. To support economic growth, the Bank of Japan introduced negative interest rates in February 2016, which resulted in negative yields on shorter duration government bonds (JGBs).

Table 4
Japan commercial insurance forecasts

<table>
<thead>
<tr>
<th>Direct premiums written*</th>
<th>2013</th>
<th>2014</th>
<th>2015</th>
<th>2016E</th>
<th>2017F</th>
</tr>
</thead>
<tbody>
<tr>
<td>Commercial lines, JPY billion</td>
<td>3,767</td>
<td>3,942</td>
<td>4,021</td>
<td>3,996</td>
<td>4,041</td>
</tr>
<tr>
<td>Liability</td>
<td>650</td>
<td>657</td>
<td>688</td>
<td>679</td>
<td>689</td>
</tr>
<tr>
<td>Property</td>
<td>736</td>
<td>776</td>
<td>853</td>
<td>776</td>
<td>803</td>
</tr>
<tr>
<td>Motor</td>
<td>1,549</td>
<td>1,622</td>
<td>1,664</td>
<td>1,681</td>
<td>1,711</td>
</tr>
<tr>
<td>Marine</td>
<td>223</td>
<td>230</td>
<td>225</td>
<td>200</td>
<td>196</td>
</tr>
<tr>
<td>Others</td>
<td>609</td>
<td>658</td>
<td>590</td>
<td>659</td>
<td>641</td>
</tr>
<tr>
<td>Credit &amp; surety</td>
<td>46</td>
<td>45</td>
<td>41</td>
<td>–</td>
<td>–</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Commercial lines, yoy %</th>
<th>10.3%</th>
<th>4.7%</th>
<th>2.0%</th>
<th>−0.6%</th>
<th>1.1%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Liability</td>
<td>18.6%</td>
<td>1.0%</td>
<td>4.8%</td>
<td>−1.3%</td>
<td>1.1%</td>
</tr>
<tr>
<td>Property</td>
<td>5.5%</td>
<td>5.4%</td>
<td>9.9%</td>
<td>−9.0%</td>
<td>1.5%</td>
</tr>
<tr>
<td>Motor</td>
<td>8.5%</td>
<td>4.7%</td>
<td>2.6%</td>
<td>1.0%</td>
<td>1.8%</td>
</tr>
<tr>
<td>Marine</td>
<td>12.2%</td>
<td>3.0%</td>
<td>−2.0%</td>
<td>−11.0%</td>
<td>−2.0%</td>
</tr>
<tr>
<td>Others</td>
<td>12.0%</td>
<td>8.1%</td>
<td>−10.3%</td>
<td>11.6%</td>
<td>−2.0%</td>
</tr>
<tr>
<td>Credit &amp; surety</td>
<td>2.4%</td>
<td>−2.4%</td>
<td>−8.6%</td>
<td>−</td>
<td>−</td>
</tr>
</tbody>
</table>

Note: # All economic data refer to calendar year ending December. *All insurance data refer to fiscal year. For instance, 2016 refers to FY2016/17 (year ending March 2017).

Conclusion

Commercial penetration in Japan has been rising steadily in recent years. However, Japanese firms are generally underinsured relative to their peers in other advanced markets. Some underlying trends are shaping the outlook for commercial insurance business in Japan. In terms of economic structure, the country’s declining manufacturing sector and industrial asset accumulation do not bode well for the property segment, but increased awareness of business interruption risk and of the expenses involved in recovery efforts, will lend support. Further, the growing services sector will drive growth in liability insurance, as service industry companies are relatively more exposed to liability and financial risks.

Moreover, Japanese corporations are increasingly exposed to liability risks in foreign markets. Many large Japanese corporations operate globally and face very different macroeconomic conditions, financial market developments, regulations, physical and virtual environments, and societal and political dynamics in these markets. The interplay of these changing risk factors can mean very different liability risk landscapes and, with growing overseas exposure, Japanese firms will likely demand more comprehensive global liability coverage in the coming years.

Evolving regulations and technological progress are changing the risk landscape and shaping the longer-term outlook for liability insurance demand. While different industries are seeking coverage for new and emerging risks, regulators are tightening requirements over data privacy and consumer protection, among others. Increasing awareness of the potential damage to reputation and business interruption will likely drive growing demand for liability and cyber risk insurance.