Life Insurance Distribution Systems in Japanese Market
--- Series 1: Pre-World War II Period ---

Modern insurance system was imported into Japan after the Meiji Restoration. A famous book introducing this system in details was published in 1867 by Yukichi Fukuzawa, titled *Travel in the Western World*. Many businessmen and intellectuals became interested in the insurance business after reading this book. Some of them pioneered the establishment of domestic insurance companies in later years.

Due to this background, most of Japanese insurance companies started their business by imitating the Western companies which included such as the product design or the distribution systems. However, the business models adopted by the Japanese and Western insurance companies differed in many points. In particular, the development of life insurance distribution systems showed some characteristics that seemed to be unique to Japanese market.

In July 1881, the first modern Japanese life insurance company, Meiji Life, was incorporated with an approval of the Tokyo Governor. Until March 1888 when the second company, Teikoku Life, was founded, Meiji Life had been nearly monopolized the life insurance market while competing with some mutual aid associations which were not considered as an incorporation. The third company was Nippon Life, established in July 1889. The three companies were founded as a stock company as well as the others established later, despite of the fact that the mutual organizational form had not been prohibited by law until June 1899.

The mutual organizational form, however, became re-legalized in July 1900, when the first Insurance Business Act came into effect. Soon after, two mutual companies, Dai-ichi Life and Chiyoda Life, were established in 1902 and 1904 respectively. This two companies later became one of the Big Five companies which also included the above three stock companies. Given such circumstances, in addition to the fact that the insurance industry was at the very early stage of the development, the difference of organizational form had great influences on the development of Japanese life insurance distribution systems.

Founder of Dai-ichi Life, Tsuneta Yano
(Source: *The Dai-ichi Mutual Life Insurance Company -- 100 Years of History*, p.36)

Before the mutual companies entered the market, the agency distribution system was most popular in the life insurance business. At the beginning, most of agencies were either the bankers or the local notables. Apparently the insurance companies' intention was to utilize their social influence and credibility to sell policies since the life insurance business was not well-known yet. Needless to say, most of these agencies purchased the policies for themselves first, before conducting the solicitation activities. Meanwhile, some of them even were a shareholder of insurance company. For example, in the early years of Teikoku Life and Nippon Life, many of their agencies held certain amount of company shares, which was so-called shareholder-agency policy.

Besides the insurance solicitation, the agencies were also in charge of premium collection. The reward was paid on a commission basis. They can earn a three to five per cent of insured amount as a commission for selling a policy. They also can take five per cent of premium collected as a commission. Considering the gradual growth achieved by all the companies, we could say that the agency system was effective in the early years.

Picture of Tokyo Station in Taisyo Era (1912-1926) (Source: 110 Years of History of Meiji Life, p.70)
Note: The Tokyo Station building was constructed as one of symbols of Japan's modernization. The construction was started in 1908 and completed in 1914.

However, the insurance business was no more than a side business to most of these agencies. Many agencies became more interested in the premium collection than the policy selling business as insurance companies' policies in force increased. Consequently, the overall operating rate of agencies began to deteriorate from the early 1900s.

At about the same time, Dai-ichi Life and Chiyoda Life, the first two domestic mutual companies, started their business. Both companies adopted the sales agent system which was paid on a piecework basis. In the meantime, Chiyoda Life also introduced the agency system, and most of its agencies were also the fund contributors. Moreover, mutual companies undertook an intensive promotion of the mutuality as their sales strategies, which were embodied in their product design, namely the sales of with-profits policies.

According to their mutuality theory, only the mutual company truly considered their policyholders first and all the company profits were be paid back to the policyholders as an owner's profits. Obviously it was a sales promotion which typically focused on the organizational differences rather than a simple price competition. In fact, the mutual companies tended to set a higher premium level than the stock companies at that time.

However, they justified it by committing a higher policy dividend, which seemed to be persuasive and widely accepted by the customers, considering the fact that the with-profits policies later became the mainstream product. On the other hand, the competition among the mutual companies was concentrated on the policy dividend.

Given the above circumstances, it is reasonable to say that the market competition had become more complicated after the mutual companies entered the market, and the stock companies were required to reform their distribution systems to make them more competitive in order to stay in business. Concretely, they started to introduce the sales agent system, while taking some specific measures such as the adoption of the piecework basis payment to improve the operation rate of their existing sales agencies. The sales agent channel eventually became the major distribution channel in the 1920s after the Meiji Life, Teikoku Life and Nippon Life declared this channel as its major channel in 1920 and 1926 respectively.

The agency distribution channel kept playing an important role, however, since most companies did not abandon this channel, and the new establishment had been continued even during the World War II period, despite of the fact that its growth rate was lower than that of the sales agent. The gap between the growth rates of both channels increased more rapidly in the post World War II period, which we will discuss more details in our next report.

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