"The complexities around finding the right targets, and the limitations in many markets on investments, are slowing activity. However, interest levels in Asia Pacific remain high as market saturation and economic uncertainty in mature markets means re/insurers look further afield for development opportunities."

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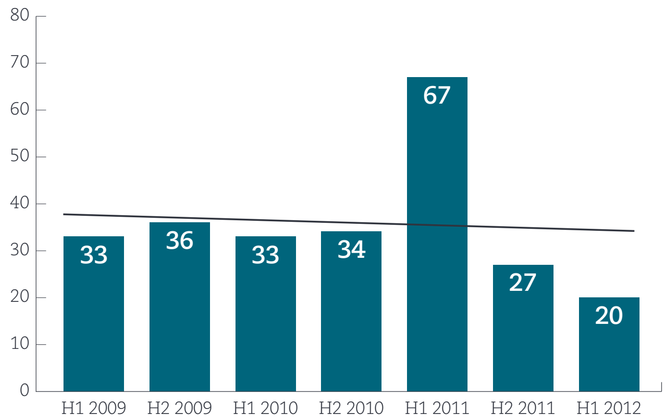
Asia Pacific

Overall, the trend in M&A activity in Asia Pacific has moved gently downwards over the last three and a half years – albeit with a dramatic spike in activity in the first half of 2011 as a spate of transactions that were put on hold during the global financial crisis were closed.

Volume of deals in Asia Pacific



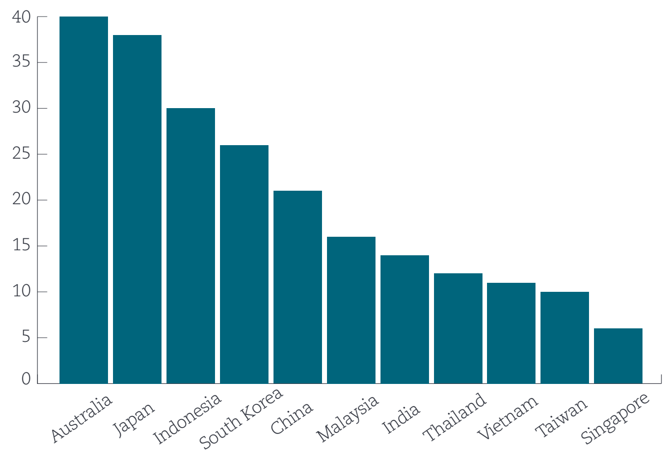
However, this is probably more a reflection of the complexities around finding the right targets, and the limitations in many markets on investments, rather than a decreasing level of interest in M&A in Asia Pacific. International insurers, whose growth in more developed economies has stalled due to a combination of market saturation and economic uncertainty, still appear keen to look further afield for development opportunities.

Primary targets appear to be in emerging market countries such as Indonesia, Vietnam and Malaysia, but insurers still have a keen focus on the more established markets such as Hong Kong and Singapore. In a number of these locations, regulators are pushing for better run, higher capitalised insurers, and are introducing new rules to deliver this. As some companies struggle to comply with the new regulations, this will likely drive an increase in M&A as the market consolidates.

In saturated markets, such as Korea and Taiwan, regulators are loosening the rules on outward investment by domestic insurers to make it easier for them to capitalise on opportunities elsewhere in the region, and, in particular, the potentially lucrative Chinese market. The fallout from the natural catastrophes in Japan and Thailand is another factor that has been driving M&A, as battered insurers look to rebuild their capital positions and diversify their risk portfolios.

Distribution remains another issue for international entrants – how do they get their products to the customer? Historically, distribution across the region has been dominated by the agency model – although greater economic sophistication and improved technology means that this may be changing. So, insurers are now looking at new distribution channels, and it is predicted that this will drive an increase in M&A in the region.

Deals in Asia Pacific by country: 2009-2012



Australia

The Australian market has seen a strong mix of both inbound and outbound activity. While Australia is very much on the radar of Asian companies with international ambitions, the market remains highly concentrated, dominated by the two biggest players: Insurance Australia Group (IAG) with around 40% of the market, and Suncorp with 34%.

The only international insurer involved in inbound M&A activity in Australia over the last 12 months was Beazley Group, which expanded its presence in the group disability market through the purchase of two managing general agencies, Australian Income Protection and Blue-GUM Special Risks, both based in Sydney. These acquisitions demonstrate the desire of international insurers to access established books of business as a way of growing their presence in the Australian market.

The unprecedented run of catastrophic losses seen in the last two years has meant that insurers in Australia and New Zealand have had to rethink their exposure and/or their reinsurance protection. This has led the biggest players to conduct a strategic review of their operations, which has sparked some deal activity.

In December 2011 Suncorp purchased AMP's General Insurance Distribution (AMP GID) as part of its strategy "to strengthen its distribution footprint and grow its business, as well as provide distribution in line with clients' preferences," according to Anthony Day, chief executive of Suncorp's commercial insurance business.

In terms of outward investments, IAG continued its expansion overseas with a number of high-profile deals. These include the acquisition of a 20% stake in China's Bohai Property Insurance in December 2011 and the purchase in May 2012 of 30% of AAA Assurance, Vietnam's sixth largest motor insurer. In the same month, IAG completed a deal to acquire AMI Insurance Ltd of New Zealand. IAG is also likely to expand its offerings in emerging markets including Thailand, Malaysia and Indonesia. IAG's CEO, Mike Wilkins, has stated that: "IAG's long term goal is to have 10% or more of its premiums come from Asia by 2016."

Japan

The domestic Japanese insurance market was static in terms of M&A in the 12 months up to July 2012, a trend that is set to continue as the country's three main insurers, Sompo Japan Insurance Inc, Mitsui Sumitomo Insurance Group Holdings and Tokio Marine, control 70% of the market between them. It was a similar story for inbound M&A since all major international insurers already have a presence in the market.

Investment returns at home are very low and Japan's domestic insurance market is shrinking because of a declining population and prolonged economic weakness. There has also been considerable fallout from the earthquake and tsunami in 2011 as insurers seek to diversify their risk portfolios.

The result is that outbound activity by Japanese companies has picked up over the last 12 months. Among a spate of deals, the most notable were Mitsui Sumitomo's acquisitions of Indonesia's Asuransi Jiwa Sinarmas PT and the Indian operations of Max New York Life Insurance, while Nippon Life Insurance Co purchased a stake in Reliance Life Insurance Co Ltd of India.

Current regulations prohibit Japanese insurers from holding more than 10% of their own total assets in an acquired entity's investment assets. This effectively prevents Japanese insurers from buying more or bigger stakes in foreign insurers. In addition, Japanese insurers' subsidiaries are not allowed to do business in areas not specified in Japan's insurance business law.

The Japan Financial Services Agency has indicated that there are deregulation plans in the pipeline which will make it easier for Japanese insurers to take advantage of the strong yen and make acquisitions in Asia's emerging markets and elsewhere. The likely result will be increased transaction activity as insurers look to diversify beyond Japan's borders to enhance their revenue, profit and stability.

Indonesia

With the number of large foreign companies establishing operations in Indonesia increasing, particularly in the natural resources sector, so the levels of employment and per capita income are rising – a situation that will undoubtedly help drive demand for insurance products.

Despite the fact that a number of insurers are looking for opportunities in Indonesia, there is a lack of attractive targets. Many local businesses are seen as weak, with insufficient business controls, and this deters potential entrants, particularly in light of growing anti-corruption legislation in developed markets in particular the UK and US.

However, the second half of 2011 and the first six months of 2012 did see a number of new entrants into the Indonesian market, with Japanese insurers Mitsui Sumitomo Insurance, Hitachi Capital Corp and Meiji Yasuda Life Insurance Co all making acquisitions.

In June 2012, ACE announced that it was continuing its Indonesian expansion with the agreement to acquire Jakarta based PT Asuransi Jaya Proteksi (JaPro) in a cash transaction worth approximately US$130 million, which is expected to be completed within the third quarter of 2012.

JaPro is among Indonesia's top 10 general insurers and has an extensive distribution system throughout the country. Announcing the deal, the regional president of ACE Asia Pacific, Damien Sullivan, said that "there is a good strategic fit between our companies" and that "the acquisition will enable both groups to complement each other's performance, allowing ACE to diversify its current business by applying JaPro's local expertise and strong customer service record to its current strategies." The move will undoubtedly assist ACE to further its expansion in the region and we expect the market will likely see other strong players looking at ways to emulate this move.

The Indonesian regulator developed new solvency rules in 2008, which have been implemented in stages since December 2010. Looking ahead, the second stage (of three, the third being at the end of 2014) is at the end of 2012 by which time insurers should have a minimum paid up capital USD7.7 million. This will result in the non-renewal of a number of insurance licences by insurers unable to meet such minimum capital requirements. In the near term, this development is likely to be the catalyst for a flurry of M&A activity in Indonesia before 2013.

South Korea

South Korea is one of the world's most saturated and competitive insurance markets. According to a Swiss Re sigma study, the country's insurance penetration, as measured by the ratio of premiums to gross domestic product, is one of the highest in the world at 11.2% in 2010.

It, therefore, offers limited opportunities for organic growth and Korean insurers are facing tough market conditions at home, with intense competition and low profitability forecasts. The result is that many are considering expanding into new markets through M&A abroad. Overseas expansion also helps to spread risk and balance business cycles, as well as broadening client bases and, as is the case in Japan, is something that the Korean regulator is actively encouraging.

Evidence of this trend was seen in November 2011 when Korea Life Insurance announced a 50-50 joint venture insurance operation in China with Zheijiang International Business Group. The insurer, South Korea's second largest life insurance company, has also expressed an interest in ING Group's Asia Pacific insurance operations and in May 2012 was shortlisted in the bidding process for a deal that could eventually be valued above US$7 billion.

This has been followed by plans made by their chief rival, Samsung Life, to develop operations in Thailand, India and Indonesian insurance markets in 2012.

Despite the difficulties of entering the South Korean market, many of the leading foreign insurers believe that the opportunities are too good to ignore and in May 2012 Canada's Tiger Holdings LP completed a deal to acquire Kyobo Life Insurance Co Ltd. In the same month French insurance giant AXA SA made a move to strengthen its position in South Korea's direct insurance market through the acquisition of general insurer Ergo Daum Direct in a deal that should be completed later in 2012.

AXA already have a leading presence in the South Korean motor insurance sector through its wholly-owned subsidiary AXA Direct Korea, controlling around 15% of the market. With the acquisition of Ergo Daum Direct, AXA will become the biggest player in the Korean auto insurance industry with a market share of 22% following the merger.

China

Now the world's second largest economy, China still only has an insurance penetration rate of 3.7%, compared with an average of 10.7% for other more developed markets in Asia such as Japan and South Korea. Despite this, China's insurance market now ranks as the sixth largest in the world.

So, while the scale of the opportunity in China is huge, barriers to entry for foreign players are substantial. Under current Chinese market regulations, 20% is the maximum holding a single foreign investor is allowed to have in a domestic general insurance company. This minority investment route remains the most straight-forward route into China, as those companies looking to open an office or a subsidiary in China will need to overcome a number of hurdles, mainly involving operating history and asset levels, while the application process to obtain an insurance licence can take more than three years.

The highest-profile inbound deal over the period July 2011 to June 2012 was IAG's acquisition of a 20% stake in China's Bohai Property Insurance Ltd, completed in April. Bohai is focused primarily on motor insurance, a product line in which IAG traditionally has had competitive strength. It is likely that there will be more transaction activity in this sector as the regulator has opened up the motor insurance market to foreign companies, removing minimum premiums in order to increase competition.

In conjunction with rising insurance demand, IAG also credited improvements to industry regulations in China with improving the sector's underwriting discipline and overall business forecast as drivers for the deal. These infrastructure efforts have, in turn, encouraged greater foreign investment in the country. The Chinese general insurance market, once dominated by four big state-owned players has become more open, enabling smaller companies, like Bohai, to remain commercially sound and present more profound and diverse opportunities for the international insurance industry.

Also in April, German insurance group ERGO, a subsidiary of global reinsurance giant Munich Re, announced that it had received the necessary start-up permissions from local regulators to launch a joint venture operation with Shandong's state-owned Assets Investment Holding Company (SSAIH). This new joint venture company, which yet has to be named, will primarily focus on selling life insurance and other savings-related products to retail customers across Shandong.

Announcing the deal, ERGO's Dr. Jochen Messemer acknowledged that the highly competitive nature of the Chinese market has been particularly challenging for foreign insurance entrants. However, he emphasised that, "we are confident that – based on our technical and risk management expertise and international know-how in setting-up life insurance operations – we will set strong foundations for being successful in China in the long run."

In terms of domestic consolidation, Wuhan Kaidi Hldg Invest Co Ltd acquired Zhongying Changjiang Intl in December. Other domestic deals that have received regulatory approval and are expected to close in the near future include ICBC's takeover of AXA Minmetals Assurance Co Ltd and Peiking Founder Group's equity transfer of 51% of Haier Meiji Yasuda Life Insurance Co.

Domestic transaction activity is likely to accelerate as China's insurance regulator embarks on creating the second version of its solvency requirements. Yanli Zhou, vice-chairman of the China Insurance Regulatory Commission (CIRC), said his country's new solvency requirements will reflect trends taking place internationally as well as the particular characteristics of the Chinese market and are expected to be implemented by 2016.

In terms of outbound activity the only transaction of note was the announcement in November 2011 of state-owned reinsurance giant China Re's partnership with the UK's Catlin, marking the first time a Chinese company has made a direct investment in the Lloyd's market.

Li Peiyu, chairman of China Re Group, said: "This new venture is a milestone in our international strategy. It will not only help us to gain a better knowledge of Lloyd's and benefit from its worldwide network, but it will also increase China Re's experience of international reinsurance operations and management and help build a foundation for China Re to grow into an important player in the world reinsurance market." Under the terms of the deal, China Re employees will be seconded to Catlin to gain first-hand experience working in the Lloyd's market.

As well as providing Chinese businesses with greater exposure to the London market, Catlin will be hopeful that the deal will, in turn, enable their company to increase gross premiums written in the potentially lucrative Asia-Pacific market. The deal marks a step forward in Lloyd's ambition to attract both capital and talent from growth economies like China. It also demonstrates the strength of the platform as an entrance point for Chinese insurers looking to enter the international insurance arena. There will likely be further interest in the Lloyd's platform both from other Chinese insurers, and those in other developing economies.

Hong Kong

Hong Kong remains a key insurance hub in the region, although the relatively low number of targets will always limit transaction activity. However, the territory has seen some significant deals recently. In March 2012, AXA strengthened its presence in the region when it paid US$494 million for HSBC's general insurance businesses in Hong Kong, Singapore and Mexico. The deal will help fulfil the French insurer's goal of becoming the top general insurance player in Asia by 2015. HSBC also sold Hang Seng General Insurance, based in Hong Kong, and a similar business in Argentina to Australia's QBE Insurance for US$420 million. For all of these acquirers, the key benefit is that they gain invaluable access to a proven distribution channel.

The fallout from the financial crisis is still being felt, with the forced sale of ING's Asia Pacific operations. It is expected that the buyer is most likely to come from North America, in part as a result of the lack of European interest due to the economic challenges in that region. The fact that the sale will also include ING's Japanese and Taiwanese business will also deter European interest due to reporting under European GAAP, which is very stringent on booking liabilities. AIA is a possible suitor, providing competition issues can be overcome, while some large Asian companies have also submitted bids.

Malaysia

Malaysia continues to attract interest from foreign investors with a number of significant deals in the second half of 2011 and the first six months of 2012. The attractive nature of the Malaysian market is further heightened by the relatively lax foreign ownership regulations; foreign owners are allowed to buy up to 70% of a domestic insurer.

In September 2011 Switzerland's Zurich Insurance Company Ltd acquired composite insurer Malaysian Assurance Alliance Berhad (MAAB). Martin Senn, Chief Executive Officer of Zurich, said: "The acquisition of MAAB is another milestone in our emerging-market strategy. It expands our presence in the Asia-Pacific region and positions us for further profitable growth. Malaysia is a highly attractive market with considerable economic potential and a young and dynamic population."

In April 2012 Australian insurer IAG's Malaysian joint venture business, AmG Insurance Bhd, entered into a conditional agreement to buy Kurnia Insurans (Malaysia) Bhd in a transaction worth US$509.1 million, which is expected to close by the end of 2012. Kurnia is the largest motor insurer in the country and in the top four overall. The acquisition will make AmG the largest non-life insurer in Malaysia with a 13% market share.

Moving in the other direction, UK insurer Aviva has put its 49% stake in its joint venture with Malay bank, CIMB, up for sale. Aviva's imminent exit comes only five years after the firm entered the Malaysian insurance market in June 2007. Their decision to sell their Malaysian venture is part of larger plans to sell their underperforming businesses globally, including those in Sri Lanka and South Korea in an attempt to raise money to protect it against its Eurozone exposure.

Another area attracting interest from foreign players is takaful insurance, which some believe holds the key to the nation's future development and expansion of the domestic insurance market.

At present there are very low levels of insurance coverage and penetration rates across the Malaysian population, particularly in the Muslim community, so this is a sector that provides significant potential – especially when coupled with increasingly sophisticated distribution methods.

India

The insurance M&A market in India has been relatively static through 2011 and the first half of 2012. The most significant domestic deals saw Future Generali India Life Insurance acquire the Industrial Investment Trust, and the acquisition of GS Mace Holdings Ltd by Max India Ltd.

International acquisitions were limited to two Japanese companies – Nippon Life Insurance Company and Mitsui Sumitomo Insurance – acquiring Reliance Life Insurance Company Ltd and Max New York Life respectively in the aftermath of heavy catastrophe losses in recent years.

The low level of transaction activity in India, in part, is a result of the economic situation; GDP growth has slowed to around 5.3% while inflation has risen, reaching 7.3% in June 2012. Added to this, with many potential buyers' balance sheets weakened by events elsewhere in the world, deal sentiment is less than positive.

Uncertainty over government policy is another factor impacting deal activity. The foreign direct investment limit remains at 26% and the fact that the long expected increase to 49% has still not materialised – nor is likely to in the near future – remains a source of frustration for multinational companies looking to enter or increase their stake in the Indian market.

Companies looking for a capital injection may now, however, have an alternative to seeking a direct investor. The regulatory restrictions around pursuing an initial public offering were lifted with the publication of new guidelines, and companies may look at a public offering as an alternative source of raising capital. However, conditions for conducting an IPO remain rigorous and while no insurer has pursued this route, it is expected that some will try in the near future.

Thailand

The insurance market in Thailand is still getting to grips with the losses sustained during the floods of 2011, the costliest natural disaster event in south-east Asia's history, with a large number of carriers calculating their own exposures based on a total industry loss of around US$15 billion.

Many have either dramatically reduced their catastrophe exposure in the market or, in the case of French state reinsurer, Caisse Centrale de Reassurance, pulled out entirely, as the secondary market braces itself to shoulder up to 80% of the total insured loss.

This means the capital fund capacity of international reinsurers, which Thai insurance firms have counted on for several years, is limited. Carriers need new capital, notsimply to pay claims but also to meet new capital rules implemented last year.

This is a clear opportunity for international insurers to move into, or strengthen their presence in, the Thai market. In March 2012 Canadian insurer Fairfax closed a deal to acquire a 25% interest in Thai Re for around US$70 million in what is likely to be the first of a number of deals in the country's embattled insurance sector.

A further catalyst for increased transaction activity is the decision by the Thai regulator, the Office of Insurance Commission, to increase foreign shareholding limits in insurers to 49% (or beyond, subject to special approval, which French insurer AXA is seeking as it looks to inject more cash into its existing Thai operations) as a way of helping many of the 67 non-life carriers operating in the sector to replenish funds and raise fresh capital in the wake of the flooding.

IAG is another insurer that has said that it will take advantage of likely consolidation within the Thai insurance sector and expand its presence in the market. IAG already offers insurance coverage in Thailand through its Safety Insurance and NZI Thailand brands, having acquired a stake in Safety Insurance in the late 1990s.

Taiwan

Taiwan is a highly saturated market, and the deal trend has been for domestic mergers to create better capitalised carriers. The largest deal last year was the sale by AIG of Nan Shan Life Insurance Co Ltd to Ruen Chen Invest Holding Co Ltd for US$2.2 billion, one of the year's biggest transactions.

Although the acquisition was driven in part by the conditions of AIG's bailout by the US government, this is the latest example of a long line of foreign insurers exiting Taiwan's insurance market, due to the high level of product guarantees and the downward pressure this places on margins. Taiwan's insurance trade has remained sluggish in the aftermath of the global economic crisis, with the market further restricted by previous business being secured at interest rates which are no longer sustainable for firms. New accounting rules that raise capital requirements on insurers, together with strict local regulators and general market volatility, have led many international insurance groups to question their continued presence in the country.

Vietnam

As manufacturing and other businesses look for an alternative to China for low-cost production, Vietnam is seeing an increase in foreign direct investment. Insurers are also maintaining a keen interest in the country, which has seen its general insurance market grow at a compound rate of 25% per annum since 2009 and is expected to continue at similar levels in the next three to five years.

In May 2012 IAG completed its acquisition of a 30% stake in Vietnam-based AAA Assurance Corporation (AAA). IAG managing director and CEO, Mike Wilkins, described the investment as a strategic stake that will deliver an exposure to the rapidly growing Vietnamese insurance market via an established participant.

In another significant move into Vietnam, driven by similar motives, Sun Life Financial Inc, a subsidiary of Sun Life Assurance Co of Canada, signed a joint venture agreement with PVI Holdings to form PVI Sun Life Insurance Co Ltd.

Vietnam is poised for more M&A activity in the coming years as large multi-national players seek to strengthen their presence in a market which still has a degree of over capacity; this may lead to the withdrawal of less successful businesses, or merger activity to create fewer, stronger players.