Key trends in the takaful sector: takaful market update

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As Takaful continues to grow and capture the attention of an ever widening group of investors the efforts to reach to a wider group of participants continues to increase. Malaysia remains at the forefront of Takaful, both in terms of size of contributions as well as depth and extent of regulations, combined with a strong presence of multinational insurers growing Takaful and incorporating international best practices in corporate governance to Takaful.

Malaysia

Malaysia remains predominantly family Takaful, with family making up over 75% of total Takaful contributions. Family contributions consist of a few main product types:

Regular contribution unit linked plans – these plans consist of a savings element but tend to have significant sales of protection riders such as medical riders in various forms such as major medical and surgical benefits as well as critical illness benefits on the life of the participant, the spouse or parents and waiver of contribution under critical illness of the payer. Also becoming popular now are early critical illness riders where benefits are paid out at an earlier stage of critical illnesses to allow better access to medical care when it is most needed. These plans are the largest in terms of Annual Contribution Equivalent (ACE, which is defined as 100% of regular contributions and 10% of single contributions). Multinational insurers tend to be relatively strong in this market segment.

Single contribution credit plans – these plans are tied to underlying bank loans and have traditionally been the largest component of new business. Growth continues to be steady and tied to the growth in Islamic bank loans. Not surprisingly the Takaful operators with Islamic banks as sister companies are particularly strong here, which tend to be local operators. Significant business also comes from government loans to civil servants as well as third party banks with no Takaful sister companies. The competition for obtaining exclusive distribution arrangements with third party banks in particular can be quite fierce. New business of unit linked and credit plans currently make up over 70% of new business.

Other plans – includes group term Takaful, regular contribution non-linked savings plans, group hospital surgical and other group plans.

Overall the new business in the family market, in terms of ACE is currently dominated by PruBSN and Etiqa. Prudential had early mover advantages due to its receipt of a Takaful license in 2006 whereas multinationals AIA/ING and Great Eastern received their licenses in 2010. There have been various recent mergers and acquisitions activities in the market recently - multinational MSIG took over from Tokio Marine in 2011, Sun Life took over from Aviva in 2013 and Metlife is now involved in Takaful via the purchase of AmFamily Takaful since 2014. For general Takaful, business is dominated by motor Takaful, with the second largest segment being fire followed by personal accident.

In 2014 a new Takaful scheme, i-Br1M, underwritten by the majority of Malaysian Takaful operators under BR1M was introduced. BR1M is a government scheme whereby Malaysian households with an income of MYR 3,000 (USD 952) and below per month receive MYR 700 (USD 222) from the government and those earning MYR 3,000 (USD 952) to MYR 4,000 (USD 1,269) receive MYR 500 (USD 159). Out of this, MYR 50 (USD 16) is used for the Takaful coverage, which includes MYR 30,000 (USD 9,518) accidental death and total permanent disability coverage and MYR 1,000 (USD 317) natural death coverage. This scheme is available to households with dependents only rather than single recipients, who receive MYR 300 (USD 95) from the government if their income is MYR 2,000 (USD 635) or below but receive no Takaful coverage. This Takaful coverage both raises awareness for Takaful in general as well as the need for micro Takaful.

In the February 2014 issue of Takaful and Mutuality, Zainal Abidin Mohd Kassim and Farzana Ismail discussed various regulations being introduced and revised in Malaysia. Operators continue to revise strategy and plans as a result of these new regulations. For instance in preparation for the split of composite licenses into family and general, operators are determining if it is feasible to run its general Takaful operations on its own or if this license should be sold off. Issues include the scarcity of talent which will be exacerbated by the split of licenses, the impending detariff of the motor and fire business

and its effect on profitability and need for general Takaful pricing tools and the potential inclusion of general Takaful operators into the motor insurance pool (MMIP).

With respect to the risk based capital guidelines (RBCT), as capital levels are now directly related to the risks being taken including mismatch of assets and liabilities, operators are now determining how to maximize its use of capital, using asset liability management (ALM). ALM presents a particular challenge for operators as beyond any contractual guarantees there are implied guarantees in credit policies in particular.

Bahrain

Changes in the insurance rulebook in April 2014 have significantly increased the level of professionalism required of the Takaful industry. **These changes include:**

- A Financial Conditions Report (FCR) is now required each year for family Takaful. This requires the actuary to assess various aspects of the operations, ensuring the business is solvent and healthy. The actuary must go beyond simply providing a yearly valuation of liabilities to reviewing its methodology, assumptions, quality of data and sensitivity of assumptions. Capital adequacy, ALM and Retakaful arrangements must all be assessed. For any issues which could have an adverse effect on the solvency of the operator remedial measures must be recommended. One particular implication of the FCR is that the operator should ensure yearly under current assumptions that the contribution rates are sufficient to cover claims cost and wakala fees and also ensuring that wakala fees are sufficient to cover management and distribution expenses.
- For general Takaful the statutory valuation is now required once every two years instead of three years.
- FCR is required for general Takaful once every two years.
- The actuary must certify the contribution rates are sufficient to cover claims cost and wakala fees and also checking that wakala fees are sufficient to cover management and distribution expenses. As this regulation has just come in force in April the actuary by right should certify all policies currently being sold as soon as possible, as well as whenever a new plan is launched. This should also be done yearly as assumptions change.
- The actuary must assess the solvency position of the participants' funds quarterly. This in effect means that actuarial valuations must be completed quarterly, both for family and general.

These changes mean the actuary now plays a central role in the operations of a Takaful operator, and must understand the nuances of Takaful.

Pakistan

In the 2005 Takaful rules, windows were explicitly forbidden for five years to allow Takaful operators time to develop. In 2012 Takaful rules allowed windows, but the existing Takaful operators brought the issue to court. In 2014 the issue was resolved and windows will now be a reality. This is good news for the large conventional insurers who are now preparing to launch Takaful. Windows do raise challenges in a pure Muslim country such as Pakistan. As awareness for Takaful grows, the corresponding awareness of the forbidden aspects of conventional insurance will also grow. Furthermore there is a significant risk of Takaful business cannibalizing conventional business. This is natural with an agency force in particular as agents trained on the Islamic aspects of Takaful may be hesitant to then sell conventional insurance to Muslims. With this in mind these conventional insurers will likely be under pressure by shareholders to ensure a consistent return on capital between Takaful and conventional products. This tends to be a challenge considering the surplus sharing nature of Takaful. A clear marketing strategy is essential to ensure Takaful is either in the same market segment as conventional insurance with unique products or in a different market segment altogether.

Africa

Kenyan-based Takaful Insurance Africa (TIA) has frequently been in the news over its declaration of surplus to participants which is rare in Africa as well as its innovative livestock Takaful plan. TIA in 2013 made its intentions known to expand into Somaliland, Somalia, Tanzania and Uganda before proceeding to Ethiopia and Rwanda. As part of this strategy TIA is now active in Somalia.

Considering the lack of insurance penetration in Muslim majority countries and a tendency of Muslims to avoid insurance in Muslim minority countries Takaful should continue to grow steadily, especially with the increasing awareness of Takaful and the growing appreciation of Takaful as insurance consistent with Muslim values rather than insurance strictly for Muslims.