

Malaysian Takaful Dynamics

A 30th anniversary preview edition

November 2014



Message from the Malaysian Takaful Association's Chairman



Zainudin Ishak
Chairman
Malaysian Takaful Association

A warm welcome to our 30th anniversary commemorative publication which reflects on Malaysia's takaful journey, from industry performance, market insights and consumer trends to our future directions and outlook.

Malaysia's three decades of takaful evolution has been characterized by steady growth of market participants, both players and agents, and infrastructure capacity building. The asset base of Malaysia's takaful industry has grown significantly to an estimated RM21 billion in 2013 from an initial asset base of just RM1.4 million in 1986.

We recognize that Malaysia's takaful industry is yet to reach its optimal market participation level and the Malaysian Takaful Association as the industry body, has embarked on various efforts to get Malaysian takaful to the top echelons of best practices.

We are also encouraged by Bank Negara Malaysia's support in creating a conducive environment for takaful to flourish with a resilient and ever-robust regulatory infrastructure - including

the development of the Takaful Operational Framework, Risk-based Capital for takaful and the new Islamic Financial Services Act 2013. These wide-ranging reforms will support the long-term sustainable growth of the industry with focus on enhancing operating flexibility, product disclosures, delivery channels and market practices for takaful operators.

In taking Malaysia's takaful to greater prominence, MTA has organized and participated in a number of strategic events, that encourage sharing of knowledge including, Konvensyen Perunding Takaful, Global Islamic Finance Forum and The Takaful Rendezvous, just to name a few.

My heartiest thanks and gratitude to everyone who has contributed to what Malaysia takaful industry has become today. We hope to garner your continued strong support in the golden years to come.

This special 30th anniversary edition is a preview of the full compendium *Malaysian Takaful Dynamics* planned for release in April 2015.

Message from EY Malaysia's country managing partner



Dato' Abdul Rauf Rashid
Country Managing Partner,
Malaysia, EY

I am delighted to see MTA celebrate their 30th industry anniversary and to witness the steady growth of Malaysia's takaful industry over these years.

Malaysia is fast gaining international recognition as a centre for product innovation and operational best practices.

Malaysia's takaful market, estimated at over US\$3.0 billion, has been on a dynamic growth track achieving double-digit growth momentum of about 19%. In addition, Malaysia has a leading position on family takaful with US\$1.4 billion in total net contributions.

The takaful industry has vast scope for continual improvement to raise industry performance standards to be on par with the conventional insurance industry and to accelerate the development of creative product innovation.

In today's highly dynamic and competitive market, the takaful industry must deliver a positive and lasting customer experience. With the growth of more sophisticated customers and their technology savviness, the industry needs to attract more skilled talent to support the financial sector.

Moving forward, the sustainability for Malaysia's takaful industry will demand the adoption of best practices and rapid adaptation to change in meeting customer needs.

We in EY look forward to continuing to play a key role in the development and growth of the takaful industry in Malaysia and globally in the years to come.

Finally, congratulations to the MTA team for their dedicated enthusiasm to drive takaful industry activities and to be at the forefront of the industry.

Vision, mission and milestones

Malaysian Takaful Association

VISION

Sustainably profitable and growing Takaful industry in Malaysia

An industry that can be trusted and recognized as contributing to society and the economy

An economic and public policy climate conducive to a flourishing industry

A trade body recognised as providing active leadership and an authoritative collective voice for the takaful industry

MISSION

To provide leadership on issues bearing on the industry's collective strength and image and to shape and influence decisions made by the Government, regulators and other public authorities, locally and internationally, to benefit the industry as a whole.

Objectives

▶ Promote and represent the interests of members and also the foundation of a sound takaful structure with cooperation.

▶ Represent the Malaysian takaful industry to government, regulators and policy makers in driving effective public policy and regulation, locally and internationally.

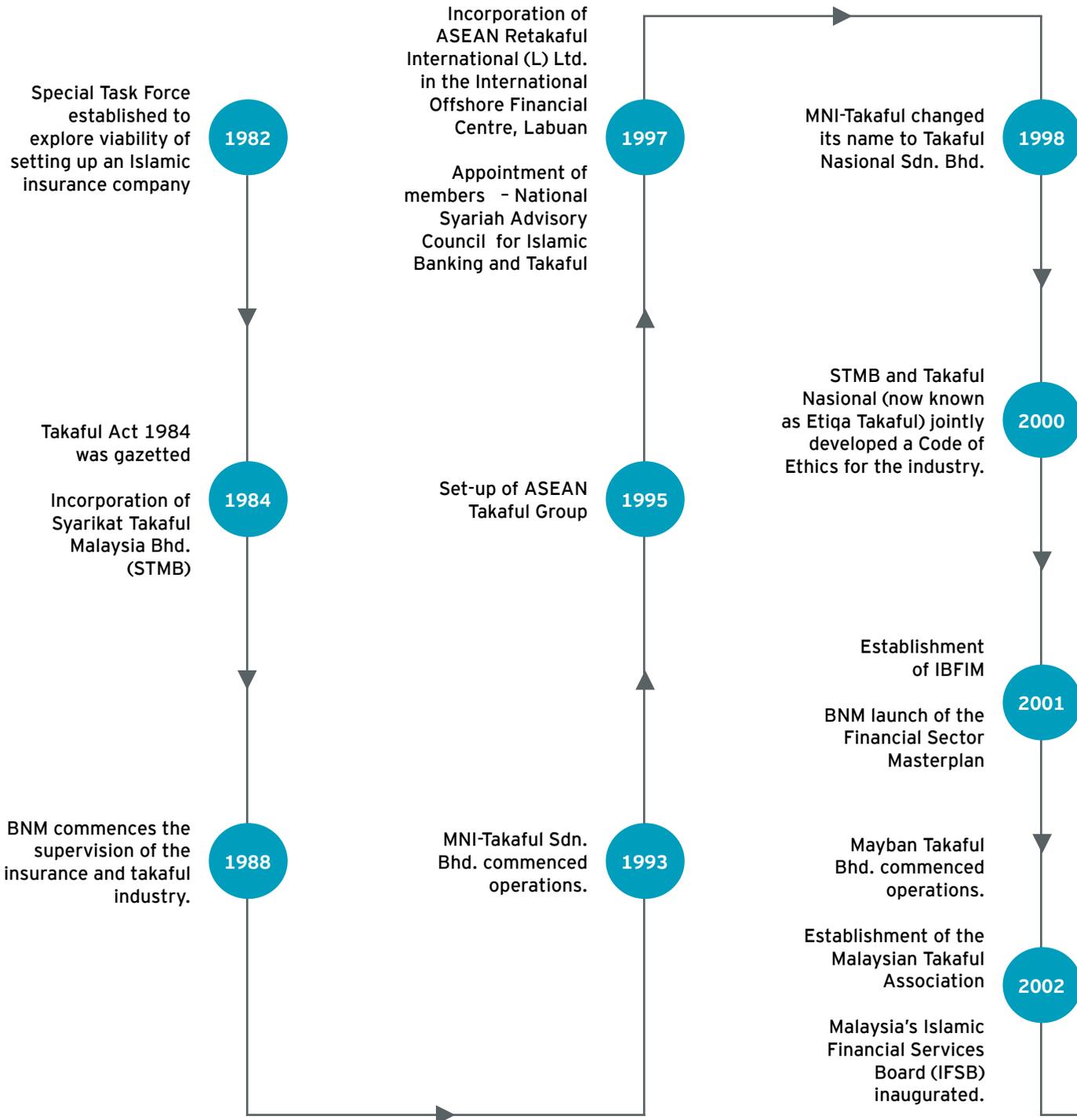
▶ Institute strategic alliances and cooperation with other similar associations both locally and internationally.

▶ Advocate high standards of services within the industry and provide useful information to the public about takaful.

▶ Promote the benefits of takaful to the government, regulators, policymakers and the public.

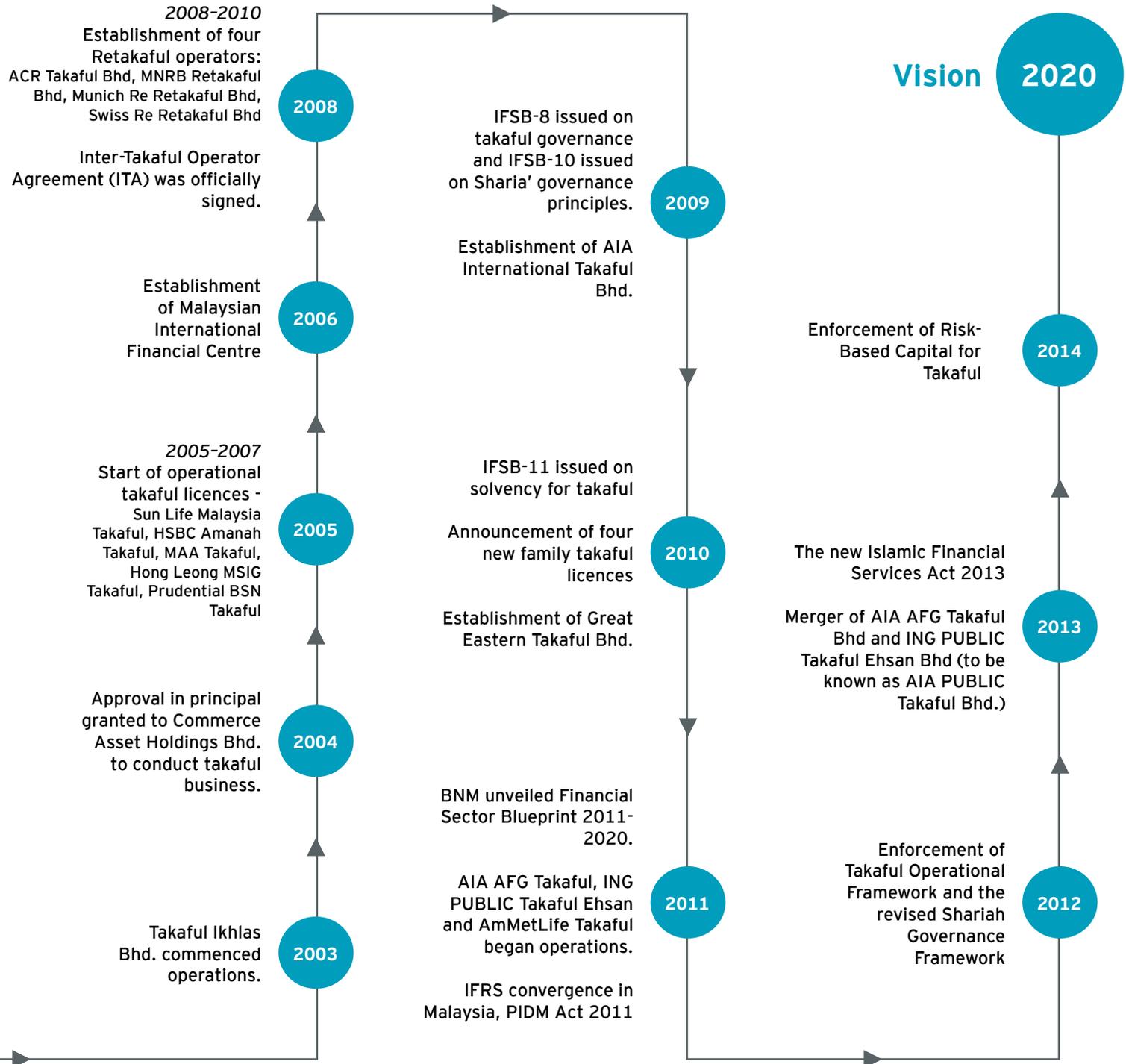
▶ Collect, collate and publish statistics and any other relevant information relating to takaful to members.

Key milestones of Malaysia's takaful industry



Note: Bhd. stands for Berhad

...celebrating 30 years together



Landscape

Markets

Quick insights

Business risks

Regulatory

Markets

Global and Malaysia's takaful markets

Double-digit global growth momentum

With the continued buoyancy in the estimated US\$2 trillion global Islamic finance markets, the global takaful market is estimated to continue its double-digit growth momentum of about 14% in 2014. Given a conducive growth landscape, the global takaful industry may reach over US\$20 billion in 2017.

However, in the short-term, undifferentiated strategies and wider regulatory compliance efforts have dented the short-term financial dynamics of takaful operators in some markets.

Challenging competition and regulatory scenario

Profitability of takaful operators in most Gulf Cooperation Council (GCC) countries continues to be challenged by intense competition. Consequently, some operators are looking at alternative customer segments and some are even exploring merger options.

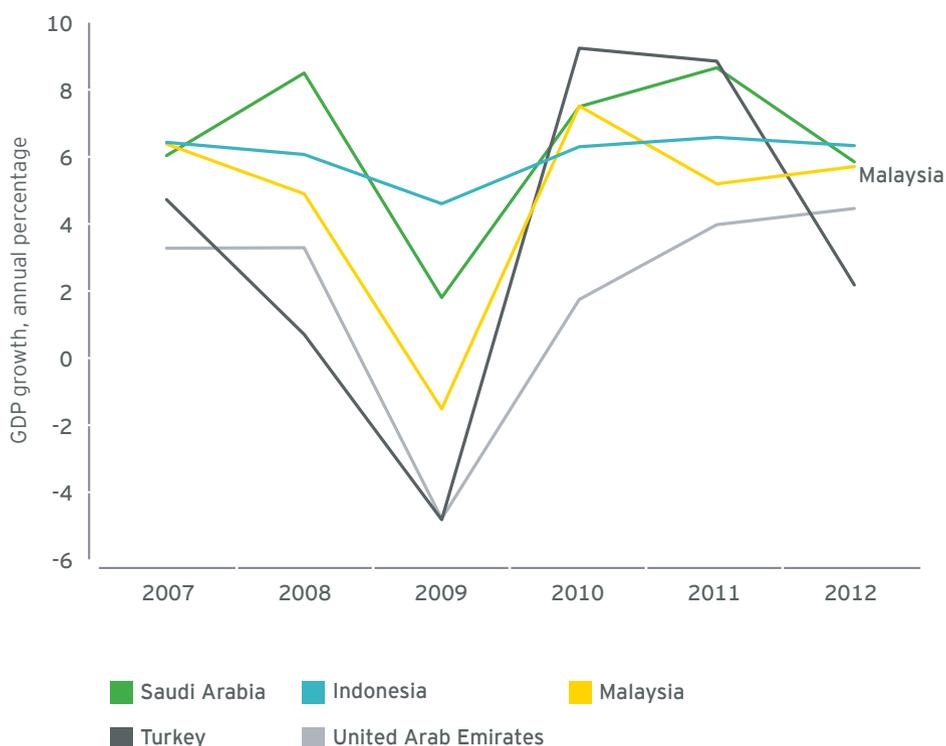
Industry players also observe the lack of uniform regulations which can allow them to operate across different takaful models as regional growth impediments.

Malaysia on steady growth traction and continual enhancements

Malaysia's total net contributions of family takaful reached RM4.5 billion (US\$1.4 billion) with steady growth from regular contribution products.

Takaful operators are also reviewing Bank Negara Malaysia's concept paper on the Life Insurance and Family Takaful Framework (LIFE) which recommends a wide range of enhancements from operating flexibility, product disclosure and delivery channels to market practices.

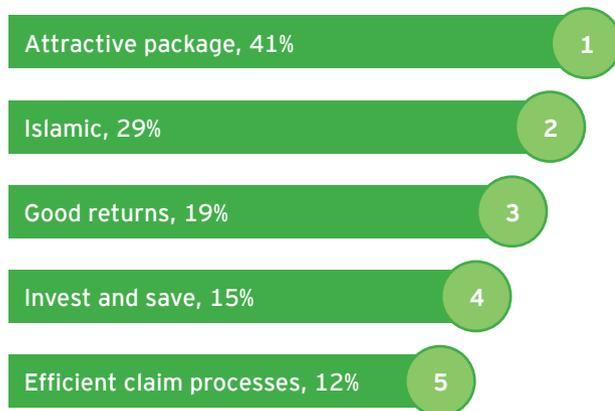
Chart 1: GDP growth of selected Islamic finance markets (annual %)



Quick insights

Malaysia's takaful industry

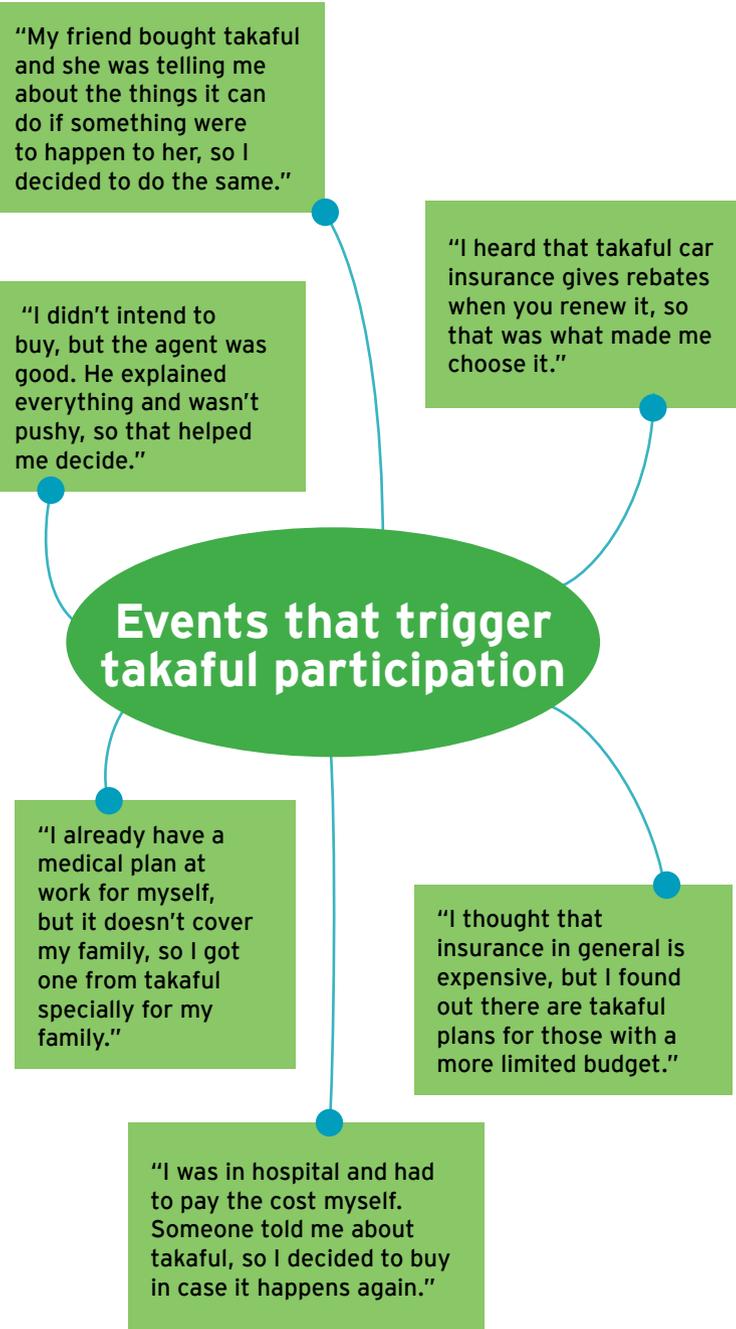
Top 5 reasons to consider takaful



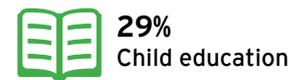
Main takaful customers are aged



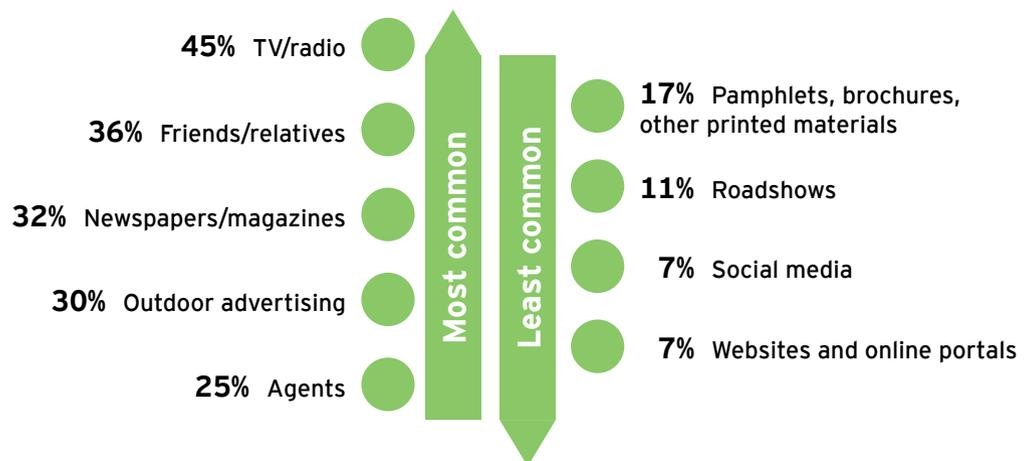
Events that trigger takaful participation



6 most popular takaful products



Overall source of awareness



8/10

Takaful customers are satisfied with services provided.

Gap findings	RM
Average gap per working person	200,000
Average sum assured for takaful policy	50,000
Age group with largest aggregate gap	Below 30 years old and/or those earning less than RM1,000 a month

Sources:

- ▶ *The Story of the Gap: Charting Takaful Growth in Malaysia*, Actuarial Partners, June 2014
- ▶ *Environment Scan on Takaful Awareness of Malaysian Youth*, Metrix Research, September 2014

Business risks

Addressing new and evolving business risks

The top three business risks for Malaysian-based takaful operators include:

- ▶ Evolving regulations
- ▶ Addressing competition
- ▶ Business transformation

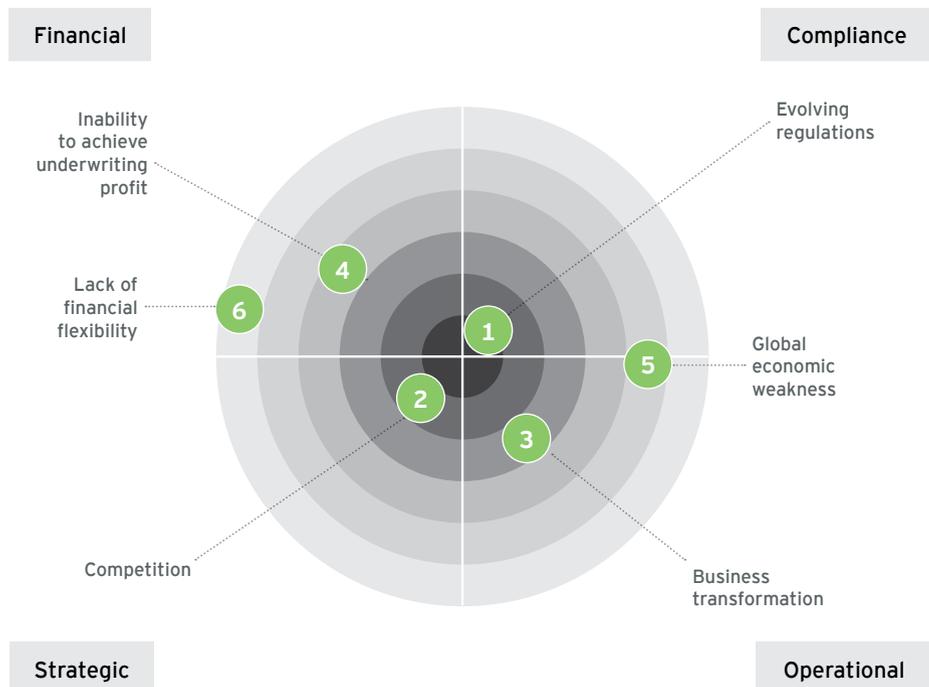
The ever-changing regulatory environment in Malaysia with the implementation of the Financial Services Act 2013 and Islamic Financial Services Act 2013; the enforcement of Risk-Based Capital for Takaful (RBCT) and other regulations; and the need for operators to comply with them accordingly were cited as the top business risks.

In addressing the new challenges and opportunities catalysed by technological challenges, Malaysian takaful operators are also reviewing their business models and are working out their business transformation strategies.

Business risk	Ranking 2014
Evolving regulations	1
Competition	2
Business transformation	3
Inability to achieve underwriting profit	4
Global economic weakness	5
Lack of financial flexibility	6

Business risk	Ranking 2014
Ineffective enterprise risk management	7
High-risk investment portfolios	8
Misaligned cost base	9
Rated retakaful shortage	
Political risks and implications	10 & 11
Hostile M&A activity	12

Chart 2: Top six takaful business risks in Malaysia



Regulatory

Life insurance and family takaful framework

Background

Bank Negara Malaysia's (BNM) concept paper on the life insurance and family takaful framework sets out proposals that will support the long-term sustainable growth and development of the industry with increased value propositions to consumers.

Scope

The proposals cover a wide range of areas:

- ▶ Operating flexibility
- ▶ Product disclosures
- ▶ Delivery channels, and
- ▶ Market practices

The initiatives, once finalized, will be reflected in the relevant documents to be issued under the Financial Services Act 2013 (FSA) and Islamic Financial Services Act 2013 (IFSA).

Applicability

This proposed framework will be applicable to:

- ▶ Life insurers licensed under the FSA
- ▶ Family takaful operators licensed under the IFSA
- ▶ Financial advisers and Islamic financial advisers approved under the FSA and IFSA

Future landscape

The framework has been introduced to transition the life insurance and family takaful industry into a new environment with the aim of achieving a higher insurance and takaful penetration rate of 75% (2013: 54%) while at the same time ensuring that consumers continue to receive proper advice. This entails having in place several initiatives broadly summarized as follows:

- ▶ Allow greater operational flexibility to promote product innovation while preserving policy/certificate value
- ▶ Diversified distribution channels to widen outreach
- ▶ Strengthen market conduct to enhance consumer protection

The framework promulgates a two-phase approach to ensure orderly implementation of the proposed recommendations.

Phase 1: Partial liberalization for better preparedness pending further liberalization

Partial removal of operating limits

- ▶ Operating cost limits of investment-linked products in the form of commissions, management expenses and agency related expenses will be removed immediately.
 - ▶ To preserve policyholder's value, a certain percentage of the premium/contribution payable must be allocated to the policyholder's/ participant's unit fund before any deduction of charges.
- ▶ Commission limits for pure protection products (pure term, medical and health insurance takaful, and critical illnesses) to be removed, subject to insurers and takaful operators offering those products via direct channels.

Diversification of distribution channels

- ▶ Bancassurance/Bancatakaful commission limits will be aligned with corporate agents.
- ▶ Incentivizing growth of financial advisers through:
 - ▶ Reduction in paid-up capital from RM100,000 to RM50,000
 - ▶ Expansion of list of qualifications to become financial advisers
 - ▶ Requirement for insurers and takaful operators to offer entire range of products for financial advisers to sell

Strengthening market conduct practices to enhance customer protection

- ▶ Intermediaries, remuneration based on a balanced scorecard
- ▶ Enhanced disclosure standards for greater consumer empowerment and awareness
- ▶ Introduce product aggregator to assist product comparison
- ▶ Introduce online insurance/ takaful account to promote awareness of policy status
- ▶ Removal of agency financing scheme limits

Key KPIs to be achieved

- ▶ Premium/contribution level of products liberalized to commensurate with benefits to policyholders/participants
- ▶ Commission-free pure protection products sold via direct channels to be cheaper than sold by intermediaries

- ▶ Availability of pure protection products via direct channels
- ▶ Market share of regular premiums for non-agent channels to be 30% (current = 14%) with higher persistency
- ▶ Banca penetration target of 10% of banking population (current = 5%)

- ▶ Scorecard for intermediaries' rating
- ▶ Number of full-time agents to be 50%

Continuous consumer education efforts

Phase 2: Full/managed liberalisation subject to achievement of KPIs and BNM's assessment

Sources:

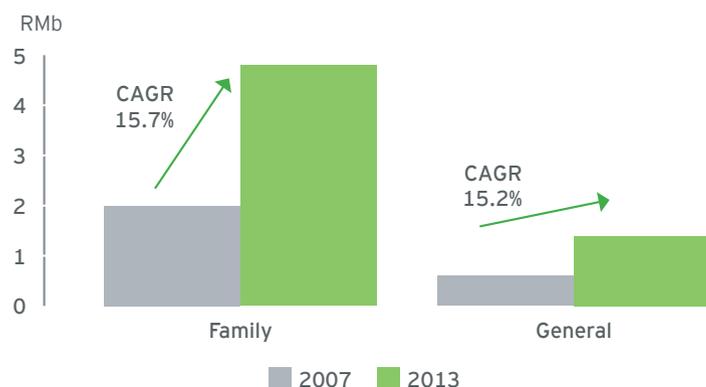
- ▶ Life Insurance & Family Takaful Framework: Concept Paper, BNM
- ▶ EY analysis

Performance

Industry performance

Takaful growth powers steadily at double-digit mode

Chart 3: Net contributions income by takaful segment

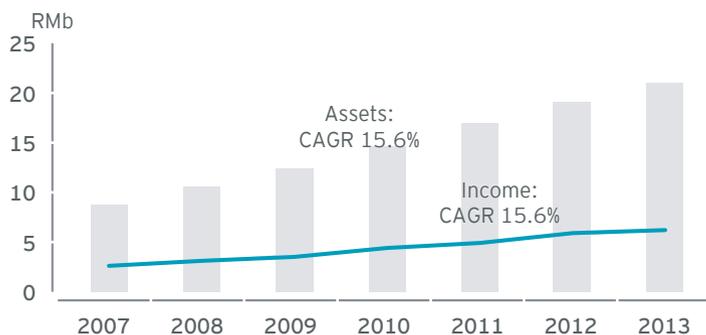


Over six consecutive years, double-digit net contributions income growth:

15.7% CAGR for family takaful
15.2% CAGR for general takaful

Growth magnitude:
2.4 X's for family takaful
2.3 X's for general takaful

Chart 4: Takaful – net contributions income and fund assets



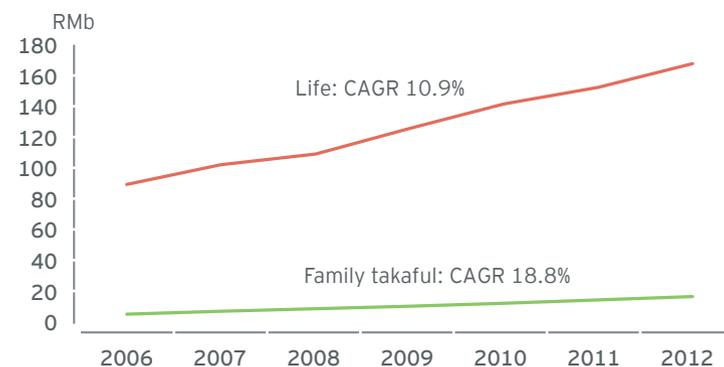
■ Takaful fund assets (RMb)
■ Net contributions income (RMb)

Double-digit CAGR, six consecutive years

15.6% CAGR for takaful net contributions income

15.6% CAGR for takaful fund assets

Chart 5: Fund assets – Family takaful and life insurance



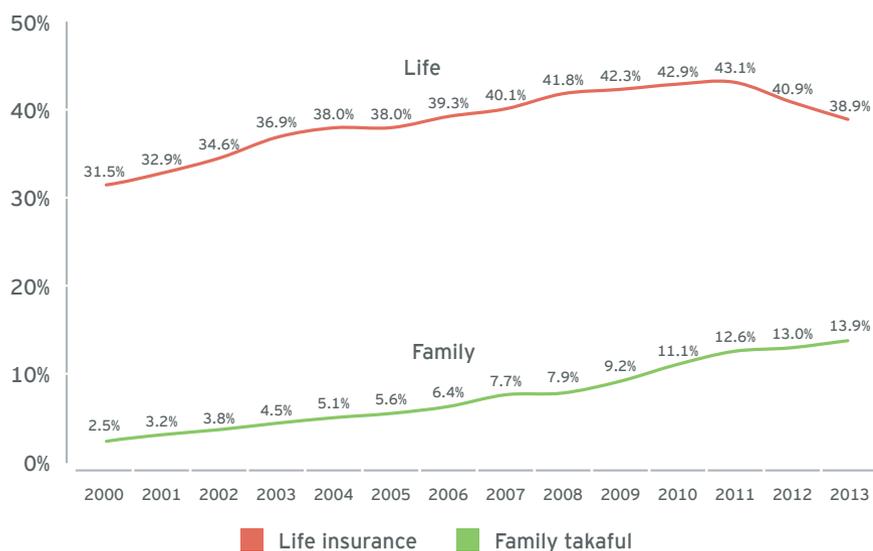
■ Life insurance
■ Family takaful

Family takaful assets growth rate is 1.7 times that of the life insurance industry, albeit from a low base.

18.8% CAGR for takaful's fund assets (vs. 10.9% for life insurance)

Note: Family takaful's fund asset is RM18b as at December 2013.

Chart 6: Market penetration rate*



The takaful industry’s market penetration rate* of 13.9% compared to the overall insurance and takaful industry rate of 52.8% reflecting significant untapped potential. The target of the Financial Sector Blueprint in 2020 is 75%.

Below optimal market penetration rates

Conventional insurance: 38.9%

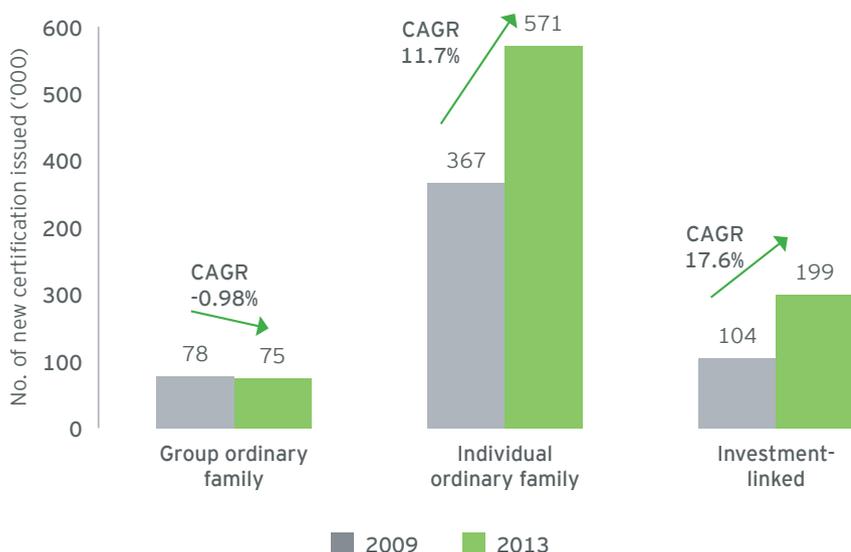
Takaful: 13.9%

Long-term target penetration rate: 75%**

*The total number of life insurance policies or family takaful certificates divided by the total Malaysian population.

**This long-term target penetration rate is for conventional insurance and takaful.

Chart 7: New takaful certificates issued by products



- ▶ From 2009 to 2013, the take-up of new individual ordinary family takaful certificates rose by 11.7% per annum whilst group ordinary family takaful tapered by about 1% per annum (CAGR 0.98%).
- ▶ Exponential growth is recorded in investment-linked takaful certificates which experienced 17.6% growth.

Source:

▶ Data on Malaysian Takaful Industry, Malaysian Takaful Association

Financial dynamics

Despite competitive challenges, Malaysian takaful operators achieved healthy financial results.

Chart 8: Average profit margin

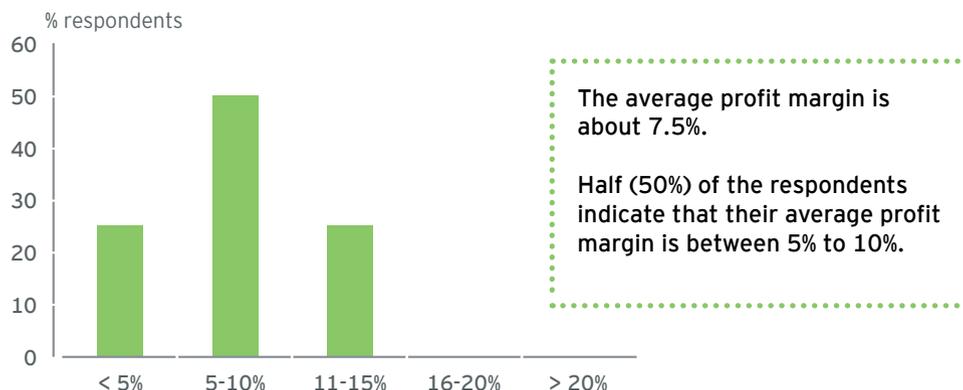


Chart 9: Average commission ratio

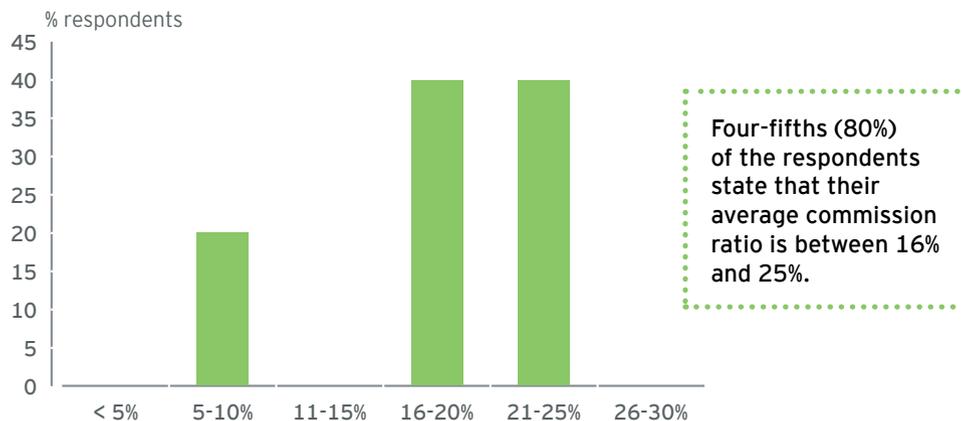
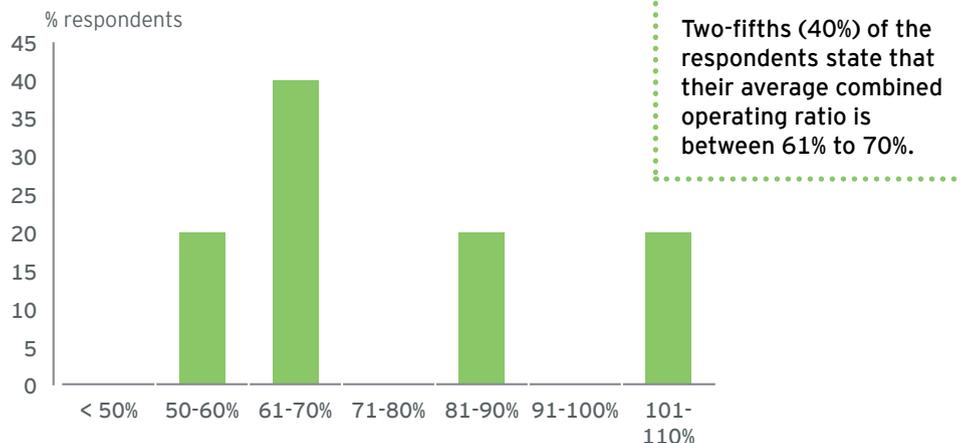


Chart 10: Average combined operating ratio



Source:
► Global takaful online survey 2014, EY

Outlook

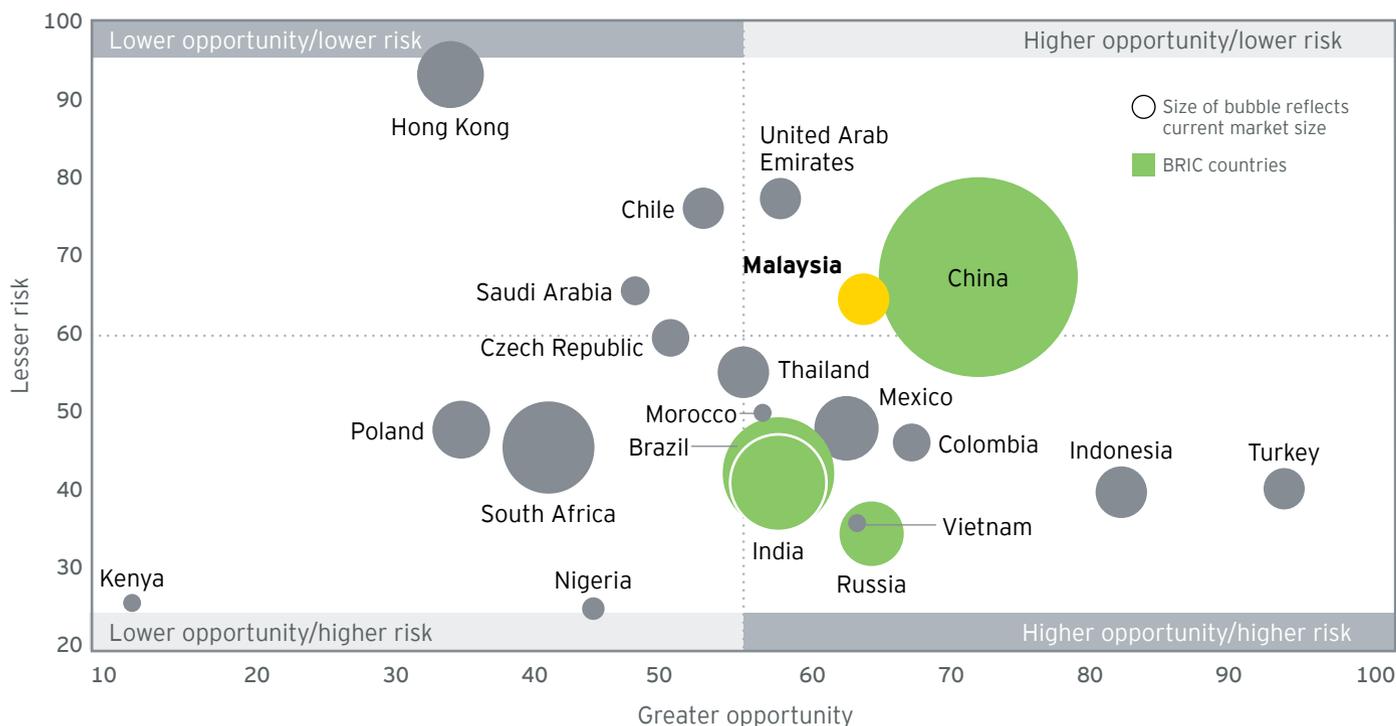
Malaysia, a leading takaful rapid-growth market

Demographic shifts and regulatory developments in rapid-growth markets (RGMs) are driving global insurers to re-assess which RGMs present highly attractive investment options. EY's recent global insurance study, *Waves of change* has identified Malaysia as a market with an attractive mix of demographics, strong economic growth and a strategic base for the development of takaful. Malaysia was ranked alongside China as a country with higher opportunities and moderate risks.

Industry regulatory initiatives led by Bank Negara Malaysia to encourage the industry's adoption of best practices and initiatives by the Malaysian Takaful Association are steps in the right directions towards accelerating the internationalization of Malaysia's takaful industry.

With Malaysia's high potential to take the lead in the internationalization of takaful, there is urgency for Malaysia to realize this aspiration by growing strong domestic players to become regional champions and winning opportunities in Asia's diverse and dynamic markets.

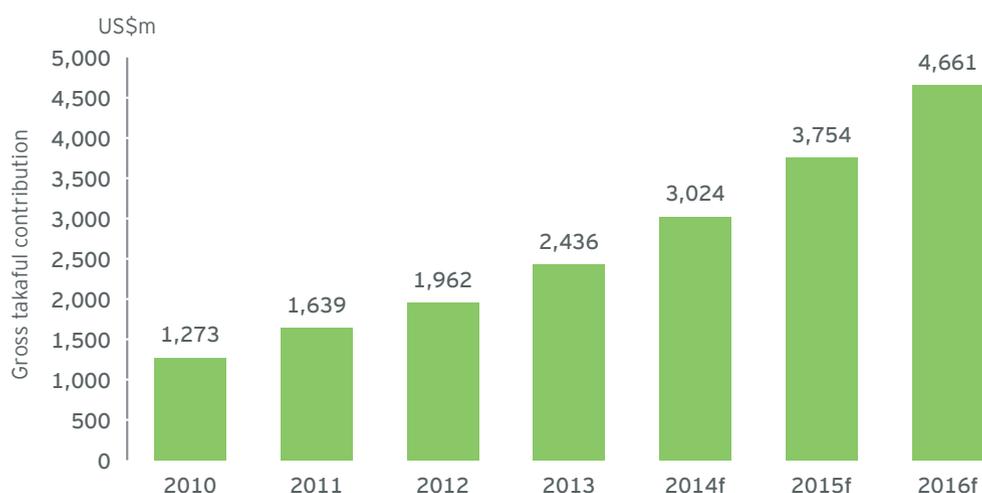
Chart 11: Matrix of opportunity and risk for insurance investments



Source:
 ▶ *Waves of change: The shifting insurance landscape in rapid growth markets*, EY, August 2014

Malaysia takaful: growth forecasts

Chart 12: Malaysia takaful contributions forecast, 2010-16f



In tandem with its takaful peers across the world, prospects for the Malaysian takaful industry continue to ride on the growth of the Islamic banking and finance sector.

Over the last five years, Malaysia's takaful industry achieved admirable CAGR growth of 24%.

Industry estimates indicate that given a conducive economic climate and its young demographics, Malaysia's takaful industry may be able to continue its double-digit growth path.

Across the world, it is pertinent to note that despite takaful's strong growth in key ASEAN and GCC markets, the insurance penetration rates in Islamic finance key markets are comparatively low and present significant untapped potential .

In the medium to long term, takaful operators in markets with stable domestic economies, good macro management and sizeable young Muslim populace can look towards capturing profitable opportunities in niche market segments.

Source:
► *Global Takaful Insights 2014*, EY, 2014

Long-term growth factors

Moving forward, the key forces of change that will drive and shape the future of the Malaysian takaful industry include:

Customer's technology adoption

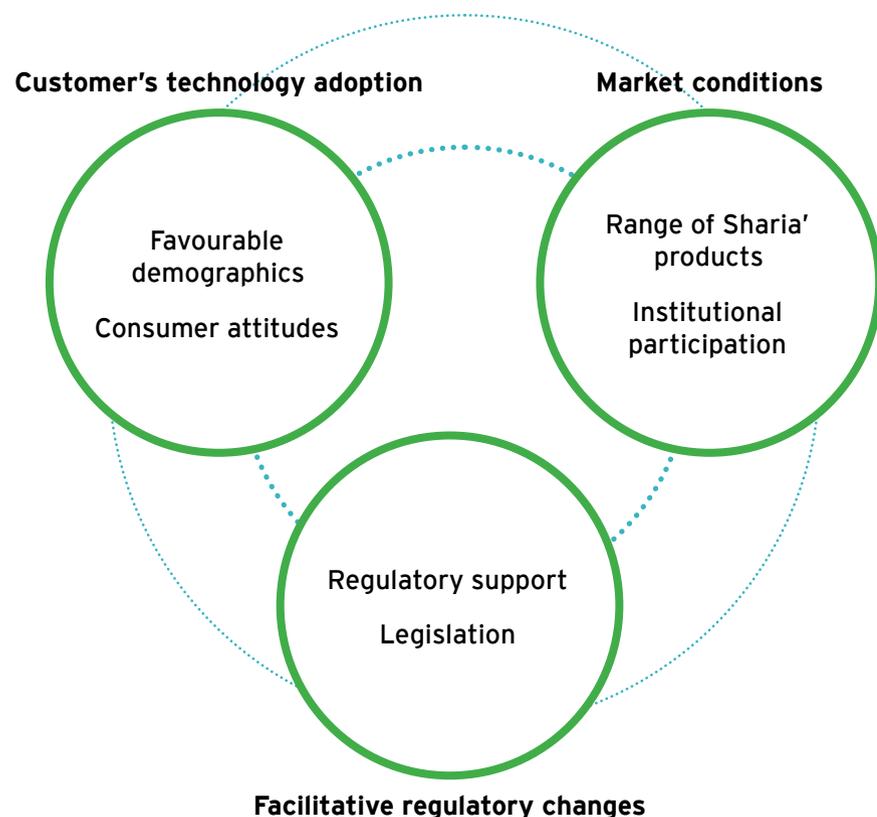
Aside from market demographics, the rise of social media and their influence on the buying attitudes of youths and even businesses provide both opportunities and risks to takaful players.

Market conditions

The state of innovation and communication of Sharia' compliant products, and the level of participation of institutions in promoting takaful products can drive the market participation of takaful .

Facilitative regulatory changes

Continued efforts to strengthen Malaysia's regulatory infrastructure such as the introduction of Risk-based Capital for Takaful provides better consumer protection and confidence to encourage takaful take-up. In addition, fiscal tax incentives for takaful products and welfare schemes (e.g. i-BRIM) can facilitate wider takaful participation.



Taking 6 actions

To ride through market challenges and realize takaful's market potential, operators need to:

1. Attune strategies to potential regulatory changes and develop plans before new rules take effect
2. Closely track consumer behaviours and rapid technological change in specific markets
3. Follow and anticipate changing government attitudes
4. Consider how macroeconomic trends can affect market(s)
5. Identify circumstances where shared service options can be applied
6. Acknowledge that local culture matters across markets

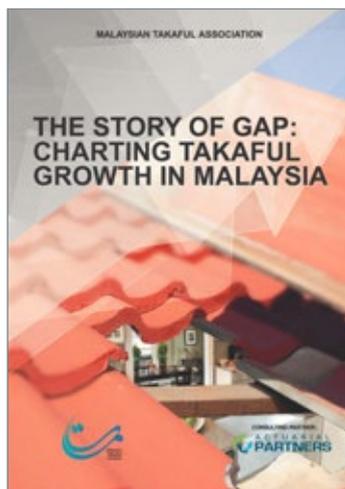
Source:

► *Waves of change: The shifting insurance landscape in rapid-growth markets*, EY, August 2014

References

Malaysian Takaful Association references

Publications



The Story of Gap:
Charting Takaful Growth
in Malaysia



Environment Scan on Takaful
Awareness in Malaysia



Annual Report 2013

MTA's online library

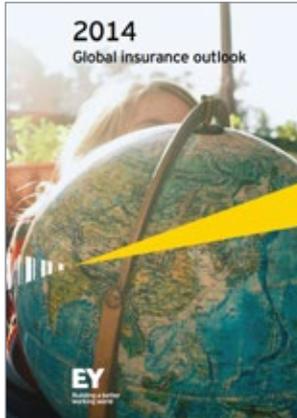
Consumer Education Series

- ▶ Motor takaful
- ▶ Family takaful
- ▶ Investment-linked takaful

Guidelines

- ▶ Code of ethics for takaful agents
- ▶ Guidelines on Replacement of Family Takaful Certificates (ROC) - inter takaful operator procedures
- ▶ Guidelines on the Continuing Professional Development (CPD) hours

EY thought leadership



2014 Global insurance outlook



Waves of change: the shifting insurance landscape in rapid-growth markets



Rapid-growth markets: EY rapid-growth markets forecast



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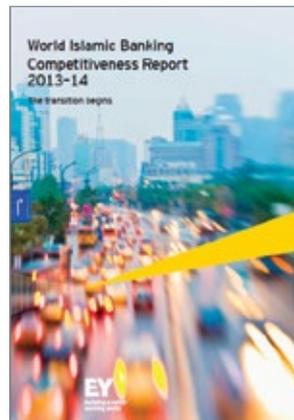
EY Insights is available on Apple App Store and Google Play.



Global Takaful Insights 2013: Finding growth markets



Take 5: Financial Services Act 2013 and Islamic Financial Services Act 2013



World Islamic Banking Competitiveness Report 2013-14: the transition begins

Malaysian Takaful Association contacts



*Azli Munani
CEO/Executive Secretary
Malaysian Takaful Association
+603 2031 8160
azli@malaysiantakaful.com.my*



*Tuan Azza Afif Tuan Yusof
Head of Corporate Services
Malaysian Takaful Association
+603 2031 8160
tuanazza@malaysiantakaful.com.my*



*Mohd Nazmi Hosnih
Head of Technical
Malaysian Takaful Association
+603 2031 8160
nazmi@malaysiantakaful.com.my*

EY contacts



*Brandon Bruce
Partner, Financial Services
EY Malaysia
+603 7495 8762
brandon.bruce@my.ey.com*



*Ahmad Hammami Muhyidin
Director, Financial Services
EY Malaysia
+603 7495 8929
ahmad-hammami.muhyidin@my.ey.com*



*Pearlene Cheong
Director, Research & Creative Services
EY Malaysia
+603 7495 8638
pearlene.cheong@my.ey.com*



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