THE INSURANCE AND TAKAFUL SECTOR

The insurance and takaful sector registered higher profitability, driven by stronger equity investment performance

Insurance and takaful funds recorded higher profitability in the second half of 2020 compared to the same period in 2019, driven by stronger investment performance of life insurance and family takaful funds. Excess income over outgo more than doubled to RM16.8 billion (2H 2019: RM7.7 billion) on the back of gains from equity and bond investments (Chart 2.18). In the life and family takaful sector, underwriting performance was sustained despite a markedly slower growth in new business premiums[15] (9.2%; 2H 2019: 18.4%) (Chart 2.19). This reflected the lower demand for mortgage insurance and takaful products amid weaker property market conditions in the second half of 2020 compared to the same period in 2019. Takaful operators have higher exposures to the Mortgage Reducing Term Takaful (MRTT) business and were therefore more affected than conventional insurers. Overall net premium growth remained below pre-COVID-19 levels but has picked up since the first half of the year, mainly due to higher growth in new investment-linked business premiums (23.6%; 1H 2020: -25%; 2H 2019: 10.9%). Insurers and takaful operators (ITOs) have observed that Malaysians are increasingly aware of the importance of insurance and takaful products in providing financial protection. This has continued to support demand for insurance despite renewed containment measures in the second half of 2020 and early 2021.

In view of the resurgence in COVID-19 cases and the reintroduction of MCO in most states in early 2021, ITOs have extended[16] the option for affected consumers[17] to defer premiums due under life insurance policies and family takaful certificates for three months without affecting the coverage. This option is now available for applications received until 30 June 2021. The impact of the temporary relief measures on ITOs' profitability has been limited as the cumulative amount of premiums deferred and on holiday[18] remained minimal at 7.7% of premiums in force. Total net policy benefit payouts have also remained largely stable. In 2021, total net policy benefit payouts could increase due to additional costs associated with COVID-19-related procedures and treatments that are incidental to covered conditions. However, the impact of this is expected to remain manageable. While death due to the COVID-19 pandemic is claimable under all life insurance policies and family takaful certificates, the low mortality rate observed among COVID-19 patients in Malaysia (0.4%; global: 2.2%)[19] will likely limit the impact from any additional death claims. Medical and health insurance policies/takaful certificates (MHIT) in Malaysia generally carry a pandemic exclusion clause in line with practices globally. These exclusions reflect the complexity of pricing for such events due to the incalculable impact and costs, an absence of viable risk diversification instruments for ITOs, and to avoid significant premium hikes following a pandemic event.

Some ITOs have made adjustments to their re-pricing plans in 2020 to reduce the financial burden on policyholders and preserve their MHIT coverage. These adjustments include deferring re-pricing plans to 2021, providing refunds to minimise the impact of price increases, and permitting extended deferral of premiums. ITOs are expected to be able to comfortably support the financial impact of these adjustments without affecting their overall resilience in the short term. Nevertheless, deferment of re-pricing over an extended period will not be financially sustainable for both the MHIT providers and policyholders as over the longer term, medical claims would reflect the underlying trends in medical inflation. Medical claims in 2021 are

15 Refers to both premiums and contributions, unless otherwise stated.
16 The three-month premium deferment option that was announced in March 2020 and expired on 31 December 2020.
17 Affected consumers are individuals who have been infected, home quarantined or suffered a loss of income; and SMEs which have suffered a loss of income, as a result of the economic impact of COVID-19.
18 Premium holiday refers to continued insurance/takaful coverage despite an absence of premium payments and applies to products with the premium holiday feature already in place such as investment-linked products. This flexibility is available to policyholders as long as the investment value in the unit fund remains sufficient to meet the necessary insurance cost during the holiday period.
19 Based on the cumulative number of cases and deaths reported by the World Health Organization as at 23 March 2021.

expected to increase compared to 2020 as a result of the resumption of treatments and procedures that were earlier delayed by policyholders due to COVID-19 concerns. Thus, further delays in re-pricing plans can lead to much steeper premium increases or reduced capacity of the industry to provide coverage in the future.

General insurance and takaful funds recorded higher operating profit, supported by better underwriting results as claims paid declined (Chart 2.20), mainly due to lower motor claims during the movement control period. Meanwhile, growth of gross direct premiums was sustained (2.8%; 2H 2019: 2.8%) (Chart 2.21). Motor premiums grew at a faster pace, supported by higher car sales in the second half of 2020 that was bolstered by the introduction of sales tax incentives. Under the phased liberalisation of the motor and fire tariffs, premium rates continued to adjust in line with policyholder risk profiles and recent loss experience. Based on recent motor claims data, certain theft-prone models and the younger drivers' segment consistently recorded higher than average loss experience, while new cars tended to be below the average. Several providers also reduced rates significantly for the optional 'special perils' coverage that provides protection against vehicle damage due to flood events. In 2020, the premiums for 56% of private car comprehensive and third party fire and theft policies were higher than under the tariff, while 38% of rates were lower. Over 95% of policies experienced premium rate adjustments that were within 10% of the previous tariff rates. While these adjustments may be insufficient to achieve technical pricing[20] levels for some risks, this is in line with the current phase of liberalisation. The phased approach aims to avoid sharp adjustments that would otherwise occur, particularly for motor risks where losses have persistently exceeded premiums for many years under the tariff. General ITOs also continued to introduce new products which are better tailored to meet customer needs and enabled policyholders to save on premiums, including usage-based motor policies which saw a two-fold increase in take-up, and products which provide flexibility for policyholders to select the coverage options that they need.

Meanwhile, personal accident premiums contracted as demand for travel insurance waned amid travel restrictions due to the pandemic. Claims from the floods in the east coast of Malaysia and several other states from late 2020 to early 2021 had a limited impact on general ITOs' profitability. Total gross claims from the floods were estimated to only account for 3.2% of general ITOs' operating profits for 2020.

Nevertheless, the insurance and takaful sector could face several challenges in the near future. ITOs continue to be exposed to heightened volatility in the financial markets from their sizeable bond and equity investments. The low interest rate environment also continues to pose challenges, especially for asset-liability management of life insurers and family takaful operators. Life insurers and family takaful operators generally operate with a negative duration gap given the lack of long-term financial assets available to match the duration of their liabilities (more than 15 years). Therefore, sustained periods of declining interest rates can have a detrimental impact on their solvency positions due to greater upward adjustments in the value of liabilities compared to assets.[21] A stronger recovery in new business growth will also depend on the easing of containment measures and a more entrenched economic recovery. Additionally, some general ITOs have indicated that they may face prospects of rising reinsurance costs during the next contract renewal following pandemic-related and natural catastrophe losses incurred by global reinsurers.

These developments could weigh on near-term profitability, but are unlikely to have a material impact on overall resilience. ITOs remain resilient, with strong capital positions. The aggregate capital adequacy ratio (CAR) stood at 219.7%, well above the regulatory minimum of 130% (Chart 2.22). Recent stress tests conducted also affirm that insurers are expected to have sufficient capital buffers to withstand potential shocks (refer to the section on stress test for insurers for further details).

[20] The level of premiums required to cover the actual claims experience of a group of similar risks and the relevant expenses incurred.

[21] While the impact could be amplified as asset and liability sensitivities, defined as the change in values of assets and liabilities from a 1% change in interest rates, tend to increase faster in a low interest rate environment partly due to the effects of convexity, the actual impact to the balance sheet would vary depending on the shape of the yield curve.

Chart 2.18: Life Insurance and Family Takaful Fund – Composition of Income and Outgo

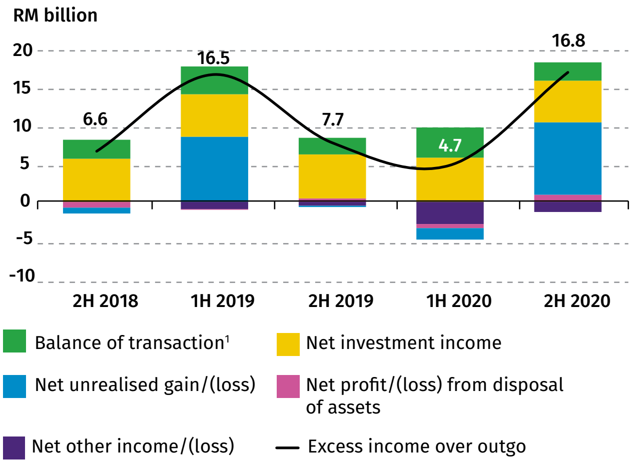


Chart 2.19: Life Insurance and Family Takaful Sector – New Business Premium Growth and Product Composition

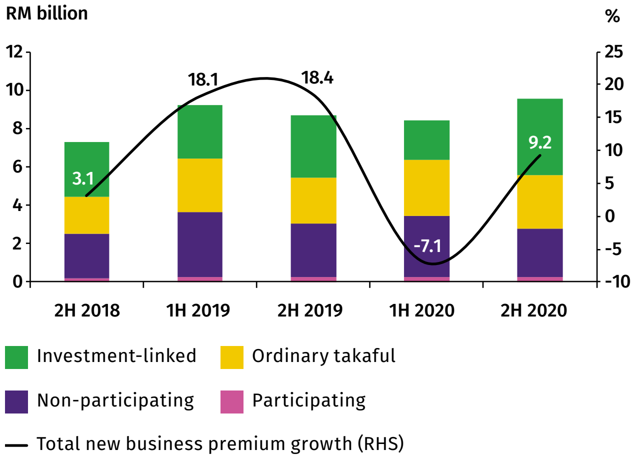


Chart 2.20: General Insurance and Takaful Fund – Composition of Operating Profits

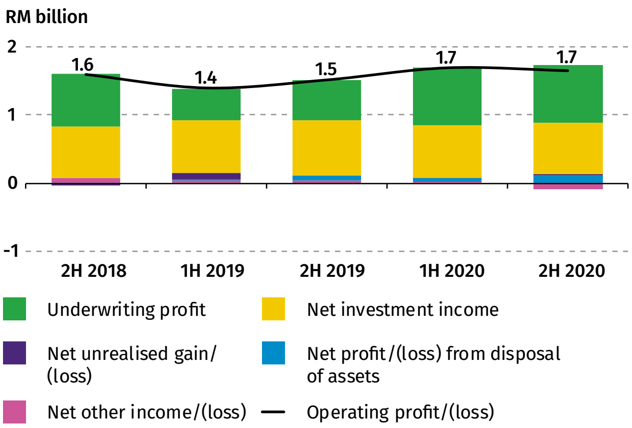


Chart 2.21: General Insurance and Takaful Sector – Gross Direct Premium Growth and Product Composition

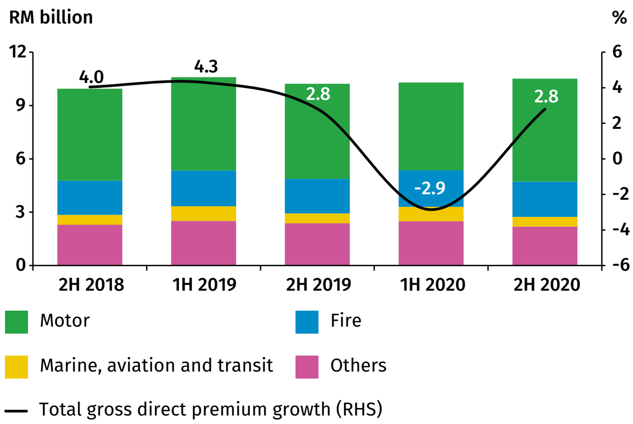
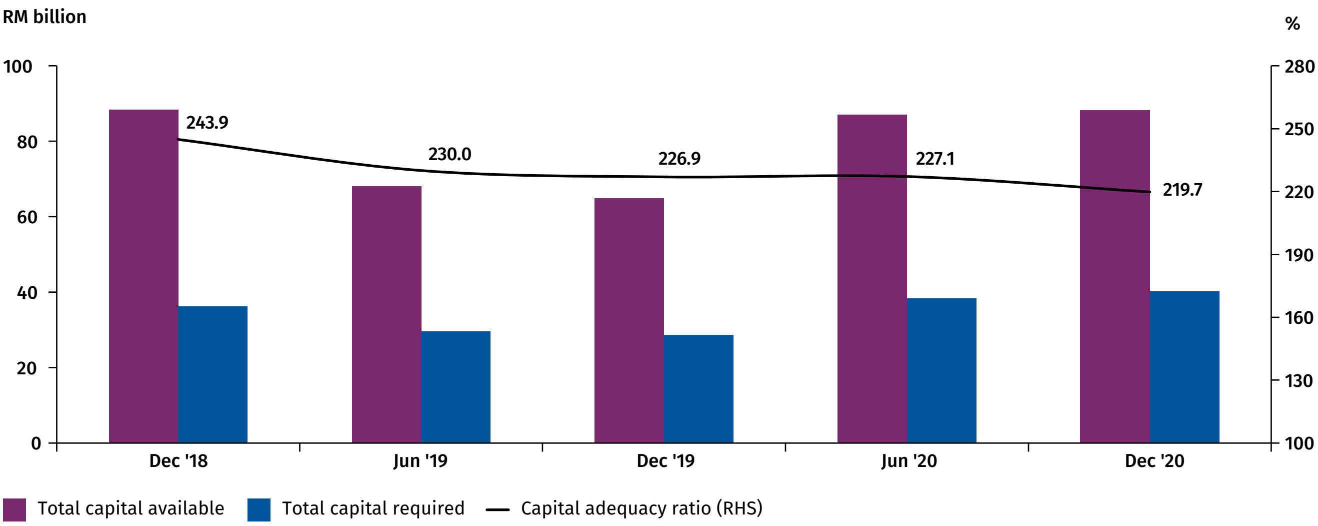


Chart 2.22: Insurance and Takaful Sector – Capital Adequacy Ratio



[1] Excess of net premium after deducting benefit payouts, agency remuneration and management expenses

Source: Bank Negara Malaysia