

## **Mohd Razif bin Abd Kadir: Our strategy towards developing a progressive takaful industry**

Keynote address by Mr Mohd Razif bin Abd Kadir, Deputy Governor of the Central Bank of Malaysia, at the official launch of AIA AFG Takaful Bhd. (a joint-venture company between American International Assurance Bhd. and Alliance Bank Malaysia Berhad), Kuala Lumpur, 28 January 2011.

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It is indeed an honour to be here this morning to commemorate the launching of AIA AFG Takaful Bhd. This occasion marks another accomplishment in the takaful industry in Malaysia, with the collaboration between two major players from the banking and insurance sector; American International Assurance Bhd. and Alliance Bank Malaysia Berhad, in forging a strategic alliance aimed to attain synergistic benefits that are of mutual business advantage. As we continuously position ourselves towards achieving a dynamic, competitive and efficient Islamic financial system that is able to contribute to the overall development of our economy, the launching of AIA AFG Takaful Bhd. is another important milestone in our strategy towards developing a progressive takaful industry that is resilient and is better able to meet the increasingly challenging and competitive business environment. I therefore wish to congratulate both partners on this momentous event.

The evolution of the takaful industry in Malaysia has been a progressive one since its inception more than two decades ago. We have witnessed significant progress amidst the orderly development of the takaful industry, which growth is underpinned by the holistic and pragmatic approach taken in developing the Islamic financial industry. The market has become more diverse, as there has been tremendous increase in the number of takaful operators operating in Malaysia, where from having a single takaful operator in 1984, we now have 9 takaful operators, 4 retakaful operators and one international takaful operator. In Labuan International Business and Financial Centre, there is also strong presence of the takaful industry, where its takaful market comprises 14 retakaful operators. The market segment for takaful has also widened over the years to meet the financial needs of the economy as its appeals and value propositions have transcended beyond religious reasons. Product offerings by takaful operators have further broadened to cater to the differentiated needs of customers, with family takaful products now dominating the market with a share of 78 percent of net contribution, as compared to general takaful products that dominated a share of 63 percent back in 1984.

The takaful industry exhibits high potential, as demonstrated by its robust expansion with annual growth rate of total assets and contributions averaging between 20 percent and 26 percent over the period of 2004 to 2009. Globally, Malaysia also signifies its presence in the takaful market, being the second largest takaful market in the world as its total assets of US\$3.2 billion dominated 26 percent of total global takaful assets in 2009. Whilst sustaining the current pace of development, growth prospect remains strong for the takaful sector, in view of the large untapped potential, where out of the 53.5 percent market penetration rate for both takaful and insurance, the market penetration rate for takaful was merely 10.9 percent in September 2010.

The takaful industry indeed represents an important component in the overall Islamic financial system. Given its role in providing risk protection, the takaful industry offers a suite of financial products and services that complement the existing range available for consumers. In recognising its importance, focus has been given in developing a dynamic and vibrant takaful industry within our Islamic financial system. Where the industry is today has been an outcome of an accumulation of efforts in instituting a comprehensive Islamic financial landscape in Malaysia's financial system. A strong institutional infrastructure and effective legal, regulatory and Shariah framework are the underpinnings of our Islamic

financial industry. In our pursuit to develop Islamic finance, the recent enhancement to the Central Banking Act has accorded formal recognition to the existence of Islamic finance as an arm of the dual financial system, thereby giving significance and due prominence to Islamic finance. Moving forward, a number of initiatives are planned to further enhance the competitiveness and growth momentum of the takaful industry, emphasising on enhancement of the regulatory and supervisory framework and the Shariah governance framework. Such initiatives are laid down for industry players to capitalise on, to achieve sustainable success and to unleash their potential gains both locally and abroad. In light of this, allow me to share my thoughts on some key focus areas and developments which embed our aspirations on the future direction of the takaful industry.

Against a backdrop of growing opportunities and challenges as the business environment becomes more intensified and challenging, capacity and capability building measures for industry players to compete effectively and efficiently will continue to be pursued. These complement our efforts to further strengthen the institutional infrastructure of our takaful industry by increasing the diversity and strength of players in the Islamic financial system. The emergence of AIA AFG Takaful Bhd. in the Islamic financial landscape is therefore timely to further inject the competitive element that would propel the growth of the takaful industry. This is particularly so, as part of Malaysia's recent liberalisation measures aim to develop a resilient, diversified and efficient financial sector with financial institutions that are in greater state of readiness to compete in a more liberalised and challenging environment. The granting of four new family takaful licenses by Bank Negara in 2009 is also complementary of Bank Negara's initiatives of promoting the establishment of a core of robust industry players that could heighten competition and spur innovation in the takaful industry. The commencement of AIA AFG Takaful Bhd., being the second takaful operator to be launched among the new licensees, offers strong value propositions and is envisioned to further enhance the development of the family takaful industry in Malaysia, namely in penetrating untapped areas of business within the family takaful industry, such as microtakaful, medical and retirement products. This would certainly enhance the breadth and depth of family takaful products available in the market, thereby widening the financial safety net of the general population. The establishment of the two additional takaful joint ventures that would InsyaAllah, be in operations by the end of this year would also reinforce the competitive element and innovation in the takaful industry.

On the regulatory front, regulations for the takaful industry will continue to focus on ensuring effective risk management in the product development process and operations of takaful operators. The takaful industry has been progressively on its track to fully embark on the principle and risk-based supervisory approach that has been implemented for the insurance sector. This is seen by the recent issuance of the Guidelines on Takaful Operational Framework, which establishes principles governing the operational processes of takaful business to ensure that business activities and innovations are within the takaful operator's risk management capacity. With effective discharge of takaful operators' duties, the interests of takaful stakeholders will be safeguarded as the guidelines place emphasis on sound management to ensure sustainability of takaful operators.

A robust Shariah governance framework is another important element to assist the takaful industry in achieving full Shariah compliance in the development and application of their products and services. Given that Islamic finance has its roots in Shariah, it is an overarching requirement for an Islamic financial institution to ensure that its objectives and operations are in accordance with Shariah principles. Recent enhancements to the Shariah governance framework are aimed to assist Islamic financial institutions in meeting this overarching requirement, through further strengthening of the existing Shariah governance process, decision making, accountability and independence. Reinforcements of the Shariah compliance functions include introduction of internal Shariah review and audit requirements, supported by an appropriate risk management process and research capability. The new framework is envisaged to contribute towards evolving a more robust and sound Shariah

governance framework within Islamic financial institutions, with the establishments of end-to-end Shariah compliant control mechanism that promotes greater Shariah observance throughout an organisation. Effective implementation of the new Shariah governance framework will further promote stakeholders' confidence and enhance the integrity of the Islamic financial industry, and for the takaful industry, by reducing the risk of Shariah non-compliance, takaful products would be at a more competitive edge in comparison with conventional insurance products, as discerning customers would opt for takaful as their ethical financial solutions.

In respond to the ever changing business environment, it is imperative for takaful operators to enhance their institutional capabilities and operational efficiency with the aim to strengthen their competitive position. It is also important for the takaful business, like other financial services providers, to select an efficient and cost-effective distribution channel that is strategically aligned to meet the participants' reasonable expectation. Strategic alliance in the bancatakaful arrangement has become an important delivery channel with significant improvements in the takaful contributions during the past years, evident by its positive increasing trend for general takaful and by being the leading distribution channel for family takaful, accounting for 50.3 percent of contributions in September 2010.

The bancatakaful arrangement between Alliance Bank Malaysia Berhad and American International Assurance Bhd. indeed offers attractive value proposition for both partners. It is our aspiration to see AIA AFG Takaful Bhd. emerge as an effective and progressive takaful operator with strong presence in the domestic financial landscape and be among the anchor players to expand takaful business at the global front. I am confident that AIA AFG Takaful Bhd. should be able to strategise itself by optimising and leveraging on its shareholders' wide customer base and network, strength, expertise, experience and infrastructure in offering diversified products of high quality and enhanced customer service. Given the strong international network and experience of its foreign insurance partner, AIA AFG Takaful Bhd. is also certainly well positioned to establish its global Takaful centre of excellence for the region in Malaysia, therefore reinforcing Malaysia's position as an international Islamic financial hub. On this note, I wish AIA AFG Takaful Bhd. every success in its endeavours and look forward to its contribution towards further development of the Islamic financial services industry in Malaysia.

Dengan lafaz *Bismillahir Rahmanir Rahim*, saya dengan sukacitanya merasmikan pelancaran AIA AFG Takaful Bhd.

Terima kasih.