Muhammad bin Ibrahim: Beyond borders – bridging new horizons in Asia Pacific

Speech by Mr Muhammad bin Ibrahim, Deputy Governor of the Central Bank of Malaysia (Bank Negara Malaysia), at the 5th Malaysia Insurance Summit "Beyond Borders: Bridging New Horizons in Asia Pacific", Kuala Lumpur, 7 October 2015.

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I am delighted to join you today at the 2015 Malaysia Insurance Summit themed "Beyond Borders: Bridging New Horizons in Asia Pacific". I understand that this is the fifth year the Malaysian Insurance Institute has organised this event which brings together insurance and takaful professionals from around the region and beyond to discuss key developments in the industry.

Prospects of the Asia Pacific region

The world is undergoing rapid structural changes amidst a rapidly evolving Asia Pacific as an important centre of growth. The International Monetary Fund has projected a growth of 5.6 per cent for the Asia and Pacific region in 2015 and 5.5 per cent in 2016, with the region expected to remain the global growth leader over the medium term. Growth is primarily driven by domestic demand of Asia's 4.3 billion inhabitants who account for 60 per cent of the world's population. The region is also expected to be the strong driver of world insurance growth, with its share of the global insurance market likely to rise to 40 per cent in the next five years.

In the medium term, the region is expected to benefit from the deeper regional financial integration agreed by the leaders of ASEAN and recently reported concluding of TPP negotiation. These agreements would result in a more efficient allocation of regional savings to meet the region's large investment needs which will support growth and consequently financial well-being and soundness. The improved income arising from the economic developments will spur greater demand for insurance services in the region and present immense growth opportunities for the insurance and takaful industry.

The Asia Pacific region offers high growth prospects over the long term underpinned by potential demand arising from structural changes and evolving risk exposure. This will have the implication of increasing wealth and shifting preferences, but challenged by a rapidly ageing population and frequent incidences of catastrophic events.

First, increasing wealth and shifting preferences in Asia Pacific

Rising incomes have increased the spending power and affluence of consumers in Asia Pacific. GDP per capita for the region reached 15,242 US dollars as at end-2013, well above the world average of 10,613 US dollars for the same period. Reflecting higher standards of living and enhanced purchasing power, demand for insurance products in the region has evolved to encompass a broader range of protection and investment solutions that are more responsive to differing risk and return preferences.

This has also been Malaysia's experience, with the significant growth of investment-linked insurance premiums over the last decade alone. Investment-linked insurance products now account for more than 38 per cent of the domestic insurance market, almost equal to the share of more traditional whole-life and term insurance products that had historically dominated the market for many years.

Second, Asia is rapidly ageing

Improvements in living standards and life expectancy, combined with falling fertility rates, contribute to a rapidly ageing population globally, including in Asia Pacific. Studies have projected that the population of seniors, ages 65 and older, will grow the fastest in Africa (296 per cent) between 2010 and 2050, followed by Asia and the Oceania countries (216 per cent), while the population of young children below the age of 15 is projected to fall by 12 per cent in Asia and Oceania. The share of the global population of people aged 65 and older living in Asia should correspondingly rise from 54 per cent in 2010 to 61 per cent in 2050 with the median age increasing from 29 to 40 over the same period. A United Nations study estimates that by 2050, the older population in the region will triple in number to more than 1.26 billion. This demographic transition has far-reaching social and economic implications as it exerts a significant strain on the social security systems, infrastructure and provision of health care services of economies.

The limited capacity of Governments are constrained to meet these rising demands to care for the elderly and the need to provide for the new demographics has increasingly become a focus of attention. Rightly so. As a civilised society we should care for our seniors. Many efforts are being initiated by economies to improve social and economic developments, including strengthening social safety nets and improving health care systems. The insurance industry has an important role to play in supporting such efforts through the provision of well-designed retirement security, private health and long-term care products.

In Malaysia, to encourage retirement savings, the Malaysian Government has provided tax incentives to encourage the purchase of deferred annuity products which provide an income stream during retirement. The Government has removed the 8 per cent tax which was imposed on investment income on deferred annuity products. A tax relief of RM3000 was also granted to encourage the purchase of deferred annuity products. Despite this, response from the insurance industry is lethargic at best. The industry ought to improve product design and delivery channel to benefit from the tax incentives given by the Government.

With the more challenging economic conditions that are confronting our societies, there is also a broader educational imperative that needs to be met. The industry should come together to aggressively raise awareness on the importance of retirement planning, and to help consumers understand and purchase retirement products. I believe more opportunities can be tapped if the industry could collectively work on this matter. The need is urgent. It is time for the industry to come together and make a more significant impact through well-planned investments in product design, risk management and to support consumer education in retirement planning solutions.

Third, catastrophic events in Asia Pacific is rising.

The region is also confronted by an increasing frequency and severity of catastrophic events. Eight of the 10 countries in the world with the highest annual natural catastrophe losses as a percentage of GDP are located in Asia. Over the last 20 years, natural catastrophe losses suffered by Asia accounted for almost half of the world's estimated economic losses from natural disasters, yet only 7.6 per cent of such economic losses in Asia were insured compared to 67 per cent in the United States for example. These significant protection gaps that are prevalent across most of Asia and expose the vulnerability of the population and economies of the region to hardship due to loss of lives and damage to properties following a catastrophic event.

The poor are most severely affected. While some countries have implemented disaster-risk insurance schemes or provide Government assistance to alleviate such losses, others continue to be exposed. In response to this challenge, more is being done among developing economies, including under public-private sector partnerships, to develop and increase access to affordable micro protection plans as a means of helping millions of people cope in the most difficult times.

Strategies to seize opportunities in the new horizon

Allow me now to turn to some of the key strategic imperatives for the industry going forward.

First and foremost is the building of strategic and quality human capital. Human capital can be likened to the indispensable crew that you need for your ship to sail. Shortage of quality talent is one of the most important risks facing organisations globally today and the insurance industry is no exception. The Malaysian Insurance Institute, like many other insurance training institutes around the world, ought to expand investments in personnel with the relevant skills and knowledge in particular the ability to adapt and innovate.

In today's environment, training needs to be continuously changed, in some cases overhauled, to maintain its quality and relevance. Central to this is the industry's collaboration with and support for training institutes. The experience of practitioners who are experts in their field would enrich training programmer considerably. In this regard, the Bank welcomes the efforts of the industry and the Malaysian Insurance Institute to build bridges with academia through practical collaborations that aim to create a ready pool of productive talent. New approaches and programmes could be tailored against proven methodology implemented by some graduate schools. On the part of Bank Negara Malaysia, the recently established Financial Sector Talent Council is collaborating closely with key members of the financial industry to identify issues surrounding talent gaps and formulate innovative proposals to address such gaps.

Another important area is to raise the professional standards of the industry that reflects the highest standards of professional conduct, knowledge and competence. In this regard, the grand design of the industry, the Financial Sector Blueprint, clearly emphasized on the need to develop talents across all levels of an institution, spanning from the entry level to senior management and the board of directors. Indeed, a holistic talent development and management is a good example of an initiative that combine art with science which a visionary institution must be able to master to achieve its goals.

The *second* imperative is the ability of the industry to effectively leverage on technology to build strong, innovative and competitive businesses. This includes developing a deep understanding of how changes in technology impact people's lives and transforming how consumers and investors behave and view the value proposition of businesses. For instance, mobile phone penetration in Asia alone makes up 52 per cent of total global penetration. The highly developed telecom markets of Asia with 3.6 billion people across Asia having mobile phones spread across a diverse range of markets, capitalising on mobile data/wireless broadband services would mostly likely chart the way of the future.

Growth across Asia in high speed access to the internet by mobile wireless devices has been largely driven by highly competitive markets combined with a general population who are prepared to embrace new mobile technologies. As consumers embrace the digital era, insurers will need to rethink their distribution strategies and partner relationships as digital and remote options are rapidly replacing commonplace functions and tasks. Digital technology can be deployed effectively to accommodate customers' priorities in ways that would promote customer support and loyalty whilst significantly enhancing the consumer experience and satisfaction.

In many ways, the human capital and technology imperatives share characteristics that are borderless. We are living in a globalised world, with significantly greater capital and labour mobility than in any other period in history. For multinational organisations, this enables ideas and innovations to transcend borders and be more easily replicated to great positive effect, to grow successful businesses and transform the economies in which they operate. This is where foreign partners of local entities with international presence have enormous potential to make a significant contribution to the development of local economies.

As international entities that actively operate in more developed insurance markets, foreign insurers should bring new and proven systems, technology and experiences which can enhance their domestic operations and benefit the wider economy of the host country. This is the fundamental value of foreign direct investments. We know of successful cases in Europe where digitisation has been transformational, where a higher adoption of straight-through processing, paperless documentation, usage of customer analytics and electronic payments have all led to improved efficiency and higher service value for insurers. The same can and should be replicated in this region, with the presence of foreign global insurers driving this process.

Major developments in Malaysia – Liberalisation of the life and general insurance sectors

On the home front, two major developments are taking place; (i) the introduction of the Life Insurance and Family Takaful Framework and (ii) liberalisation of the Fire and Motor Tariffs. Both these initiatives will allow the industry greater operational flexibility to innovate, while ensuring that consumers' interests remain adequately protected. Our goal remains unchanged – to ensure Malaysians have the opportunity to avail themselves of efficient and effective means to manage risks with insurance and takaful solutions that are appropriate for their circumstances. For the life insurance and family takaful sector, the focus remains to increase the penetration level, as measured by the number of policies in force per population, from 56 per cent currently to 75 per cent by 2020. This is envisaged in the Economic Transformation Programme and this target is certainly achievable. Product innovation remains key to achieve this target, particularly in the micro-insurance and micro-takaful space which would expand the reach to the underserved segments of society.

In the non-life or general insurance space, a more market-driven pricing structure will be introduced for motor and fire insurance. This will also pave the way for the development of products that can be more responsive to consumer and business needs in the two most dominant lines of business in the Malaysian general insurance sector.

Importantly, this development will be critically dependent on insurance and takaful companies building strong internal underwriting and risk pricing practices to ensure the sustainability of the business, particularly in the highly competitive motor insurance segment. Let me re-emphasis the importance this development to our market and the criticality to remove the current market distortions that undermine the long term sustainability of motor insurance.

The industry cannot afford to take a short term view; it must keep its sights on building the foundations for operating in a more diverse and mature market, with stronger value propositions for consumers. Presently, with the high volume of vehicles referred to by the industry, the Malaysian Motor Insurance Pool has a life of its own and I was told the MMIP is the 9th largest general insurer in Malaysia. This was never the intent. Let's revert to its original mandate as a mechanism to insure the highest risks motor vehicles.

In tandem with these developments, insurers and takaful operators must be fully accountable for the conduct of their intermediaries in ensuring that customers receive proper advice and quality service throughout the duration of the policy. It is important that adequate training is provided and the right remuneration and incentive structure is implemented to promote a committed and professional agency force.

With this expectation there is increased demand for a full time and professional agency force. Conduct issues are viewed seriously by the Bank and we are fully committed to the responsibility entrusted to the Bank to effectively enforce regulatory requirements on fair conduct towards consumers.

The Financial Services Act provides the Bank with explicit and expanded enforcement powers which include monetary and non-monetary actions. In addition to private and public reprimand as well as direction to make restitution to aggrieved parties. As a result of supervisory interventions by the Bank, more than RM30 million in premiums were refunded to the affected policyholders due to mis-selling practices in the sale of life insurance products in the past.

The Bank had also directed insurers to refund the premiums in more than 700,000 cases involving the forced purchase of personal accident policies. In addition, insurers have been directed to modify or withdraw misleading advertisements, make call backs to consumers to confirm the products purchased without adhering to proper disclosure practices, as well as strengthen internal controls over sales and marketing practices with respect to bancassurance products.

The enforcement measures undertaken signals the Bank's low level of tolerance for misconduct. It also serves to remind the industry of the Bank's expectation for common complaints and grouses against the industry such as delay in claim settlement and mis selling practices by agents to be completely eliminated or at the very least reduced significantly.

Conclusion

The period ahead for the Asia Pacific region presents new risks, challenges and opportunities for the insurance and takaful industries. In facing them, we need a visionary industry and creative solutions that will lift our economic potential and improve lives of our people. Such solutions must be built on the strongest foundations the strength of our technical capability, our financial strength and our uncompromising stance towards professional ethics and standards. With these foundations firmly in place, the industry can bridge new horizons and expand beyond traditional borders.