

Zamani Abdul Ghani: Significant trends surrounding the takaful industry

Opening address by Mr Zamani Abdul Ghani, Deputy Governor of the Central Bank of Malaysia, at The 3rd International Convention on Takaful and Retakaful, Kuala Lumpur, 29 August 2007.

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Bismillahirrahmanirrahim,
Distinguished Speakers,
Ladies and Gentlemen.

Assalamualaikum w.r.t. and Good Morning.

I am indeed very pleased to be here this morning to welcome you to Kuala Lumpur . Alhamdulillah, we have among us today distinguished market players, regulators, scholars as well as participants from many parts of the world, including Brunei, Thailand, Indonesia, Singapore, Bangladesh, Sudan, Nigeria, Pakistan, Kuwait, Egypt, UAE, Bahrain, Jordan, Turkey and many others. On behalf of Bank Negara Malaysia, I wish to congratulate the Islamic Banking and Finance Institute Malaysia (IBFIM) and the Malaysian Takaful Association (MTA) for their efforts in organizing, for the third consecutive year, this International Convention on Takaful and Retakaful. Let me at the outset reiterate the importance of this Convention as a source of collaboration for ideas, sharing of knowledge and exchange of experiences for the continuous development and improvement of the takaful and retakaful industry.

In few days time, on 31st of August, Malaysia is celebrating the 50th National Day and therefore, the organization of this 3rd Convention on Takaful and Retakaful is indeed very special. The convention and independence celebration have similarities in their core values. Both cherish the spirit of alliance, tolerance and togetherness. Both also share strong call for “muhasabah” or reflection – to strategize for the future by reflecting on past experiences. My address today will touch on these two aspects. I will share my observations on the significant trends surrounding takaful industry in recent years as well as key focus areas for the industry moving forward. Finally, I will highlight a couple of major initiatives undertaken by Malaysia to further strengthen as well as expand the breadth and depth of the takaful and retakaful industry.

High growth potential of global takaful market

As a starting point, allow me to share with you five major trends in global takaful industry over the past few years. These trends have significant bearing on the development of this industry moving forward.

First, the takaful and retakaful industry continued to show rapid growth momentum, and is increasingly being recognized as one of the major components of the overall Islamic financial system . Global takaful contributions amounted more than USD2 billion in 2005 and are expected to reach USD7 billion by 2015. The past few years have seen growth rates of around 20%, indicating high growth potential in years to come due especially to the present very low rate of takaful market penetration. As for Malaysia, a commendable track record of the takaful industry has been recorded since its inception more than two decades ago. For the first half of this year, the total assets of the takaful funds stood at RM7.6 billion (as equivalent to USD2.2 billion). This represents 6.3% of the entire takaful and insurance industry funds assets and an increase of 11% as compared to the end of 2006. In terms of net contributions, RM1.2 billion was recorded in the first half of the year, an increase of 36% from the same period of last year.

Second, there is growing international consensus on the need to have a strategic direction for an orderly development of the global Islamic finance industry. The ten-year blueprint on the development of Islamic finance, a joint initiative by the Islamic Financial Services Board and Islamic Development Bank, has laid down guidelines on the strategic steps to be taken by several specific jurisdictions for this purpose. It is envisaged that with more orderly development of Islamic financial services, including takaful, a more comprehensive Islamic financial system will evolve in more jurisdictions. The number of takaful operators, which currently stands at more than 100, is set to increase.

Third, dramatic growth of the global sukuk market can potentially become a key supporting factor for the strong growth of takaful and retakaful industry. Sukuk is increasingly becoming an important investment avenue for the takaful industry. Today, the global sukuk market, denominated in international currencies, is estimated to have exceeded USD50 billion [including domestic sukuk issuance]. Although the size of the market is modest by global standards, the sukuk market is experiencing remarkable growth, increasing at an average rate of growth of 40% per annum. Issuance of sukuk with longer tenure will match investment and risk management needs of takaful industry with largely long term liability. This, in particular, will greatly spur the growth potential of investment-linked products. I am sure you will also be briefed on the development of the sukuk market in Malaysia later on.

Fourth, the increase in outsourcing and white labelling activities. Competitive elements and strong demand for takaful require takaful players to constantly search for solution towards greater efficiency and shorter time to market. There is strong potential for strong and experienced takaful players to leverage on their competitive strengths to be an ally of other players, especially from a new market, by becoming either outsourcing partner or white labelling provider.

Fifth, as seen in international Islamic banking scene, there was growing participation of major conventional global players in the takaful and retakaful industry. In Malaysia, the strategy to encourage alliances and collaborative efforts between local and foreign players has resulted in a positive outcome with the licensing of new takaful operators consisting of joint ventures and consortia of local and foreign players which have registered early strong performance. In addition, the other 100%-owned Malaysian takaful operators are now actively looking for strategic partnership with foreign financial institutions so as to facilitate their expansion abroad and exploit opportunities in untapped markets.

These five trends point to one direction – that the industry will continue to present high growth potential with growing demand, increasing competition, supported by greater sophistication and innovation of products and services. While the double digit growth is commendable, the takaful industry is still small i.e. constituting 6.3% in terms of assets of the insurance industry. The success of takaful in the future rests on the ability of the industry to collectively position itself strategically to meet the needs of the economy and the ability to be competitive and innovative.

Global takaful strategies

Let me now turn to the strategies for the global takaful industry moving forward, which essentially is the theme of the Convention. The key strategy is to amplify a simple, but yet a powerful concept, which is the core concept of takaful itself, that is, **collaboration**. That is in consonance with the Quranic verse from Surah Aali-Imran verse 103's quote: *"And hold fast, all together, by the rope which God (stretches out for you), and be not divided among yourselves and remember with gratitude God's favour on you..."* end of quote. Allow me to expound a few angles on this new collaborative framework.

The first area is talent development

A key challenge confronting the industry at present is the shortage of talent. Rapid development of the takaful industry in recent years demands adequate supply of competent human capital to drive innovation, to sustain competition and to raise the performance of the takaful industry to greater heights. The takaful operators are constantly in search for high level of expertise in all relevant areas in the management of takaful business including technical, actuarial, distribution, underwriting, investment, Shariah as well as strong leadership at the helm of a takaful operator. This talent war even persists in Malaysia where medium and long term plans to develop adequate human capital are in place. It may not be sustainable for the industry to rely on the current pool of intellectual capital in this rapidly growing industry.

For this, concerted and collaborative efforts should be taken at the industry level involving all stakeholders to develop structured human talent developmental programmes at all levels which include the leaders, technical personnel as well as the regulators. The organization of this Convention by IBFIM and MTA presents a model for such collaboration between takaful stakeholders in promoting human talent development, not only for Malaysian takaful industry, but also for the global takaful sector. The industry needs also to consider further proactive approach to address this issue. For example, the industry may take a united stance to train a specific number of new talent in key areas. For Malaysia alone, assuming that a good candidate requires two years of training to be a well-rounded takaful practitioner, if each operator is able to train 50 new talent at various levels in specific key areas, we will have at least 2000 new talent in 2009. In fact, we should do better.

The second area relates to operational harmonization and global support system

To sustain the current pace of growth in this new industry, global takaful alliance is indeed crucial. The takaful industry needs to present itself as a united front with a common voice in operational and even Shariah matters. Although minor differences are needed to propel innovation and creativity, major divergence in operational practices and Shariah application would pose unnecessary confusion to the consumers at large.

For this, the transformation of an informal grouping of ASEAN Takaful Group or ATG into a registered legal entity limited by guarantee called "Global Takaful Group" or GTG is indeed timely. I am glad to note that the Annual Meeting of GTG was held yesterday in conjunction with this Convention. I believe GTG will serve as the best platform to enhance greater mutual co-operation and foster cooperation and interlinkages among the takaful operators globally. It is a tangible vehicle of cooperation among takaful operators and provides a conduit for exchange of information on all facets of takaful operations among the members. I understand that currently there are more than 20 member companies of GTG and it is our hope to see more takaful operators from all over the world to join this Group. I wish to urge all takaful operators to leverage on this Group as an official platform for greater interaction and collaboration, not only among the players, but also with other stakeholders such as the regulators, Governments and the public at large.

It is also encouraging to note that rating agencies have come forward to formulate rating methodology and review for takaful operators.

Third area relates to the need for joint effort to shape prudential rules for takaful.

For the formulation of prudential standards, the setting up of the IFSB remained one of the landmark developments in this decade. Established in 2002, the IFSB's core role is to promote prudent, transparent and robust development of the Islamic financial services industry through the promulgation of international prudential standards that are consistent with the principles of Shariah. The IFSB provides the platform for cooperation among the regulators through meetings, conference and the setting-up of working groups that give

opportunity for the regulators to discuss and exchange information on issues confronting Islamic finance. For takaful industry, two developments are relevant that are:

- i. the issuance of Issues Paper jointly by IFSB and IAIS on the applicability of IAIS core principles to takaful, and
- ii. the formation of a working group to formulate corporate governance standard for takaful industry.

In view that the formulation of the IFSB standards involves consultation with IFSB members, I would like to call more takaful operators to be members of the IFSB so as to provide the opportunity for the players to be part of the official consultation procedure for IFSB and to make comments on draft IFSB standards. Given your vast experience in the area of takaful, both domestically and globally, we believe that the industry players will provide valuable contribution towards the formulation of the IFSB international takaful standards. Your experience and inputs on issues are relevant to or have impact on the regulation and supervision of the takaful industry.

Malaysia as takaful & retakaful hub

Let me now turn to the final part of my address by sharing Malaysia's latest initiatives to strengthen its position as a takaful and retakaful centre.

I. MIFC initiatives

Malaysia aims at enhancing its inter-linkages with the global Islamic financial markets. Among these are its continuous efforts to not only develop the financial infrastructure of the takaful industry but to also implement measures and initiatives that will strengthen our position as an international takaful and retakaful centre. Besides allowing up to 49% of foreign equity participation in domestic takaful operators, the Malaysian Government has also launched an initiative known as the Malaysia International Islamic Financial Centre or MIFC. The MIFC initiatives are specifically undertaken by the collective efforts of the country's financial and market regulators, including Bank Negara Malaysia, the Securities Commission, the Labuan Offshore Financial Services Authority and Bursa Malaysia, together with the participation of representatives of the banking, takaful and capital market sectors. It is aimed at building greater intermediation linkages between East Asia, South Asia and the Middle East which will, in turn, further expand inter-regional trade and cross border investment flows.

As part of these initiatives, foreign financial institutions are allowed to establish International Islamic Banks, International Takaful Operators, as well as International Currency Business Units to undertake international currency business in Islamic finance with non-residents in Malaysia or abroad through a locally incorporated entity or a branch. This entity is granted attractive tax package in terms of a 10-year tax holiday. To date, ten financial institutions have been granted approval to set up international currency business units, and one institution has been granted approval to set up an International Islamic Bank. The strong sukuk market in Malaysia that accounted for about two thirds of the global outstanding sukuk issued in 2007 would further provide a conducive environment for the MIFC activities.

II. New retakaful framework

Malaysian Government has also focus ed its efforts towards widening and deepening the retakaful sector in complementing the growth and expansion of the takaful industry. I wish to announce and declare here that Bank Negara Malaysia is inviting strong and qualified applicants to make Malaysia as their centre for retakaful activities. The application for retakaful licenses are open to qualified local and foreign players. Besides fulfilling the need for retakaful support of the takaful operators, the new retakaful licencees will assist in

reducing the industry's dependency on conventional reinsurance support. More importantly, the licensing of new retakaful operators in Malaysia will also ensure that the technical knowledge is made more readily available and enhanced in the market, particularly in takaful and retakaful underwriting, as well as in promoting product development and innovation. Under this initiative, qualified applicants will be allowed to conduct in both the Malaysia Ringgit and international currencies retakaful business under the Takaful Act 1984. Flexibility is accorded to the retakaful operators to conduct its retakaful business in Malaysia by way of an incorporated entity or a branch. Foreign applicant is also welcome d to conduct retakaful business in Malaysia through a joint-venture with Malaysian companies, subject to the merits of each case. It is anticipated that this measure would serve as a catalyst in our efforts for Malaysia to become the centre for takaful and retakaful business through the establishment of a significant number of strong and reputable retakaful operators.

Ladies and gentlemen,

Let me conclude by saying that the future prospects of the takaful industry will be very much depend on the combined efforts of all the relevant parties; the regulators, market participants and the international community at large, to chart the strategic direction for the industry. Collective effort is crucial in order to maximize the potential for the industry. Sharing common vision and goal will be an important first step. I believe that our sincere efforts in realizing this noble objective would InsyaAllah, God Almighty will shower us with His blessings, guidance and assistance.

On that note, I wish you a successful and productive Convention.

Wabillahi taufik walhidayah. Assalamualaikum warah matullah hi wabarakatuh.