

Takaful to lead the way in sustainability



The pandemic has provided a new opportunity for takaful operators to overcome issues of scale, distribution and relevance.

By **Ridwan Abbas**



The pandemic has accelerated a shift towards a more 'values-based' approach to takaful backed by a greater commitment towards the ESG and sustainability agenda, said Malaysian Takaful Association (MTA) chairman Elmie Najas at the virtual Takaful Rendezvous meet last month.

Mr Elmie added that members of MTA have successfully developed a framework that seeks to further ingrain sustainable business practices and values within the takaful businesses.

The values-based intermediation for takaful (VBIT) initiative, which is set to be launched at the end of this month, will thus put Malaysia's takaful sector at the forefront of sustainability and set a benchmark for the wider insurance sector.

"It is expected that this framework



Mr Elmie Najas

will amplify the takaful value proposition to realise the intended outcomes of shariah in its conduct and offerings, going beyond the minimum shariah requirements," he said.

The VBIT framework would also serve to guide the Malaysian takaful industry in drafting the sector's roadmap over the next few years, thus allowing the industry to build up the necessary capacity to ensure consistent and effective implementation of the VBIT initiative, said Mr Elmie.

Scaling up through digitalisation

The digital transformation which the takaful sector undertook prior to the pandemic has put the industry in a good position to adapt to changes that have been brought on by the COVID-19 crisis.

"We have seen an explosion in remote-sales capability and the use of apps to service customers. The COVID-19 situation has significantly

accelerated opportunities for digital engagement and digitised delivery for the industry,” said Mr Elmie.

The takaful sector has found it hard to achieve scale for more than a decade and to overcome the advantage that conventional insurers have in terms of distribution. But technology may well help the industry overcome such barriers.

“It has given the takaful industry a new capability to now reach and service customers across physical locations or boundaries. With more and more customers being more comfortable with online transactions and face-to-face interactions via video calls, the industry is entering an exciting period of change and technology will be the driver of growth,” he said.

Despite the challenging conditions, Malaysia’s family takaful segment last year registered a 7% increase in new business contributions to MYR6.59bn (\$1.6bn).

Meanwhile, the general takaful business recorded a 4.4% increase in gross contributions to MYR3.31bn with motor takaful accounting for two-thirds of premium volume. Interestingly, the online channel grew by 22% last year to MYR213mn in gross contributions with motor takaful sales responsible for 96% of online sales.

Towards a greener industry

Further reinforcing the issue of sustainability, DDCAP group head of corporate responsibility Jennifer Schwalbenberg said (re)takaful operators should view climate change as a major reputational, legal and financial risk.

She added that investors are demanding more transparency on ESG issues, especially from providers of Islamic finance where ethics is a core value proposition.

“A greener and more sustainable (re)takaful industry is one where people and entities are aligned in adopting sustainable practices. Innovative product development and considered underwriting are



Ms Jennifer Schwalbenberg

important to reducing risk and achieving ESG outcomes, but green takaful requires attention across the value chain including the assets in which policyholder funds are deployed,” she said, adding that sovereigns and corporates need to increase their focus on green sukuk issuances.

She proposed three things for the industry to take a strong lead on sustainability and they include, embedding ESG issues within the takaful industry and in decision making; working with clients and partners to raise awareness of ESG issues and develop solutions; and working with governments and regulators to spread action across society on ESG issues.

“Takaful operators are well-placed to play this catalyst role and if the takaful and Islamic finance industry do not rise to this challenge, then our markets and operating models could be severely disrupted.”

IFRS17 considerations

Another issue that has an immediate impact on takaful operators is the implementation of IFRS17 standards. In Malaysia, there remain ongoing discussions on the appropriate methodology to implement IFRS17 for (re)takaful companies given the operational differences with conventional insurers. There are some aspects which remain unclear in modelling IFRS17 for insurance contracts issued by mutual entities, which impacts takaful operators and insurers with participating business.

From a retakaful standpoint, IFRS17 requires insurance and reinsurance contracts to be measured and reported separately, although retakaful arrangements typically have a direct effect on the takaful fund surplus and thus directly affects surplus distribution to participants, said Milliman Malaysia consulting actuary Chong Wen Ang.

Similar to mutualised contracts, the profitability of retakaful contracts cannot be assessed without considering the profitability of the takaful fund on aggregate, he added

while stating that there is not yet an industry consensus on how to account for retakaful in Malaysia.

ERM

Resilience to disruption and shock are important themes as the pandemic has proven. AM Best senior director Mahesh Mistry discussed some of the lessons learnt from the COVID-19 crisis from a risk management perspective, noting how the crisis has reinforced the issue of risk correlation and accumulation as well as risk identification and preparedness among other things.

He said that insurers have generally managed operational risk well and adapted to new ways of working with the aid of technology. He added that stress testing of insurers showed that most companies were well capitalised and hence were able to absorb the stress test. However, companies in emerging markets tended to have a higher level of asset risk due to higher exposure to equities and real estate – with smaller companies that have more concentrated profiles being the most exposed.

“Enterprise risk management is thus critical to the industry, and takaful operators have the added layer of complexity with the existence of shareholders fund and policyholder fund and these companies have not been immune to market risk.

“But they have not been as affected as others as a number of them are focused on the retail business although performance remains mixed and uncertainty persists, hence they need to adopt the right practices,” said Mr Mistry.

He added the insurance industry cannot be complacent when it comes to ERM and should ensure they have an effective and dynamic risk management framework in place that can react to an evolving risk environment.

The Takaful Rendezvous 2021 was organised by *Asia Insurance Review* and supported by the Malaysian Takaful Association. 



Mr Mahesh Mistry



Mr Chong Wen Ang