

## ROUNDTABLE



# What does the future hold for the Takaful industry in Indonesia?

### Panelists:

- Moch. Muchlasin** – Director of Shariah Non Bank Financial Industries, Otoritas Jasa Keuangan (OJK)
- Firas El Azem** – General Manager, Takaful-Re
- Marcel Omar Papp** – Head of Retakaful, Swiss Re
- Srikandi Utami** – Head of Shariah, Sun Life Financial Indonesia

### Moderator

- Lauren McAughtry** – Managing Editor, Islamic Finance *news*



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Awards 2012

**Panelists:**

**Moch. Muchlasin**  
Director of Shariah Non Bank  
Financial Industries, OJK



**Firas El Azem**  
General Manager, Takaful-Re



**Marcel Omar**  
Head of Retakaful, Swiss Re



**Srikandi Utami**  
Head of Shariah, Sun Life  
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**Moch. Muchlasin** formerly worked in Directorate General of Financial Institutions – Ministry of Finance in Indonesia in various roles as analyst, examiner and enforcement officer for the Pension Directorate between 1994-2006, prior to the establishment of Capital Market and Financial Institutions Supervisory Agency (BapepamLK) in 2006. He was also involved in the government guarantee scheme project that led to the establishment of the Indonesian Deposit Insurance Corporation (IDIC) in 2005. He was instrumental in the amendment of the Pension Law and the establishment of Indonesian's Financial Services Authority (OJK).

**Firas El Azem** has been General Manager of Takaful Re Limited since August 2013, and has more than 22 years of experience in insurance and reinsurance with a special focus on Takaful. He began his career with Munich Re and worked there for 15 years until reaching the position of CEO and General Manager of its Kuala Lumpur branch. He then returned to Syria and led the establishment of two new private insurance companies. He is a graduate of business administration from the University of Cologne.

**Marcel Omar Papp** is the Head of Swiss Re Retakaful. He started his insurance career as a claims broker with Willis in London more than 20 years ago before moving to Union Re (Zurich) in client market and underwriting functions. He joined Swiss Re in 1998 and worked as a casualty underwriting manager for Southeast Asia based in Singapore and then as the head of the Casualty Treaty Desk in Hong Kong, before moving to his current position when the Retakaful branch was set up in Kuala Lumpur in 2009 as the global center for Swiss Re's Family and General Retakaful business.

**Srikandi Utami** has worked in the life insurance industry for over 20 years, with a particular focus on marketing management. Over the past seven years she has focused on developing Takaful business with several multinational companies. As Head of Shariah at Sun Life Financial Indonesia she is responsible for developing individual and group Takaful business through the distribution channels of agency, bancassurance, telemarketing, and worksite. She is also the vice-chairman of the Indonesia Shariah Insurance Association and part of the microTakaful taskforce with Financial Authority Services and GIZ RSPI Asia to develop market surveys and prototypes of microTakaful products in Indonesia.

## What does the future hold for the Takaful industry in Indonesia?

In September 2014 a group of regional and international experts gathered together at the Shangri-La Hotel in Jakarta to conduct a high-level discussion on the future of the Indonesian Islamic insurance industry. With a broad range of perspectives including from the regulatory, practitioner, reTakaful and observer angles, the debate was wide-ranging and rewarding, with lively interaction and valuable collaboration between the parties.

Seeking to uncover the key trends and developments in the Indonesian Takaful and reTakaful industry and gain an understanding of the requirements for growth going forward, the conversation focused on the anticipated regulatory

updates and their impact on the Takaful landscape; as well as the differentiation and distribution strategy and what changes were needed to the current business model; the key product growth segments and trends in the market; and the core challenges facing the Takaful industry as a whole and how these can be met by all stakeholders.

Islamic Finance *news* was delighted to bring together the comprehensive knowledge and experience of leading industry experts including Moch. Muchlasin, Firas El Azem, Marcel Omar Papp and Srikandi Utami; representing a cross-section of the Takaful industry and achieving a rewarding and challenging discussion.



**IFN:** So perhaps we can start off with a general look at what the current situation is like for Takaful in Indonesia – where are we now, what growth are we seeing, and what is driving that? As a practitioner, can I pass that to Srikandi to start off with?

**Srikandi:** Currently in the market we have 20 family Takafuls, which consist of three Family Takaful companies and 17 units of Family Takaful, and then we have 25 General Takaful consisting of two fully-fledged Takaful companies and 23 units, then three reTakaful windows. Currently the business model is dominated by the agency distribution channel. Most contributions come from individual Takaful products, which are sold through agency distribution. Generally the product is unit-linked, which is mirroring the conventional product. The significant contribution is generated from windows, whereas they have a sales force who can sell both product types of conventional and Takaful. Many of the Takaful windows do not have dedicated distribution channel for Takaful products. To make sure agent are qualified selling Takaful products, agents join training where the syllabus consists of Shariah concepts, Takaful concept and products. The agent has to be registered to get the license of Takaful from the association. Agents who work for Takaful windows feel more comfortable selling unit-linked conventional and Takaful products where the features are alike. The agent approach to the same segment market level uses the same selling techniques and conventional mindset, so far there is no differentiation of selling skills between conventional and Takaful. So Takaful products are developed based on what conventional products have been made, not based on specific Muslim needs.

Operators provide Takaful products that the agent wants to sell instead of for customer needs.

In Indonesia, many segment market levels are low income level to affluent level. Many Takaful products are aimed at the middle to affluent market and it is the same with conventional. Large population numbers in Indonesia are Muslim in the low to middle market levels which are less aware and lack having Takaful. There is a gap between the affluent market and the low to middle market which are not touched by Takaful. This is our challenge in Indonesia - to create Takaful products that are really needed and build distribution channels, services and sales management that are addressed towards entering those markets.

On the other side, we face that many windows do not focus on running Takaful. Insurance companies who have Takaful windows put their main strategy and resources to conventional, then Takaful comes after. Without a focus on managing the Takaful business well by operators, Takaful will not grow well despite the big potential market.

**IFN:** So does anyone have any suggestions as to how that middle market can be tapped?

**Firas:** Before we get into this question, I would first like to learn a little bit more about the Indonesian Insurance and Takaful market. From what we know, the overall Indonesian market premium is around US\$15 billion, is that correct?

**Moch:** Yes.

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Marcel

**Firas:** And how much are the estimated contributions of the Takaful market? Is US\$600 million a reasonable estimation?

**Moch:** Right now, the Takaful market is around IDR19 trillion, which is around US\$1.6 billion. I think that's a reasonably correct estimate. Does that collate with your figures?

**Firas:** The Indonesian market is surely a growing market, but our estimations are in the mentioned range.

**Moch:** We had around IDR300 trillion, and around 4% of this is the Takaful market, in terms of gross contributions. Every year we have been seeing about 30-40% growth, although last year we only saw 26% which is the lowest we have seen in five years.

**IFN:** What do you think contributed to the lower growth rate?

**Moch:** Partly due to the slower economic growth, while another product which is also dominant on top of unit-linked assets is credit life, which attaches into credit. And credit from Shariah banks is a bit slower. Also consumer finance is growing more slowly, so that has affected the Takaful industry. We still have to analyze why we have seen growth slow to below the 30% average, but in 2014 H1 I think we have seen it increase again.

**this session, and how do you view the competitive opportunities in the market?**

**Firas:** Well for us it is a very promising market. TRL is represented well in the Middle East, and in Malaysia. The Indonesian market is a target market for us. The growth expectations are high. Moch also mentioned a figure of US\$1.6 billion. The biggest market right now is Saudi Arabia with US\$6.5 billion in Takaful/cooperative contributions. It worth mentioning that the whole Saudi market works according the cooperative insurance model.

**Moch:** US\$1.6 billion is the total Takaful assets, not the premium contribution.

**Srikandi:** We have big potential market, the contribution is not big enough yet. Meanwhile, OJK is issuing many regulations now to regulate how to manage it prudently and properly. Currently we have guidelines of doing Takaful business, financial solvency of company funds and Tabarru' funds, good corporate governance and they are preparing a draft of risk-based supervision for Takaful to ensure we are managing risks well.

**Firas:** Where is the Indonesia's Takaful market in comparison to other markets in the world? And what will be done to develop and promote it?

**Srikandi:** The market is open but it needs strategy how to focus on products, distribution channels which are suitable for product type and target market, education programs, marketing plans and selling processes.

**IFN:** So perhaps we can take a look at what steps have already been taken – what has been done over the past few years to encourage this development?

**Moch:** Perhaps before answering that – we have 250 million people, 80-87% of which are Muslim. So over 200 million Muslims. That is a huge potential. And if you look at the Indonesian economy, we are scoring a good GDP growth rate. We believe this will be a good market in future for both insurance and Takaful.

**Firas:** Is faith and religion an aspect influencing the behavior of consumer?

**“ Yes, Takaful growth is still outpacing the conventional industry. For example, last year Takaful grew 26% while the total industry only grew 11%. So it's still almost triple in terms of premiums ”**

**Firas:** And this 30-40% rate is just for Takaful?

**Moch:** Yes, Takaful growth is still outpacing the conventional industry. For example, last year Takaful grew 26% while the total industry only grew 11%. So it's still almost triple in terms of premiums. While on contributions, growth for Takaful was still 25% and conventional 11%. We also experienced very high growth in 2009, where the growth of total Takaful assets was 80%, while total insurance growth was 32%. So we are still beating conventional insurance, but the margin of competitiveness is decreasing.

**IFN:** You mention the margin – how competitive is the market right now? I know some of our panelists today are looking at what they can perhaps do in the Indonesian market – Firas, what are you looking to find out from



**Moch:** Well, we observe that most of them are rational. As long as you offer them a good price, good benefit, lower contributions, that will take it. If I divide the market, there are three types of consumer. First is rationalists: which as I said, will choose based on price sensitivity, so the question of faith perhaps comes second. And another is a group who choose based on faith: they are devoted Muslims and they don't mind paying extra for compliant products. But I'm not sure how big that group is because we don't have many statistics on this. But if you look at the current organization of Islamic communities, with Imams and so on, we find that most Indonesians are moderate and flexible, in almost every aspect. They are not fanatics. And then the third group perhaps is made up of those who don't care much either way – there is no opposition but no driving factor either.

**Firas:** Price is in most the Arab countries the main decision driver. Nevertheless, Takaful companies would be preferred, subject to matching their conventional peers as far as price and services are concerned.

**“ What Indonesia needs right now is a good financial system and economic growth ”**

**Srikandi:** Many Muslims are buying Takaful products because of benefit and price rather than Shariah principles or following religion.

**Marcel:** But for OJK, what is your grand aim? In Malaysia, the regulator clearly wants to push Islamic finance. Does Indonesia have the same goal? What is your 10-year plan, or five-year plan. Where do you want to see Takaful and Islamic finance go?

**Moch:** I think if you ask me about OJK, I have to be fairly circumspect. My title is head of Shariah and that is what I can comment on. But in general, I think that what Indonesia needs right now is a good financial system and economic growth. So we will pursue a dual system for the time being, with conventional and Takaful insurance. Also for Islamic banking, Islamic microfinance and so on. Both industries will be promoted and will be pushed towards a better position. However, we do know that since we are growing so fast, and there are still some interest groups that say we don't have any alternatives for some Shariah compliant products, we do need to take some steps to place more weight on Shariah compliant finance. Because on the banking side, we are still below 5% market share. So this is about developing areas, talking about inclusion, access for the poor – which is something we want to focus on and direct more resources towards. The market is huge, as I said earlier – if they can find a way to 'Halalize' their economic activities, we should support that.

**Marcel:** So what steps do you want to take in the next three to five years to promote Takaful in particular?

**Moch:** From the regulatory perspective, we are a newly integrated supervisory body right now, so there are some harmonizing Islamic banking and non-banking issues still to overcome. One area we want to tap is education – not many people understand insurance, let alone Takaful. Less than a quarter of Indonesians really understand the product. So we need to broaden the market. Most of us use very traditional methods – communities, village links, self-help groups. We want to access these and help them understand the role of Islamic insurance and Takaful. The second, as Srikandi already mentioned, is product innovation. Right now we are head to head with conventional insurance – we are offering the same products, just to different markets. And in fact not always to different markets, sometimes to the same market. So product innovation is important to pursue. And on that, it is not just the product but the general industry, the business processes – is there any better way to do it? Because over 95% of Indonesian Takaful players right now, I would say, have learned their business from the conventional providers. So yes – education, innovation, and then yes a regulatory angle as well, to encourage better corporate governance, a bigger role for Shariah compliance, better general distribution via agencies and so on.

**Firas:** Most Takaful companies are currently windows. Will you consider a clear separation?

**Moch:** Yes – it's actually in discussion with parliament right now. It is for the Ministry of Finance to decide the future of Takaful – and not just takaful but the whole insurance industry. The discussion is still in progress but will hopefully be concluded by the end of this month. We will have to wait for the result but on the concept, I think there may be a decision to require a spin-off within five or 10 years, so that no windows are allowed. There are still negotiations but I think the fastest will be five years and the longest it will take is 10 years. But it will definitely happen.

But it is more than just spinning off. We need to look at how we can identify and define the advantages of Takaful in Indonesia, encourage that through regulation and then establish that. We have some Fatwas, but compared to the banking side, not nearly enough. Islamic finance is driven by Islamic banking, in every area in the world. Takaful always has to try and catch up.



Moch

This is the same in the capital markets – if they are given a better return, they will take it. So, education is important as well as to offer good and comprehensive product benefits.

OJK, Takaful players and the Shariah council are promoting an education program to the public – they go to the schools, university, kampungs, and they make a curriculum for the students to learn about Islamic finance. This is a good step but we must improve ongoing programs.

**Marcel:** We have been traveling to Indonesia regularly and often on a monthly basis for the last five years. We have business interests on the Family and General side. And we see one big challenge. Whenever I talk to the CEOs, they tell me they have not much incentive to grow Takaful, simply because if they look at the ROE, between the conventional and the Takaful unit the ROE for conventional is a lot higher, because they don't have to share the profit. So what we see is that most Takaful companies really have a lack of commitment to put in resources. Actually we went to many players this year with new product ideas, trying to promote them, trying to help companies, offering expertise from Malaysia – but if there is no commitment from the senior management (and I am not talking about the Shariah unit itself which tends to be small, but from the overall management) then it is very difficult. And I think this is something you need to address, as the regulator.

So the fourth thing is how to access that 200 million people – so we are talking about empowerment. The Takaful industry might be growing at the moment, but right now it only seems to tap the crème de la crème of society, the affluent ones. If I pick any policyholder, I will probably find they are from the middle class, with a good education, a university degree, a good position on the economic scale – and they understand the offering. The problem with the lower social scales is that they don't understand what Islamic finance is. We need to focus on inclusion and empowerment – to encourage the working classes to use Takaful for their needs.

**Srikandi:** So if we look at the Indonesian market we have several stakeholders in the Takaful space. We have the National Shariah Board, which has currently issued five Fatwas for the Takaful industry – out of 95 in total for Islamic banking and capital markets. National Shariah Board makes Fatwas based on Islamic finance players' requests and based on market-driven needs. If the players ask National Shariah Board for a Fatwa then they will oblige – but if they do not ask, they won't receive them. So it depends on players to market Takaful products actively. And on the other side we have the Shariah Insurance Association which should promote Takaful as well. We have OJK who has made many regulations to support us. But still we need specific support and specific programs to develop the industry. Other Islamic financial institutions, both bank and non-bank, are still growing as well - but those are still far below conventional ones. So there are many aspects that still need to be improved.

On the other side, many Takaful windows don't yet have a specific SOP for Takaful – they use the same as the conventional, as long as it meets with business purposes then they can use the same ones. But there is good news, as next year, OJK will force all Takaful windows to create and manage their own SOP. And for the customers, in Indonesia (as Moch has already said) Indonesians are fairly moderate, compared to perhaps the Middle East. We are Muslim yes, but in our daily activities perhaps we do not always follow strictly the Shariah way especially in economic and business transactions. So many of our Muslim population do not know about Shariah in Muamalah (business transactions using Shariah law) and avoid Riba. So if you go to the bank, when the bank gives you high interest, they accept that because they don't know any Shariah law in return of investment type.

**“ Most Takaful companies really have a lack of commitment to put in resources ”**

The same with microTakaful – if you go to an insurance company they will tell you that it is not commercially viable. What I would like to see is the same as in Malaysia – the regulator pushing the industry a bit in order to make it grow. And in a way, so the split between window to fully fledged is a very important step, because when you are fully fledged you have to stand on your own two feet – and at the same time, inshallah, the ROE target of a Takaful operation will not necessarily be as the one of a conventional one, so that it a very important step and I hope this will happen sooner rather than later.

And returning to microTakaful, I really hope that the government or other third party organizations can help in public-private partnerships, perhaps. And the third step which at least in Malaysia has been successful, is that for any government-linked business, there is a preference for Takaful or for Islamic financing. So they place a priority on Islamic financing for their own needs, in order to grow the market. For micro especially, it really makes sense. Because on a Takaful basis, there is this sharing element, it is mutual. Everyone always things that insurance companies are in it to make profit, but when you do it on a Takaful basis, any profit ultimately goes back to the policyholder – by reduction in future contributions or even giving back money.



Srikandi

**Firas:** So my second question is – when the Takaful Insurance concept was introduced it was to offer a Shariah compliant insurance alternative, similar to Islamic banks on the banking side. Insurance penetration is still low in Indonesia - would you link it to religious reasons, or is it just because of a lack of awareness and/or lack of financial resources.

**Moch:** I think the second – no awareness and lack of money. Because for many it is just too expensive.

**Firas:** Takaful as a Shariah compliant solution is based on the concept of mutuality. Do think that – if applied correctly - this fact could promote Takaful companies in Indonesia?

**“ The Takaful industry in Indonesia must not only be Shariah compliant but must be innovative ”**

**Moch:** What I want to highlight is that here, the Takaful industry in Indonesia must not only be Shariah compliant but must be innovative. We are not facing a devoted Muslim customer who will switch as soon as there is a product that meets his faith; but someone who will continue to look at the other side of the offering, and who will pick what looks best to him. So being in this kind of market, it is also important for us a promoter to work with the industry to find the beauty of Takaful and then present it to the population that by choosing this type of model you get both financial/economic and religious/ethical benefits.

The Tabarru concept is close to the mutual concept but it also mimics the self-help community groups that Indonesians are traditionally familiar with.

**Firas:** Exactly – so they should already be familiar with the concept.

**Moch:** Yes, but in Indonesia we already have a big mutual company, Bumiputera, which has been in the market since 1912 and is very close to Indonesian culture. The concept of self-help and community is embedded in the culture.

**Srikandi:** Yes, helping each other is very close to the Indonesian culture.

**Marcel:** But you have some very big cooperatives here – even Islamic ones. But it seems it is impossible to do anything with these cooperatives, even though their involvement would be very good for Takaful. Why do you think it is not possible – because they are so loosely organized? Or because they are not economically interested?

**Srikandi:** Maybe I can help, from a practitioner’s perspective. Lack of awareness of insurance and Takaful. They need get more information about how much they can pay, what

**Moch:** What you say about spin-offs, that’s very interesting. But talking about more regulatory involvement – can you make it more specific?

**Marcel:** Well the windows have to be phased out as soon as possible, that’s one. Several companies will then lose or give back their window license and only the committed players will remain, which will be a benefit. Secondly the microTakaful industry – I know you have some plans on microinsurance already. One idea would be to do these on a Takaful basis, to promote the risk sharing element and to raise its profile and awareness of the people. Because the first time they get the product it will be a Takaful product. And the third element is for government-linked business to give priority to Takaful and Islamic methods, because that is what Malaysia has done – they had to create an agenda to promote Takaful and I think that aspect really helped the industry to grow.

**Moch:** Well just looking at the third area – this is something that perhaps makes Malaysia and Indonesia quite different. Some people see it as political will. OJK is not part of the government so I can say this. When we talk about Islamic banking, the government of Malaysia really supports it with more budget – Tabung Haji, etc. Here in Indonesia, that is really not the case. So in the Islamic banks do not really get any tangible facility from the government, and they have to deal on a daily basis with all the Islamic-specific challenges but also compete with the conventional industry, which is much older and bigger. And it is the same with Takaful. We don’t have any affirmative action from the government right now, no projects helping it. So it relies on natural growth – and that means our growth rate is really real, with no artificial help or incentive. 4% market share really is 4%, there are no boosts.

**Firas:** If you want to promote Takaful - from the government side - a split between Takaful and conventional would surely assist. Preferential treatment of Takaful companies, like in Malaysia, would be another driver. But that is not the intention right now?

**Moch:** As far as I know, there is no intention towards preferential treatment. Also we have experience of a very incubated, protected industry and it’s not good, we try to avoid it.

products are really suitable for the purpose and how to collect contributions and payments. On the other side, building reputation and trust is important. It could be high risk if we do not know how to handle them. Mostly they are in small cities and rural areas.

**Marcel:** High risk?

**Srikandi:** High risk. The moral hazard is high. We need achieve a certain volume with low distribution cost. Meanwhile we need to educate communities about products and Takaful. Moral hazard may happen for example if we cover people who are already sick or ID data is not clear, or misselling. Some of the companies have already entered the market, but the persistency ratio is very low. Socialization and education activities to those target markets is important to ensure Takaful products will help them in case of any bad things happening in the future. If you go with a credit Family Takaful, maybe it's possible because it is a mandatory product with a loan. But if we go with other individual products, we need be careful to determine the action.

In Indonesia, there is a Takaful broker that has been selling and building relationships with communities to approach this market. They make an agreement with the Takaful operator to educate and sell microTakaful. They use the Shariah approach that helping each other is a form of donation. If you give mote then you will obtain more goodness. In the selling method, we sell Takaful values rather than comparing with conventional products - for example in Takaful, we are doing business ethically, sharing surplus and helping each other. And that does show to people that there is a differentiation from the conventional.

**Moch:** I agree with what Srikandi said. And to expand on that, I think there is a need to improve not only on the Takaful side but also with the cooperatives and in the microfinance area. We face a huge problem in this. It is a very traditional area but it is mostly dependent on a couple of managers, and we can't expect people to perform all the time. And it is not regulated yet.

There are many microfinance operators in Indonesia simply because they don't want to be banks, and don't want to be regulated as banks. There are lots of small 'people's banks' but they don't want to be ruled by the banking regime, they would then lose that cooperative aspect of helping each other. We assume that cooperatives are good. But when they try to help their members, they find that when giving them access to finance or loans, they also need to give them some protection. And when the perils come, they cannot handle them. So it needs a broker, to act as a bridge between the insurers, the Takaful operators – who recognize a risk there. We have only had national identity numbers for the last few years. So fraud is still endemic in that environment, for example. So I can understand that operators are cautious.

**Firas:** So the share of Islamic banking here is less than 5%, and Takaful is below 5% as well?

**Moch:** Yes, Takaful is around 4.7%.



**Firas:** Is this driven by the banks?

**Srikandi:** No it is mainly through agencies. If you look at Islamic banking in Indonesia, they are small compared to conventional banks in terms of assets. So there is not much contribution you can get from the banks. So agency distribution is the predominant channel. Not the bancaTakaful.

**Marcel:** You both mentioned product innovation as the way forward. But everyone says this – which areas do you think you can move forward in?

**Srikandi:** Currently, the production is driven by unit-linked products. We need to be careful, as unit-linked products should be sold to people who have knowledge of investment - which is the middle to affluent segment. Unit-linked products do not meet the needs of the low income market where their understanding of investment risk is low. So we need create simple, easy to understand products where the risk is easily understood and the claims process is simple and fast. So, we need to create additional products beyond unit-linked. These products should be backed up by conservative and moderate investment risk such as money market and Sukuk.

**Marcel:** The challenge is that the commission you get as an agent for these products is much lower than for a unit-linked product. So the agents don't have an incentive to sell them.

**Srikandi:** If agents sell non-unit linked products to low level income segments, they need sell many policies because the contribution is tiny, which means they don't make much commission. Unit-linked give you very high commission – the best products give basic commission of up to 30%. 90% of products sold through the agency distribution channel are unit-linked. To manage contribution cost efficiently, we need to determine an appropriate distribution channel for low income products.

**Firas:** So what is the different between a conventional and an Islamic?

**Srikandi:** Unit-linked uses an Islamic investment vehicle such as equity funds, balanced funds, Sukuk. Takaful products also give additional benefit such as underwriting surplus, if any, for eligible customers who did not claim within the underwriting surplus calculation.

**Moch:** Let me talk about the survey we did earlier this year. When we asked what kind of protection was most important, the majority of the audience mentioned education first, then health and then general and property protection third. So if you put education as the most important, you need something to protect savings from inflation etc. And if someone sells you a unit-linked product, which should have a better result than the conventional, assuming the underlying product is good, then they will try to tap into that market. I think most of us are driven by that motive – trying to save some money through protection. They don't really look at whether it is Takaful or not. I think it also depends on who sells it. There are so many agents in Indonesia now that if someone has a niece or a nephew or a friend – if they sell you Takaful, you buy Takaful. If they sell conventional insurance, you buy that.

**Firas:** As it seems the government prefers a competitive market situation without special promotion of Takaful operators. This means Takaful companies need to compete by providing excellent products and services and this may take some time. But in case of Takaful windows I trust they are already in a position to offer similar products and services as their mother companies. In addition they share the surpluses with their policyholder. This should be a great competitive edge and Takaful windows should benefit from it! Why is that not the case?

**Marcel:** Again, lack of awareness. Even with the companies we work with, I have to say that the people selling the product, the agents, don't always understand how Takaful works. And then also as I mentioned before, the incentive of the companies is not really good for Takaful, so they lose out on conventional. So that is a big challenge we are seeing.

**Moch:** But there is something that you have to understand about Indonesian society. Indonesian society is in my view, very independent. What I mean by that is that every person feels that they can go in the direction he or she wants. Even under a very repressive regime, like Suharto, we still survived. But now the people's mindset is different. They are moving towards a new understanding, but it has to be gradual. You cannot ask them to make a quantum leap – it is not possible. It has to happen slowly.

**Firas:** Sure, but if I go to a Takaful window and ask for an insurance product, it would be similar to the conventional one as far as insurance protection is concerned. So, what is the advantage for me to go to Takaful?

**Srikandi:** You will get the surplus if any, you have an alternative investment portfolio which is under an Islamic investment vehicle.

**Firas:** Right – so if it is the same price and the same benefit, but I get something extra, which is the surplus-sharing, why wouldn't I go to the Takaful window? Aren't mother companies assisting their windows?

**Moch:** But this is the key, Firas. This is what happens today, or in three years. But in 10 years, we don't know what will happen. I don't know how my children will behave.

**Firas:** Srikandi, what is your portfolio proportion in comparison to the conventional business?

**Srikandi:** Last year, Takaful was 17% of total premiums. This year we are expecting around 20%.

**Firas:** So 80% goes to conventional, even though the Takaful product would share the surplus?

**Marcel:** But as she said, the returns on the conventional unit-linked might be higher, because of what they can invest in.

**Srikandi:** Agents are comfortable selling conventional products, so we need to change the paradigm of how to sell Takaful and how to make access to the Takaful market easier. On the other side, sometimes the return on investment on the conventional side is higher than Shariah. In conventional funds, they can put money in conventional or Shariah investment vehicles. On the conventional side, they also have the financing sector which sometimes gives more return than Shariah.

In the market, agents who sell both conventional and Takaful products have other challenges, including that when they sell Takaful products they need effort to explain the Takaful concept, and they are afraid of getting it wrong when customers ask about Shariah law.

**“ Agents are comfortable selling conventional products, so we need to change the paradigm of how to sell Takaful and how to make access to the Takaful market easier ”**

**Firas:** I agree and that is surely true on the Life side, but what about the Non-Life sector? The market share of conventional insurers is also much bigger than their Takaful windows. Could the window structure be a reason?

**Srikandi:** I agree, and I think maybe if the government insists on a spin-off that is the key. Because then companies would have to focus on driving forward their businesses on their own.

**IFN: Are there any lessons that Indonesia could learn from Malaysia or the Middle East? Perhaps aside from political will or government support?**

**Marcel:** I think that in most other countries, Takaful operators are fully fledged so they have to stand on their own two feet. And also, it is an issue of human resources. That is not



unique to Indonesia, but what will happen is that the number of companies out of the 48 currently offering Takaful solutions, if they have to spin-off, will probably reduce a lot. But at the moment even the five fully fledged firms are struggling a little bit. You have to have a strong shareholder backing. Really, what you need to do here is sell the growth story. That is what encouraged foreign companies to come into Malaysia and set up JVs – SunLife recently came in and set up with Khazanah for example. Even local investors want that. Growth is still in double digits and there is still a low insurance penetration. So ideally you want to tap into areas that conventional might not want to go, like maybe the low and middle income areas. But then it is a question of profitability, and the foreign investor might say well why should I invest in these lower profit areas instead of looking at conventional insurance in higher income markets and sectors?

**IFN:** So what can be done to change this or push it forward?

**Firas:** Well in Malaysia, Takaful was promoted by the government, and the same is true for Saudi Arabia. But I don't think it should be done this way here. The sector should grow by standing up on its own. The best would be to focus on the mutual aspect of Takaful. This could be achieved by actively involving policyholders in the operational structure of the Takaful operators. As an example they could have a representation on the board of directors or board committees and it would be good to give them some rights to the distribution of the policyholder surplus. This would give policyholders the feeling of ownership and differentiate Takaful from conventional Insurance.

**Marcel:** One area of interest is that you said you have developed a microTakaful product. That's an area you really could try to work with the regulator to promote. Just having the product will not be enough to sell it – you need the third parties to distribute it. In Indonesia I think this is one of the four areas you need to promote. And this is an area where Takaful could compete very strongly against the conventional as they do not participate in this area with any conviction.

**Srikandi:** I think for the middle and upper market, companies can compete and grow on their own, because there is profit there. But for the lower income level, we need support from the regulator. They are not giving it to us yet. Because for

a Takaful operator, they can't go there because there is not much profit yet. They need to give us funding for socialization, education, rather than us using our own budget. If the government gives us that, actively, then we can increase our market share and that makes it worth it for us.

**Firas:** But it seems like the government will not go in, so what will you do?

**Srikandi:** No, this is part of the government's program this year – but only for microTakaful.

**Moch:** When we talk about high income people, anyone wants to sell to them because there is money there. We understand that it is not the same at the other end. Also during the crisis, the higher end were able to self-sustain. For the lower end we need to try and achieve that, help them be able to finance themselves and use the financial system – so we do have a grand design of microinsurance including microTakaful. But it is not so easy to develop a standardized product that can be mass-sold – we are working towards it. We also plan to make a big effort to raise awareness of this product.

**“ Muslims really need, but using the same paradigm as the insurance industry – for example, why is there no property or General Takaful selling protection for tractors, for small farmers? ”**

But the other aspect of Takaful and insurance in Indonesia right now is the Shariah compliant versus Shariah-based products. We have to understand that associations do not have any thinktanks on what kind of product is actually needed by the population. If you ask people about their needs, they might not really have any idea either. So unlike other sectors that may have an active research component, we do not have that yet. We need to ask what Indonesian Muslims really need, but using the same paradigm as the insurance industry – for example, why is there no property or General Takaful selling protection for tractors, for small farmers? Most small farmers I can safely say are Muslim. But there are so many firms wanting to sell insurance for motorcycles but not for farm equipment.

**Firas:** But this is a normal risk. It's not Muslim-specific like Hajj or Umrah or similar.

**Moch:** Yes, but it is an opportunity that no one has offered a product in yet. Takaful should be looking at areas like this. But

yes, you mention Umrah. We have 1.5 million people every year doing that pilgrimage, and we do not have any kind of comprehensive Takaful protection for that. In Malaysia, it says everyone who does Umrah has to take Umrah insurance.

**Firas:** There are existing Takaful solutions in other countries!

**Moch:** For Hajj yes, but for Umrah none. Or for example, there is no law requiring third party liability. Some insurers have come to the government asking them to introduce this. But it is not here yet. So there are so many questions still in Indonesia. And we have not had much success with mandatory insurance programs. We do have some employer pension and provident funds, but not many compared to Malaysia for example.

In my belief, don't be surprised if in the future Indonesian people become more demanding about Shariah compliant products, compared to what we have today – because I think the growth will come from the bottom up rather than from the top down.

**IFN:** *We are coming to the end of the session and I've largely let you just talk on; because you are asking all the questions you want to know! [Laughter] But is there anything we have not yet covered, or any question you think is relevant that has not been asked yet?*

**Moch:** Well actually, we do have some gentlemen here from the reTakaful industry – I would like to ask why there is no interest in this yet. Indonesia is deficit in reinsurance, including reTakaful. Malaysia has something like US\$9 million I believe – why is there no interest in international companies coming to Indonesia and doing business here.

**“ Don't be surprised if in the future Indonesian people become more demanding about Shariah compliant products ”**

**Firas:** Do you mean setting up in Indonesia?

**Moch:** Yes, I mean we have the tax benefits etc, so why not?

**Marcel:** It's very simple, it's a question of the gross potential. It's not something, at least in Swiss Re's case, which is currently on the cards. It could happen, but I would have to convince my senior management that the growth is there. It's a chicken and egg situation really. At this moment I can tell you – we tried to create business – we visited many companies – but usually the quantity of actual Takaful business available is very small, and it just doesn't make it efficient for us. That's the big challenge we face. If I could

sell the growth story that in the next five years, business will grow say, 50% per year (just making up the numbers) then it is an easy sell. But at the moment, conventional is so large and Takaful is so small that they think why invest resources. I mean the idea would be to have a local operation, eventually, but it's really a question of how much capital you would have to invest compared to how much business you can generate.

**Firas:** Being registered in Dubai, tax benefits wouldn't affect us at the current stage. For us it would be a question of costs and profitability. The attractiveness of the Indonesian reTakaful market will surely grow in the future and with population of 200 million Muslims I expect it to do so, but it needs time and effort.

**Marcel:** And generally reinsurance and reTakaful is an international business anyway. What would be the advantage for you to have operators here, compared to the situation now? Do you feel it would create more capacity, more support for the local industry?

**Moch:** Yes, I think so. That is my impression. In my view, expertise we could leverage is by having reTakaful companies close to your side. Because they don't do day to day business, so they have more time to develop the industry, work on the concepts. For example, Munich Re are championing microinsurance, because they don't have to do day to day sales work. In my opinion reTakaful could have a huge impact on the Indonesian industry through innovation, through human capital. I think it has had this effect in Malaysia.

**Marcel:** Well, we have been going to individual companies promoting that we want to help – but I feel that people are not always so much interested. This afternoon, I am actually going to meet the Shariah Insurance Association to talk about how we can help – and we do want to assist. But we can do that from KL, we can help the industry from there, as long as it is a win-win for us! But for the last few years we have been going to local companies saying we want to develop products, give training – and have not met with a lot of interest. Now, in a next step, we will also go to the Shariah Insurance Association and see how that approach will work.

**IFN:** *Firas, you mentioned you would like to touch upon the regulatory aspects a little more?*

**Firas:** Will the new Insurance/Takaful Act favor a special Takaful model such as the Wakalah model, or will operators be free to choose whatever model they want?

**Moch:** I think that what we have achieved in the upcoming law is that there is Takaful operation in Indonesia. The last law, of 1992, did not recognize it at all. Then we managed to introduce it as a chapter in the law. And there should also be some regulation in the new law which solely talks about Takaful – about governance, about how to support the Takaful industry.

**Firas:** I am of the opinion, that it is very important to regulate the treatment of the 'interest-free loan' (Qard Hasan). As you know, all Takaful models require a clear split between the policyholders' fund and shareholders' fund. The



questionable practice followed in some countries is that although there is a deficit on the policyholder side, which is financed by an interest-free loan, no special provisions are requested on the shareholder side and as a consequence the shareholder equity remains unaffected by the mentioned loan. Shareholders may not recognize that the consolidated results (policyholder and shareholder) are in a negative position and this could be dangerously misleading.

**Moch:** We have just made it standard, 1 to 1 I think. But I will have to check. In most cases, I think we are still struggling on the accounting aspect.

**Srikandi:** Sorry, I am not clear. So what is your suggestion?

**Firas:** My recommendation is to follow IFRS or a similar standard. This would take care of the problem: i.e., whenever there is a deficit, there will be an equal provision affecting the shareholder equity.

**Marcel:** I heard a story that some companies in the Middle East charged a Wakalah fee of 75%, simply to increase the contribution in the shareholders fund, and didn't take care at all of the risk fund.

**Firas:** Yes, some operators used to charge high fees – but now the fee is around 20-25%. But it can happen, that the participant side is in a loss, whereas the shareholders' side has profits due to the Wakalah fee - and profits are distributed to the shareholder. The question is who will eventually burden the interest-free loan.

**IFN: Well to wind up, perhaps to conclude we could go round the table and each of you could summarize what you think is the biggest requirement or need within the Indonesian Takaful industry to help it grow. Marcel, if we could start with you?**

**Marcel:** I think it is not just one thing – we have touched on many issues. For the industry to grow it needs a favorable regulatory environment – I'm not saying it has to push Islamic finance but it at least has to give it the chance to grow. Another issue is the spin-off. Another is the Shariah Association, which should play a more important role than it has in the past, by education and training agents.

MicroTakaful products should be developed. And finally, you still have to convince investors, ultimately, that Takaful is a growth area worthwhile investing in – be it local or foreign investors. That ultimately is what will grow the industry.

**Firas:** The regulatory environment is of course a key topic. It is very important, but as it seems it will take some time to be fully implemented. As a result the Takaful market needs to be driven by the Takaful operators themselves. The quality of the offered products and services is in this respect essential. It will also be very important for the Takaful operators to differentiate themselves from conventional insurance and to show why Takaful could be a real alternative for anyone, whether Muslim or not. As mentioned earlier the mutual/cooperative aspect of Takaful should serve here.

**Srikandi:** I think the big issue at the moment is how Takaful players focus on Takaful business. So what is important for me is to see the regulators issue spin-off rules from windows to fully-fledged companies as soon as possible, and make the transition as smooth as possible, so the windows do not miss out on business as they go through the process over the next five years. As well, perhaps the regulator needs to determine a standard competency for Takaful operators: for risk management, for Shariah experts, to ensure that windows can operate and manage properly and prudently.

**Moch:** I think most aspects are already mentioned, but I would like to raise one angle. The Takaful industry is part of Islamic finance as a whole, and we should also synchronize with other sectors within the industry – for example bancaTakaful. We cannot expect to have walk-in customers – we have to promote it through distribution channels. To be able to attract general attention towards Takaful and away from conventional insurance, we have to work very hard, especially in an environment where the majority do not understand the concept of protection. This could be from a regulator, a player, an association – but I think any help in this area would be welcomed.

And finally, I think we would like to say thank you to IFN for organizing this very useful and rewarding discussion.

**IFN: Well thank you all very much for participating, and I hope it was helpful to you all.☺**



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