Winning essay

A strategic vision for the Asian insurance/reinsurance industry

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The Vision

My vision for the Asia (re)insurance industry is that it will one day be a dynamic, vibrant and self-sustainable environment capable of providing financial assurance by retaining all risks that relate to Asia. This would be characterized by:

a. A marketplace with a high degree of risk awareness by buyers and providers of life and non-life insurance;
b. An (re)insurance industry with deep local market knowledge in understanding the risks and perils that Asia is exposed to, and how they are quantified;
c. Risk capital of depth and flexibility that is capable of retaining all the risks originating out of Asia, by way of insurance funds or the capital markets;
d. A supportive and leading regulatory framework which encourages development while exercising prudent risk management; and
e. A progressive and deep talent pool of practitioners equipped with technical and managerial capabilities to run global organisations.

The Asian (re)insurance industry is in a dynamic and vibrant state

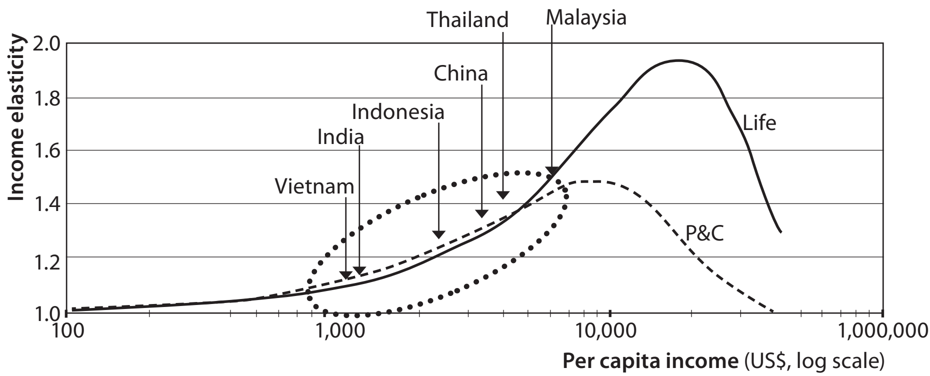
The Asian continent has over 50 countries in various stages of economic development with various sizes and sophistication levels in their respective life and non-life markets. Whilst there is significant market growth opportunity (Asian insurance market expected to grow at 8.7%[1] CAGR until 2020, compared to the rest of the world growing at 4.9% CAGR for the same period) driven by the underlying catalysts of asset buildup, wealth accumulation and longevity, there is also a diverse range of local and foreign market players who have created a highly competitive landscape. Globalisation has opened up Asia to plenty of international players but the flood of capacity has also caused some markets to suffer sustained depression of pricing. In addition, the dismantling of tariffs in countries hoping to enter the World Trade Organization has also created greater pricing pressure. However, new opportunities are constantly opening up due to the fast growth of markets with new products and services being developed to meet market needs.

To this dynamic and growing market, the characterisation of my vision would be:

1) An Asian (re)insurance marketplace with high degree of risk awareness

The various insurance markets in Asia are in different phases of growth, and hence, have different degrees of risk understanding. From the highly advanced markets of Japan and Australia, to the mature markets of South Korea, Taiwan, Singapore, Malaysia and Hong Kong, to the upcoming giants of China and India, and finally the high potential markets of Vietnam, Indonesia and the Middle East, the degree of risk awareness varies greatly. Swiss Re's S-Curve effect1 describes insurance spending growing faster than the general economic growth rate, as GDP per capita income nears US$1,000 and rises particularly fast when GDP per capita levels are in the range of US$1,000 to US$10,000. Not coincidentally, many of Asia's high growth markets are at the cusp of significant insurance market growth (Fig: 1). To this end,

Figure 1: S-Curve effect



Swiss Re's S-Curve effect implies that many of Asia's growing economies are at the cusp of accelerated Insurance growth

Asia's share of the global world premium is expected to grow from 24.3%1 in 2009 to 32.4%1 in 2020.

The growth in insurance spend across Asia, will and should be as a result of an increasing awareness of the risk landscape which Asia is exposed to. As the world's most populous continent, and one which is exposed to numerous natural and man-made perils, the awareness of how insurance or reinsurance may help mitigate financial devastation, whether one is a resident requiring life insurance coverage or an asset owner (including public and private enterprises) requiring non-life coverage, is crucial.

As witnessed by the natural catastrophes that Asia experienced in 2011 (Tohoku Earthquake and Tsunami, Thailand Floods and New Zealand Earthquakes), the cost of natural and man-made perils on human life and assets owners are significant and a huge burden that can be shared by (re)insurance risk carriers. Together with governments, Asian (re)insurance risk carriers, can help to deepen risk awareness and take up through schemes like Taiwan's Residential Earthquake Insurance Fund (TRIEF) or New Zealand's Earthquake Commission. On the life side, financial education on wealth management and preservation will play an important role to deepen insurance take-up as the wealth buildup in Asia gains momentum. Of particular interest would be the engagement of the growing Asian middle class by insurers and governments alike, in cultivating healthy and prudent insurance planning and purchases through financial literacy and transparency. Singapore's Income has been particularly successful in growing market share in an already mature market by promoting transparency in wordings, proactive marketplace engagement and innovative products to meet market needs.

2) An Asian (re)insurance marketplace with deep local market knowledge and understanding of risks and perils

The Asian (re)insurance marketplace has a unique landscape which requires much investment into greater understanding of the risks and perils. For the life segment, greater understanding of the impact of infectious diseases (SARS, bird flu, dengue fever, for example) as well as a fast aging population and related risks would impact populations in Asia. Similarly for the non-life sector, the issues of food and water security, agriculture, energy and natural catastrophes present many challenges to the Asian (re)insurance marketplace which need deeper understanding. While studies into these areas, and many others, are well documented, sufficient knowledge is still lacking to develop effective solutions. Risk carriers in Asia must appreciate that whilst upfront investment into research may be high, there are first-mover advantages to developing effective solutions to these problems, where significant margins can be reaped.

3) An Asian (re)insurance marketplace with depth and flexibility of risk capital

Whilst there is currently significant insurance and reinsurance capital deployed by local and global insurance carriers in Asia, this is not a status quo that can be perpetually expected. Solvency II will impose significant pressure on global carriers to be highly discerning on the allocation of capital, especially to businesses which are marginal. We have witnessed the disruption to Asian markets caused by global players when capacity is withdrawn to shore up balance sheets impacted by 9/11 and the global financial crisis. Hence, for the long term stability of the Asian industry, it is imperative for more locally based capital that would not be disrupted by global events to be built up.

Already, Japanese and Australian risk carriers have ventured out of their home markets, while South Korean and Chinese players are starting to do likewise. These inter-regional developments have been aided by a deep sense of cultural alignment and market place proximity. At the same time, active global players have provided capital and expertise to Asian markets over many years. An ideal state would be for local Asian risk carriers to be the bedrock of risk capacity that is substantially capable of carrying most of the risks in Asia, with global risk capacity providers such as Lloyd's of London adding additional buffer or specialist risks capabilities. To this end, the large Japanese, South Korean, Chinese, Indian markets have been highly successful in creating a largely local capacity bedrock, and to achieve the same of Asian capacity as a bedrock for Asian risks therefore would not be impossible.

In terms of the flexibility of risk capital, we have seen that mature western markets have evolved to extensively use capital market solutions and alternative risk transfer tools to further enhance risk capacity. The use of hybrid capital in Asia is only just beginning and hopefully, in the near future, the use of securitisation to tap the huge pool of non-traditional insurance risk capacity would make risk premiums cheaper to carry. Developments have already taken place in the form of Japanese earthquake risks being borne by catastrophe bonds, and more recently, the TCIP 's (Turkish Catastrophe Insurance Pool) inaugural catastrophe bond issuance. Other peak exposures to address could be Chinese earthquake risks (in peak industrial zones like Guangzhou, Shanghai and Hua nan) or Asian High Net Worth mortality cover which perhaps securitisation could provide a viable capacity solution.

4) An Asian (re)insurance marketplace with supportive and leading regulatory framework

Across the diverse spectrum of insurance regulators in Asia, we see different degrees of sophistication to manage their respective varying stages of development. The transparency and challenges of operating across these varying jurisdictions also vary greatly and as a result, the marketplace cannot always operate smoothly. Much more can be done by individual nation's central banks or finance ministries in promoting and adopting a more Asian-centric framework to jointly bring up the support for (re)insurance in Asia as a trading bloc. It is evident that economic trading blocs are gradually forming across the globe, and with economic growth gradually pivoting towards Asia, it is perhaps also imperative that Asian regulators strengthen their support and align their regulatory framework for smoother intra-Asian insurance development. As many of the insurance risk carries in big markets like China, Japan and South Korea have started to expand along with their clients to Southeast Asia, regulators on both sides could work together to align their supervisory frameworks and facilitate business growth whilst preventing regulatory arbitrage.

5) An Asian (re)insurance marketplace with a progressive and deep pool of practitioners

No marketplace can be sustainable if there is a lack of talent pool to grow and develop. Yet, this important element of the financial services sector is lacking in the Asian (re)insurance marketplace. The industry has failed to attract and retain the best talent, as it is often viewed as less attractive when compared to banking and finance both in terms of profile and remuneration. The insurance and reinsurance industry in Asia is highly dependent on actuarial capabilities, and even though there have been many Asian actuaries trained over the years, not many have chosen to carve a career in the industry; neither are there many Asians occupying the highest ranks of Asian risk carriers. Whilst it is common to see actuaries in the pricing and reserving functions of life insurance companies, it is much less common to see non-life companies extensively employ actuaries, often relying instead on third party consultants for actuarial support.

A continued low emphasis approach to technical capabilities in managing risk carriers will have serious implications on the sustainability of the sector, and across the value chain of insurance underwriting management. Several areas in which talent has to be built up include:

a) Risk assessment – technical competency in understanding the risk;

b) Risk pricing – sufficient data/experience in quantifying the exposures;
c) Risk accumulation – robust modeling and exposure tracking ability;
d) Claims management – data accuracy;
e) Claims reserving – sufficient experience and data transparency; and
f) Investment management – skill in strategic and tactical asset allocation

6) Asians have a vested interest in ensuring the continued strengthening of the (re)insurance marketplace

For those of us living in Asia and calling it home, the onus is on all of us to take a serious stance in the healthy and sustainable development of the market. Should there be another global risk capacity crunch (such as the Asian financial crisis for the banking sector), Asia could potentially face another huge spike in risk premiums or even withdrawal of coverage altogether (as witnessed by Asian Insurers after 9/11 and by the Thai market after the 2011 floods). These would be issues faced not only by individuals and corporates, but also sovereign governments. Asia is now leading the charge on global economic growth and is in an ideal position to effect much needed change in the (re)insurance sector and make the necessary changes to provide for sustainable growth. Investments into understanding risks unique to Asia have to be made, talent and capabilities have to be groomed, and perceptions have to be changed. Perhaps even tariffs have to be imposed to ensure that sufficient premium is charged for undertaking certain essential coverage (such as health insurance in Singapore, covered by the government-driven MediShield plans).

There is an opportunity for the big boys like Japan, South Korea, China, Australia and India to work together to lead in the changes, but this would require strong political will to jointly strengthen this essential component of the financial services sector.

I believe that my vision for a dynamic, vibrant and self-sustainable environment capable of providing financial assurance by retaining all risks that relate to Asia is not impossible and would very much hope to see it being reality.