

Takaful in Europe: A fertile ground

The expansion of takaful may be more dramatic in Western Europe than in the traditional markets of Middle East and East Asia, provided the right products and regulatory balance can be found.

By Mr Ridwan Abbas



Mosque of Rome, Italy

The expansion of the takaful industry has been a growing feature of the insurance landscape in recent times. While the initial phase was dominated by domestic operators in Sudan, Malaysia and the Middle East, the latter stages of growth has enticed big conventional insurance and reinsurance providers – Allianz, Munich Re, Swiss Re etc – to enter the takaful fold.

Although such major players have moved beyond their home markets and into the underpenetrated insurance segment in Muslim countries, a reverse trend looks imminent as growing calls are heard for the takaful industry to look towards the West in its next phase of growth.

While takaful has made considerable headway in Muslim-majority states, the awareness and tendency to purchase coverage is undoubtedly much greater in Western jurisdictions than in developing countries. The significant disparity can be seen in a recent Swiss Re *sigma* report which revealed that general insurance spending per capita in North America and Europe stood at approximately US\$2,000 and \$1,000 respectively, while the Middle East came in at just \$56.

With roughly 53 million Muslims scattered across Europe, including 20 million in the European Union where insurance is viewed as something expedient rather than the exotic, takaful would seemingly lend itself to a much



Mr Gul Khan

informed and more inclined market segment.

“These customers are already buying insurance and are obviously much more aware about protection, especially in Europe and the US, and the challenge for all of us is to make products relevant for them,” said Mr Gul Khan, Global Head of Wealth Management at HSBC Amanah.

UK in pole position

At present, London-based Principle Insurance remains the only takaful operator in Europe so far – offering motor

and home insurance products in the UK since 2008. Many believe it is only a matter of time before others come on-board, particularly as Europe opens itself up to the Islamic financial services sector.

In its Budget 2009 report, the UK treasury announced provision of relief from tax on capital gains and capital allowance rules to encourage Islamic debt issuance in the form of sukuk, all as part of its “ongoing drive to promote the UK as a centre for Islamic finance”.

“Now the UK government is very keen to promote Islamic finance, to promote Islamic banking and Islamic insurance arrangements. Of course, the London market in the form of Lloyd’s has led the world in insurance. I think we can use the UK as a springboard with regards to penetration into other parts of Europe,” said Lord Mohamed Sheikh, a Conservative Party member in the British House of Lords.



Lord Mohamed Sheikh

Other European jurisdictions, especially France, have also been quite vocal of late in their pronouncements to attract Islamic financial services to the country. The French government has recently announced plans to adjust its fiscal and legal framework to render it friendlier to Islamic finance.

The financial regulatory body in Malta has also expressed its intentions to release a public consultation document this year regarding takaful and sukuk, after undergoing a similar exercise with financial services stakeholders last year on the topic of Islamic finance in Malta.

From a regulatory standpoint, the passporting process and harmonisation of European Union (EU) laws is a positive for potential takaful operators – as authorisation in one EU jurisdiction would enable it to carry out business in other member states.

In that respect, choosing an appropriate host regulator as a launch pad for developing operations in other parts of Europe becomes important and the UK is seemingly

ahead of the game, according to Ms Susan Dingwall, Partner at Norton Rose.

"You have to choose a host regulator that understands takaful and in the UK, we have the first takaful operator that was authorised last year. So the UK regulatory authority has been through that process and understands that there are a number of other takaful operators waiting to be authorised and as we go along, that process gets much easier and streamlined," explained Ms Dingwall at a recent takaful industry gathering.



Ms Susan Dingwall

Like in other parts of the world, the potential for takaful bears considerable relation to levels of disposable income. In this regard, British Muslims are ahead of their Muslim counterparts elsewhere in Europe.

"We have to penetrate into areas where there is a high take-up rate of insurance and where there is affluence. And if you look at Muslims in the UK, a lot of them are very affluent," said Lord Mohamed Sheikh.

In fact, the Muslim population GDP per capita indicates British Muslims as having the strongest purchasing power among Muslims in Western Europe – followed by those in France, Germany, Belgium and Holland.

Opportunities in takaful

At present, the focus in providing Islamic financial services in Europe remains primarily in the area of banking. But as the retail Islamic banking pie grows, takaful would serve as a key complimentary offering for consumers seeking Shariah-compliant products.

For instance, a Shariah-compliant home financing programme would derive better value should homeowners' takaful be available. Such is the case with Principle Insurance, which launched a takaful home insurance last April to compliment the growing demand for Shariah-compliant mortgage schemes in the UK.



Mr Richard Thomas

"For those who opt for car finance, they would also need to take out car insurance, and those who seek pension schemes would have to have family takaful. And until a wide range of products are available, no single product is going to be successful," said Mr Richard Thomas, Chairman of Gatehouse Bank plc which operates a Shariah-compliant investment bank in London.

"So Islamic banking in the UK or Germany or France will only be successful when potential clients can get a good range of competitive services and insurance would be a very big part of that," he added.

Many in the industry are also pointing out the vast opportunities to develop family takaful in both the developing and developed markets. The relatively youthful Muslim demographic – 60% of Muslims worldwide are under the age of 35 – can be a point of leverage if suitable family plans are introduced and effectively marketed.

Indeed, conventional insurance products have constantly evolved to meet the social and economic needs of the population. Hence, the impending retirement of the "baby-boomer" generation signifies huge potential for retirement solutions, including Shariah-compliant ones.

No doubt, state pension schemes are institutionalised in much of Western Europe – with contributions from the working population of the society distributed to its pool of pensioners. But the system has come under serious pressure as an ageing population means catering to huge numbers of post-war "baby-boomer" pensioners.

Thus, experts have predicted the demand for personal pension products to grow dramatically in the next decade, and Muslims living in the West similarly have a real demand for Shariah-compliant private pension plans.

So far, a number of takaful operators such as Allianz and SABB Takaful are in various stages of designing Islamic annuities to be introduced to the market.

Reaching out to non-Muslims

The low proportion of Muslims in Europe also brings about the question of whether takaful would be able to penetrate the non-Muslim segment of the population as well.

Though Islamic financial services are barely understood by the Western consumer, the concept of mutuality and co-operative insurance is indeed present in many European countries where some of the largest cooperative and mutual insurance movements reside. As the idea of mutual support evident in takaful is closely aligned to this, takaful has a genuine opportunity to make headway with non-Muslims compared to other offerings in the Islamic finance universe.

"I think it will be quite an easy sell as it strikes a chord in the hearts of people because they know that takaful represents mutual support. And this thing about supporting one another is there in the minds of people whereas when you are talking about Islamic banking and riba'-free environment, you have to ask people to adjust their psychology," said Dr Alberto Brugnoli, President and founding member of ASSAIF, a European Islamic finance consultancy based in Milan.



Dr Alberto Brugnoli

He added the growing affinity towards "ethical finance", especially in the wake of the global financial crisis, is a positive development for Shariah-compliant products.

"We have this enormous environment called ethical finance which has a keen interest in Shariah-compliant products, and a number of interviews I ran across Italy, Spain, France and the UK showed a keen interest amongst devout Christians and Jews for Shariah-compliant offerings," revealed Dr Brugnoli.

Cost-effectiveness

But ultimately, the issue of cost-competitiveness has to be factored into the equation. While a number of Muslims are willing to pay the premium attached to takaful and other Islamic finance products, others are not quite as forthcoming. While higher service standards and delivery may go some way towards mitigating the extra cost, attaining prices competitive to conventional products remains a major goal.

But as the takaful industry builds up a critical mass, economies of scale and standardisation would gradually bring about greater price-competitiveness, according to Mr Thomas.

He also believes the mispricing of products in conven-

tional finance, which has come to bear amid the current crisis, will force a more level playing field for takaful and other Islamic financial service providers in the long run.

“The cost of lending money and the cost of other products have been way too low (in conventional finance) in comparison to what was sustainable. People do not realise that it is in effect mispricing at the front end which has been heavily discounted and we are paying for it now with billions of dollars in this crisis – which is a combination of effects including mispricing.

“I see that the cost of conventional finance will have to rise significantly whereas the Islamic market has been fairly priced all along. And when you have a more level playing field, that is the opportunity for the Islamic market to show its real benefits,” explained Mr Thomas.

Several industry observers have repeatedly mentioned the provision for surplus distribution in takaful, which is not mandated in conventional insurance, to be advantageous in providing a distinct benefit to customers.

Key considerations

One of the biggest challenges for takaful operators is creating adequate consumer awareness, with many Muslims still living under the misconception that insurance is antithetical to the principles of Islam. But even for Muslims conscious of takaful as a religiously validated alternative to conventional insurance, it would be misguided to view them in a monolithic fashion.

“One often sees forecasts that start with the difference between insurance penetration in Muslim countries and in the West and directly deduce the market potential from it – as if Muslims had a switch on their back where you just offer them Shariah-compliant products and they start buying takaful policies. It is more complicated than that in the Middle East and it is even more complicated in the West, with Muslims living in a non-Muslim environment where all their neighbours have policies and coverage in place. So they are already used to insurance,” said Dr Ludwig Stiftl, Chief Executive Officer, Munich Re Retakaful.



Dr Ludwig Stiftl

“Still, Shariah counts for these people in a number of ways – not only in terms of compliance and, interestingly, not only for those who consider themselves devout or traditional. Shariah is a point of reference for the identity of Muslims and has relevance throughout different groups.”

Hence not unlike conventional insurance, the key lies in crafting the right products in niche markets based on the over-riding sociological needs.

Takaful operators may also face regulatory challenges unique to operations in the EU. The Solvency II capital adequacy regime for insurance firms, which was adopted by the European Parliament in April, could pose a challenge for takaful companies in meeting solvency and risk-management guidelines.

The myriad of issues include investment compliance, where regulations concerning “concentration risk” may require takaful operators to have a sufficiently diversified portfolio within and across certain asset classes.

But the shortage of Shariah-compliant assets – particularly relating to sukuk within the EU – stands as a major hurdle for takaful operators, and one which Islamic capital market stakeholders have to address effectively.

EU governments have demonstrated awareness towards the problem and are considering solutions, including the real possibility of issuing sovereign and even corporate sukuk out of Europe.

Finally, while there are enough compelling reasons for takaful providers to enter into Europe, the realities emanating from the credit crunch means that insurers face the dilemma of deploying diminished resources into uncharted territory.

But with a well-defined Muslim segment alongside scores of non-Muslims availing themselves on the basis of faith, ethical considerations or pure economics, takaful operators in Europe have a potentially bright prospect should they find the right solutions for discerning customers. ■

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