

...extending the Shariah-Compliant supply chain

THE TAKAFUL SUMMIT 2009

RETAKAFUL OPPORTUNITIES & CHALLENGES

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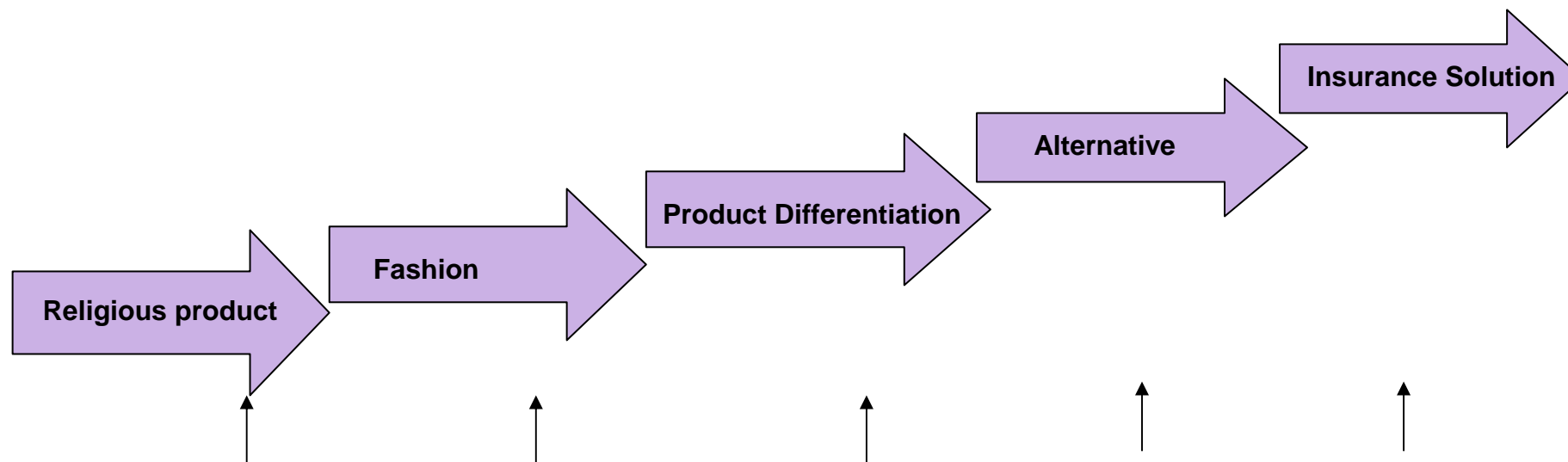
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1. Evolution of Takaful (Asian Experience)



Initiators :	Operators	Insured Muslims	Insurance companies	General Public	Risk owners
Status :	Yes	Yes	Yes	Yes/No	??

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2. Unique Significance to Industry

Similarity to Reinsurance	Unique to Takaful Industry
<ul style="list-style-type: none"> • Risk Management Mechanism <ul style="list-style-type: none"> - Spread across larger pool • Protection to Takaful Funds <ul style="list-style-type: none"> - TOs :- still small fund size but growing • Asset Management <ul style="list-style-type: none"> - Contingent Asset • Value Added Services 	<ul style="list-style-type: none"> • Shariah elements <ul style="list-style-type: none"> - Governance Structure • Extending Shariah-Compliance Supply Chain <ul style="list-style-type: none"> - Integrity of Islamic Finance Industry • Qard Hasan/Benevolent Loan by RTO to Retakaful Fund

3. Industry Landscape (Takaful & Retakaful) – Sectoral Perspectives

Financial	Counterparties	Process	Learning/Growth
<ul style="list-style-type: none"> • Capital - relatively low • Retakaful Fund – still small and portfolio based , • Underwriting Capacity <ul style="list-style-type: none"> - Treaty (sufficient) - Facultative (low) • Contribution pricing – conventional formula • Qard Hasan Concept <ul style="list-style-type: none"> - Benevolent loan by operators 	<ul style="list-style-type: none"> • IFIs – General non-challenge on compliant chain • TOs – mixed placement priorities • Regulators <ul style="list-style-type: none"> - local focus • Rating Agency <ul style="list-style-type: none"> - using “reinsurance” perspective • Shariah Scholars <ul style="list-style-type: none"> - yet to be (re)takaful savvy (practical aspects) • Government <ul style="list-style-type: none"> - Islamphobia 	<ul style="list-style-type: none"> • Shariah-Compliance Governance structure <ul style="list-style-type: none"> - Organs/Mechanism • Account Separation <ul style="list-style-type: none"> - Shareholders & Retakaful Funds • Investment <ul style="list-style-type: none"> - Shariah-Compliant instruments • Products – Clearance by shariah advisory body • Outsourcing <ul style="list-style-type: none"> – affects intellectual development 	<ul style="list-style-type: none"> • Conventional mindset, • Product focus <ul style="list-style-type: none"> - elementary product range, • Shariah issues <ul style="list-style-type: none"> -Standardization / harmonization, • Operating Models - evolutionary • Islamic Finance knowledge • R & D – model/contract • Disconnect & gaps between practitioners and scholars, • Value Added Capabilities • Range of permissibility to forbidden (Business sources, Risk types)

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4. Operating Model

	Concept	Mode	Income Stream
1.	Wakalah	Agency	<ul style="list-style-type: none"> ✓ Wakalah Fee from contribution ✓ Wakalah fee from Investment activities on fund
2.	Mudharabah	Profit-Sharing	<ul style="list-style-type: none"> ✓ Profit sharing on Investment activities on fund ✓ Profit sharing on surplus (not widely practiced)
3.	Hybrid (Wakalah & Mudharabah)	Agency & Profit Sharing	<ul style="list-style-type: none"> ✓ Wakalah fee from contribution ✓ Profit sharing on investment profit
4.	Configuration of above + Jualah/Hafiz	Configuration above + Performance or Incentive fee	<ul style="list-style-type: none"> ✓ Configuration of above + Performance or Incentive Fee on underwriting surplus

Remarks : Models are still evolutionary

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5. Opportunities & Challenges

5.1 Growing awareness of Ethical Nature of Islamic Finance

- Insulated from “credit/interest” driven current financial crisis
- Entry of more shariah-compliant financing instruments
- Endorsement by the Vatican - “New Horizon”, Issue No. 171, April- June 2009

Quotation by L'Osservatore Romano. (Daily newspaper in the Vatican, regarded as the mouthpiece of the Pope)

“The ethical principles on which Islamic finance is based may bring banks closer to their clients and to the true spirit which should mark every financial service”

“Western banks could use tools such as the Islamic bonds, known as sukuk, as collateral, to finance the car industry or the next Olympic Games in London”

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5. Opportunities & Challenges

5.2 Increasing acceptance of Islamic Finance in the leading economies

- Finding appropriate (Re)Takaful products,
- Developing underwriting capacity,
- Applying right pricing formula,
- Human capital development,
- Living up to expectations.

5.3 Alternative to conventional insurance/reinsurance

- Is it ready to play alternative / solution
- Expectation – Equal if not better
- Value propositions

5.4 Interest at Lloyd's

- Adaptability to Lloyd's structure
- Sufficiency of business

5.5 Captives

- Captives in its various forms

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6. Going Forward – Food For Thought

6.1 Worldwide Takaful Contribution (High Growth Rate)

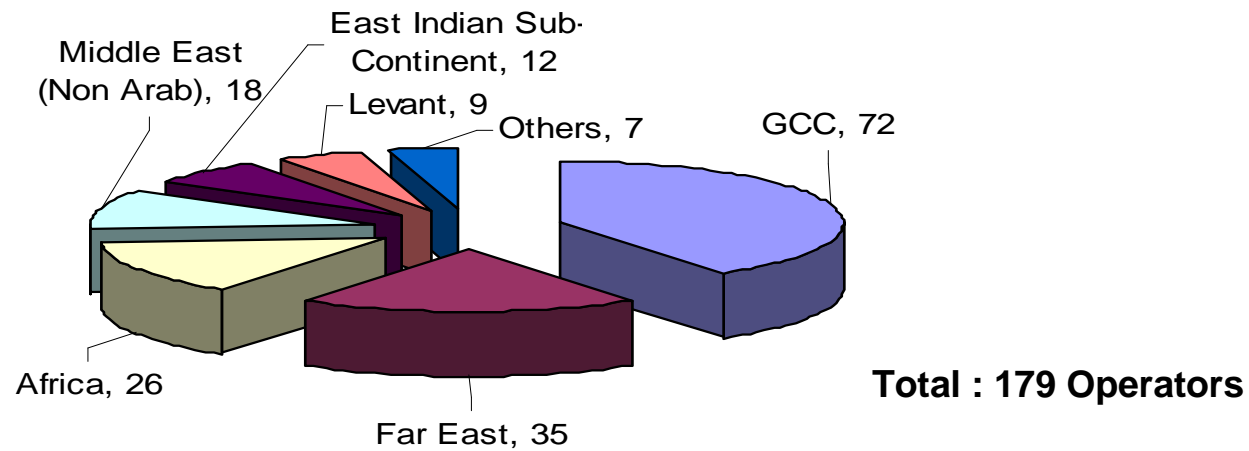
	2005	2006	2007 est	Growth (2005 - 2007)
East Indian Sub-Continent	8	11	13	62%
Middle East (Non Arab)	2,372	2,880	3,505	48%
Levant	15	18	22	47%
GCC	1,547	2,088	2,560	66%
Far East	537	695	872	62%
Africa	181	215	246	34%
Total	4660	5907	7219	55%

Source: World Islamic Insurance Directory 2009 (Figures rounded-up to nearest million)

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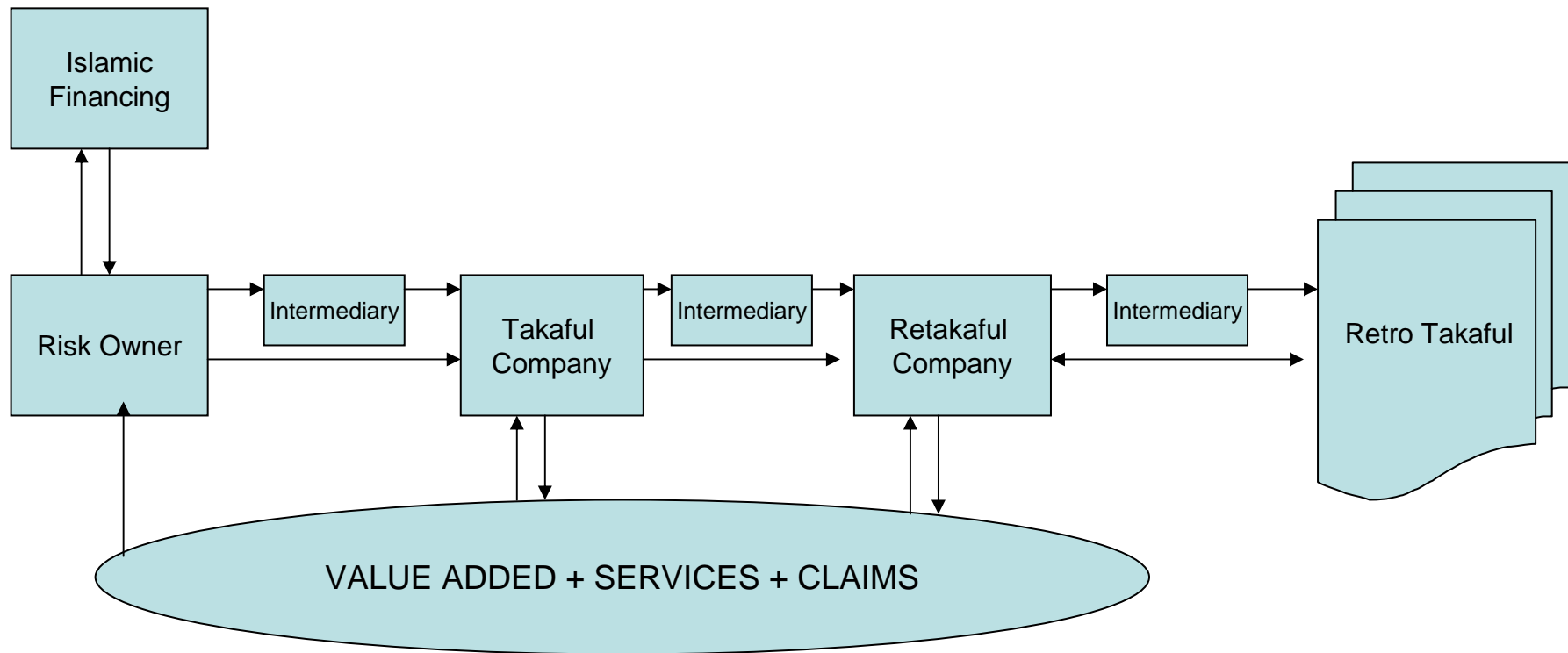
6.2 Islamic Insurance Operators Worldwide



Source: World Islamic Insurance Directory 2009

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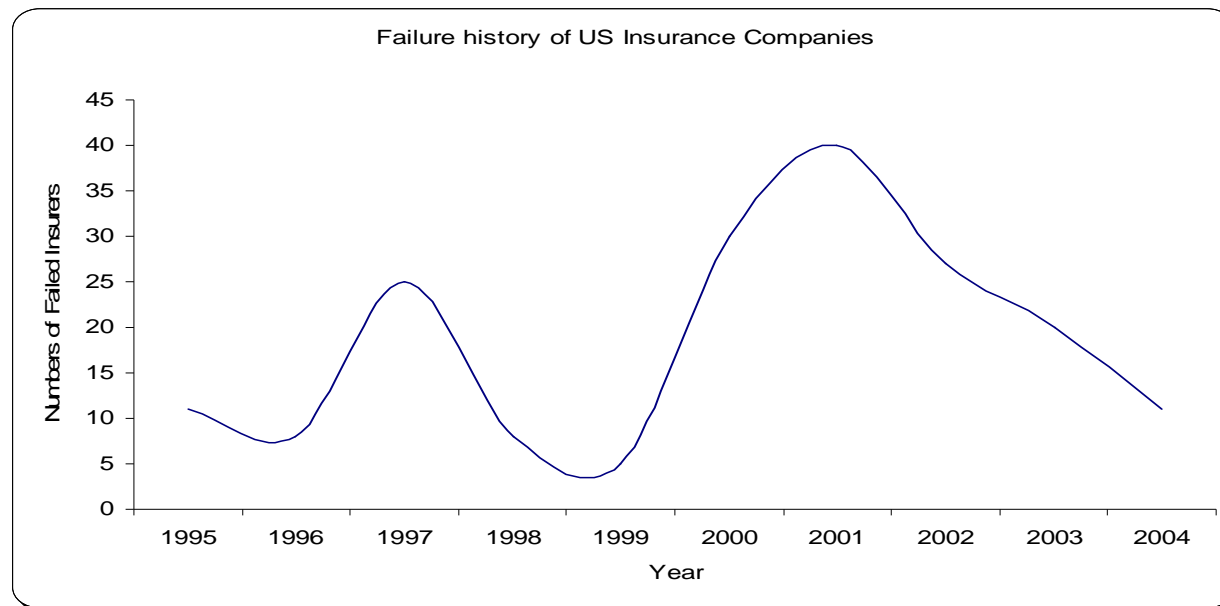
6.3 Shariah-Compliant Supply Chain



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6.4 Combined Ratios of USA Insurance Industry (1975 – 2003)

6.5 : Failures of Insurance Companies in USA (1995 – 2004)



An Insurance company is deemed to have failed if, at any time, meets any of the following criteria:

1. Falls under the supervision of the regulatory authority
2. In the process of rehabilitation
3. In the process of liquidation
4. Voluntarily dissolved after disciplinary or regulatory action taken by the regulatory authority

NB: 1995-2004; Over 190 US companies failed, 23% happened in 2001 alone (WTC 9/11)

Source : Muhaimin Iqbal

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6.6 Conventional Profitability Formula

Underwriting Profit = (Premium)- (Combined Operating Ratio)

Operating Profit = (Premium)-(COR)+ Investment Profits

Diagnosis:

- ✓ Premium rate in general shows declining tendency
- ✓ Claim Costs and Management Expenses, increasing tendency (inflation?)
- ✓ Acquisition costs, adjustable within reasonable band
- ✓ Investment Climate - Uncertain
- ✓ Tendency towards underwriting loss and reliance on Investment Income

Prognosis : Premium ↓ ; Acquisition ⇕ ; Claims ↑ ; Management Expenses ↑ ; Investment ⇕

: Profit is difficult to make

6.7 Takaful Underwriting Equation (Wakalah Model)

Pure Cost of Risk Ratio + Acquisition Cost Ratio + Wakalah Fee

Observations:

- ✓ Eligible participants within a homogeneous group is charged appropriate cost,
- ✓ TO not exposed to unhealthy underwriting loss (Loss due to poor cost management) ,

Challenges :

- ✓ Operationalizing the concept

6.8 Islamic Banking (encouraging development)

No.	Countries	Descriptions
1.	USA/Canada	-Banks offering Islamic forms of financing for property, trade & microfinance
2.	Japan/Korea / China	<ul style="list-style-type: none"> - 2007, Japanese government promoting Islamic finance as a method to develop the Asian bond market. - JBIC sells sukuk for the first time in May 2008 -The first sukuk, out of Korea expected in 2009 - China amends laws to the specifications of Islamic banking, especially with regards to Islamic Sukuk (bonds)
3.	Europe	- Tax laws amended to facilitate / encourage Islamic finance (Stamp duty, Property and profit taxes)
4.	India	- Establish Islamic Development Bank
5.	Singapore / Hong Kong	<ul style="list-style-type: none"> - Establish the Islamic Bank of Asia (first Islamic bank) - MAS amend laws to exempt Murabaha financing from the restriction in the Banking Act - Hong Kong establishes Islamic indexes on the Hong Kong stock exchange - Both aspire to be international Islamic capital markets hub
6.	Australia	- License issued for full Islamic banking operation



THANK YOU
&
PEACE TO ALL

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