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Global takaful: facing the challenge of digitalization

Sohail Jaffer writes about how the takaful sector is embracing the opportunities and challenges of digitalization

Following a period of breathless expansion in the early 2000s, growth in the global market for Shariah-compliant insurance (Takaful) has decelerated in recent years. According to numbers published by Moodys[1], Takaful gross contributions grew at a compound annual growth rate (CAGR) of 33% between 2005 and 2010, slowing to 18% between 2008 and 2013.

Nevertheless, in many markets Takaful continues to expand more rapidly than conventional insurance. For example, in Malaysia – the world's most developed market for Islamic financial services – family and general Takaful grew by 9.8% and 5.8% respectively in the first half of 2016. This compares with 8.2% in conventional life and 2.6% in general insurance in the same period[2].

Although Moody's expects growth to continue to decline in 2017, the agency believes the Takaful market will still post double-digit growth levels this year, driven primarily by *"a more educated, working-age population and increasing awareness of the concept of Takaful and its religious orthodoxy. Increasing customer affluence and a growing insurable asset base in key growth markets are further factors."*

The digital challenge

The compelling potential of the Takaful sector means that it shares many of the opportunities and challenges now confronting the broader global conventional insurance industry. These were summarised in the introduction to a report published by Ernst & Young (EY) in 2013[3].

"The global insurance market shows unprecedented growth potential, whether it is the sizable global population moving into retirement with greater life expectancy and health protection needs or the massive emerging markets of South America, Asia and Africa demanding the full suite of insurance products," this noted. *"But the toughest challenge faced by the insurance sector is the one that is transforming consumer behaviour and business models – digital technology."*

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In some respects, these opportunities and challenges are amplified by the structure of the Takaful industry, especially in the Middle East in general and the GCC in particular. The opportunities for Takaful operators are probably more extensive than they are for conventional insurers simply by virtue of the continued under-development of insurance services, twinned with rapid population growth, throughout the Muslim world. To date, however, even after rapid recent growth, penetration of specialist Shariah-compliant insurance remains modest.

Stretched resources

While the relatively low penetration levels of insurance services in Muslim-majority countries presents exciting long term opportunities for Takaful companies, the structure of the industry suggests that they may not be equipped to

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Takaful operators with the capacity to grasp the opportunities presented by digital innovation will be ideally positioned to capitalize on the rapid development of the digital economy in the Middle East capitalize on this potential. Especially in the Gulf, fragmentation and fierce price competition has eroded margins and starved companies of the financial resources they need to invest in digital technology and enhanced distribution.

The digital opportunity

For those that have the critical mass and the resources, the opportunities for digital-driven growth are considerable, not least because Takaful companies are generally less burdened by legacy technology and cultural constraints than conventional insurers.

More important, Takaful operators with the capacity to grasp the opportunities presented by digital innovation will be ideally positioned to capitalize on the rapid development of the digital economy in the Middle East. Those that lack the financial or human resources to do so, however, will risk being left behind. This is because by 2025, it is estimated that the Middle East will be home to as many as 160 million digital users.

As a result, according to a recent report published by the Global Manufacturing and Industrialisation Summit (GMIS) and conducted by PwC, the region's digital transformation could generate $16.9 billion in extra revenue each year for companies in the Middle East from 2017 to 2021, as well as a further $17.3 billion in annual cost savings and efficiency gains[4].

The acceleration of the digital transformation is an explicit component of government economic policy in a number of GCC countries. Saudi Arabia, for example, has pledged to *"partner with the private sector to develop the telecommunications and information technology infrastructure, especially high-speed broadband, expanding its coverage and capacity within and around cities and improving its quality."* Specifically, the government's target under its Saudi Vision 2030 programme is to exceed 90% housing coverage in densely populated cities and 66% in other urban zones[5].

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The UAE government is also committed to digital transformation as part of its blueprint for development over the coming decade. Symptomatic of its ambitions is Dubai's leadership in the implementation of Li-Fi (Light Fidelity), which is said to have achieved speeds of 224 gigabitts per second – making it 100 times faster than Wi-Fi[6].

According to a recent McKinsey analysis, however, while some governments in the Gulf have been especially proactive in promoting digital use, it is consumers in the region that are the driving force of the digital revolution. *"As measured by digital consumer adoption, Bahrain, Qatar, and the United Arab Emirates are among the top countries in the world, with more than 100% smartphone penetration and more than 70% social-media adoption—even higher than in the United States,"* notes the McKinsey report[7].

Rising consumer demand for digital adoption in the Gulf mirrors a broader global trend. A 2015 Bain survey of more than 158,000 consumers in 18 countries found that the share of digitally active insurance customers currently ranges from 35% to 70%. Over the next few years, 79% said they will use a digital channel for insurance interactions[8].

The use of digital technology innovation applied to insurance, InsurTech, is transforming the traditional business model of the global insurance market, and Takaful operators are well positioned to adopt new digital solutions to grow their penetration, by focusing on the 6.4 billion connected digital devices in use globally. With about 5.5 million devices being added daily, according to Gartner, by 2020 the total number of connected digital devices will likely exceed 21 billion[9].

The potential of InsurTech to deliver growth for the Takaful industry is clear, with global insurance industry participants investing over US$4.4 billion over the past 2 years in InsurTech initiatives.

Consultants warn, however, that insurers continue to lag behind the digital curve relative to other sectors. According to Bain, *"most established companies in the insurance industry have been slow to adopt digital tools and business*

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models, relative to other industries, such as retail, media, travel and retail banking." For example, according to Accenture, during 2015 the total value of global FinTech investment reached US$22.3 billion.

Specifically, Bain reports that although most insurance executives realize they have to step up their digital investments, many remain unclear about exactly where to start and how to proceed in organizing for digital innovation and redesigning their processes.

This suggests that the digital challenges identified by Ernst & Young are as relevant to the insurance industry today as they were when its survey was originally undertaken in 2013. This warned that legacy technology, the slow pace of product delivery and culture constraints were all hindering progress across the industry. It emphasised the importance of retention through improved customer experience and of recognizing that distributors are also digital customers. It also identified that analytics were critical to success in the digital world, and that it was essential for insurers to embrace the mobile and social media wave.

As in so many areas of the global Islamic financial services industry, Malaysia has been the most vocal and proactive in calling for its insurers to respond to the challenges and opportunities generated by digitalization. Warning that growth in the insurance sector had plateaued in the last three years, Bank Negara Malaysia (BNM) Governor Datuk Muhammad Ibrahim pressed industry players to *"wake up from their slumber"* in terms of technological development or risk a decline in growth[10].

The industry is responding constructively to these pleas. Ahmad Rizlan Azman, Chairman of the Malaysian Takaful Association, has said that the country's insurers are planning to double the number of policyholders over the next few years by increasing its investment in digital technologies to attract a younger customer base[11].

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More broadly, he added that Malaysia's Shariah-compliant insurance sector is aiming to lift its market share from 14% at the end of 2014 to 25% by 2020. In order to reach this ambitious target, Takaful operators will need to keep pace with consumer demand for digital services as smartphone penetration and the use of social media gathers momentum.

Conclusion

For Takaful specialists in Malaysia and elsewhere, the opportunities for growth remain compelling. If the industry is to grasp this opportunity, it will need to ensure it builds the critical mass, human talent and financial resources to invest in the technology necessary to keep ahead of the digital curve. ■

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Endnotes

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