Indonesia's reinsurance industry

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The outlook of Indonesia's reinsurance industry is stable in the near to medium term. After high premium growth at above 20% in 2017 and 2016, we project the industry will grow by 11%-12% in the next 12-18 months as we anticipate that the windfall effect of the mandatory domestic cession – as stipulated under POJK No.14/POJK.05/2015 – will start to stabilize. In our projection, we incorporate growth in the insurance industry given the large untapped potential, Indonesia's large population, high consumption and growing middle class, as well as improving market awareness. We expect this growth to have a knock-on effect on the reinsurance industry, which remains key in mitigating insurance risk.

With the establishment of PT Reasuransi Indonesia Utama – built from the merger of PT Reasuransi Internasional Indonesia and PT Asei Reasuransi Indonesia (Persero) – the Indonesia's reinsurance industry had a stronger equity base with total equity of IDR7.2 trillion as of December 31, 2017 (FY2017), up from IDR5.4 trillion in FY2016. Thus, we project the industry to have the capacity to realize its business potential, which may in turn reduce the outflow of reinsurance premiums as well as minimize the current account deficit. In our view, given the increased risks in the domestic reinsurance industry, reinsurers will also have to exercise more prudent underwriting controls and ensure strong risk and capital management capabilities are in place.

Growth in conventional and sharia reinsurance

The conventional reinsurance industry booked total gross written premiums (GWP) of IDR16.0 trillion in FY2017 and IDR13.2 trillion in FY2016, representing annual growth rates of 21% and 44.6%, respectively. Growth in 1Q2018 remained promising at 24.6%, compared to 24.3% in 1Q2017. This strong growth was due to the enactment of POJK No.14/POJK.05/2015, which became effective in January 2016.

The premiums mainly came from property and motor vehicle insurances. We project soft growth from the motor vehicle insurance segment, as we estimate automotive sales to be modest. As in the health insurance segment, in addition to life insurers, general insurers also face competition from the national insurance scheme (BPJS Kesehatan). The growth in infrastructure projects, in line with the government's economic plans, should also generate demand for related insurance services, such as engineering and surety bond.

In line with the performance of conventional reinsurance, the sharia reinsurance industry also recorded a fast pace of growth with total gross contributions (or GWP in conventional terms) of IDR780 billion in FY2017 – a 92% increase from IDR405 billion in FY2016. The positive growth continued in 1Q2018 at 59.4%, even higher than the 32% increase in 1Q2017. In contrast to conventional reinsurers which generate most of their business from the general insurance segment, sharia reinsurers rely on life insurance as the key business driver. The life segment supplied 82.5% and 81% of sharia insurance's gross contributions in 1Q2018 and FY2017, respectively. We estimate that unit-linked products will continue to dominate the life sector in the medium term as we anticipate further integration between banking and insurance services. This is also in line with our projection that banks are emphasizing cross-selling and focusing on their fee-based income to improve their revenue diversification.

Table 1. Gross written premiums (IDR billion)

	1Q2018	FY2017	1Q2017	FY2016	1Q2016	FY2015
Conventional reinsurance	4,818	16,029	3,868	13,248	3,113	9,160
Sharia reinsurance	204	780	128	405	97	286
Conventional growth year-on-year	24.6%	21.0%	24.3%	44.6%	NA	NA
Sharia growth year-on-year	59.4%	92.6%	32.0%	41.6%	NA	NA

Source: Reinsurance companies' financial highlights, www.ojk.go.id

There are only nine players in the reinsurance industry: six engaged in conventional reinsurance and three in accordance with sharia principles (two of which still operate as sharia business units). The level of competition among them is moderate, as reinsurers have the flexibility to maintain certain underwriting criteria. However, they remain exposed to the intense competition in the general and life insurance industry, which may affect underwriting results. They are encouraged to maintain underwriting discipline and control as we expect business risks will continue to emerge.

Table 2. List of reinsurance companies operating in Indonesia

Company name	Total assets (IDR Bn)	Total equity (IDR Bn)	Total GWP (IDR Bn)	PEFINDO's rating
PT Reasuransi Indonesia Utama (Persero)	8,087.7	2,883.4	5,776.6	$_{id}$AA/Stable
PT Reasuransi Nasional Indonesia	4,617.9	1,618.0	5,613.4	-
PT Tugu Reasuransi Indonesia	3,400.2	1,077.8	3,007.6	-
PT Maskapai Reasuransi Indonesia Tbk	2,880.0	1,356.9	1,805.1	$_{id}$AA-/Stable
PT Reasuransi Maipark Indonesia	589.3	430.5	300.6	-
PT Reasuransi Nusantara Makmur	-	-	-	-
PT Reasuransi Syariah Indonesia	793.4	259.1	437.2	$_{id}$A+/Stable
PT Maskapai Reasuransi Indonesia Tbk (sharia business unit)	225.9	146.8	73.1	-
PT Reasuransi Nasional Indonesia (sharia business unit)	579.3	322.9	273.5	-

Note: figures as of December 31, 2017

Main challenges to increase insurance penetration

Insurance penetration is considered low for both the conventional and sharia types. The penetration rate for conventional insurance was at 2.5%-3% in 1Q2018, and even lower at only 0.1% for sharia insurance in the same period, despite the large Muslim population in Indonesia. This indicates that the industry has strong potential to grow further. Indonesia's financial services regulator is pushing for more affordable insurance products, or micro-insurance, to increase the penetration rate. Industry players are also challenged to seize the opportunities through increased efforts to educate the market education and tap the market potential.

Given sharia insurance's very low penetration rate, we are of the view this industry faces significant challenges to be able to reach a comparable scale with conventional insurers. In addition, the limited number of sharia insurance companies may put additional burden on this industry. We are of the view it may expose the companies to concentration risk, where a deterioration in a few counterparties may substantially affect business generation and operating performance.

Key growth factors

We are of the view that distribution channel is one of key factors in determining growth in the industry. This includes digital channels, as technology is expected to continue to be the main driver of business. Industry players are seeking more effective and efficient ways to acquire customers. However, this highlights the need for additional protection against cyberattacks on both their systems and their business partners' systems.

With competition rising, we see that sustaining innovation is important for stability and sustainable growth. Innovation will support the industry players in keeping up with market dynamics, as it will likely meet customer needs. Innovation will also bring added value to the industry players, as it brings competitiveness or unique selling propositions over its competitors.

Over the last two years, the issuance of new regulations related to Indonesia's insurance market has increased significantly – the single presence policy, commission limits, domestic reinsurance requirements, as well as tariffs and capital requirements. We expect that this pace of change will not slow down in the near to medium term. The industry regulator, through the domestic mandatory cession, aims to push the growth of the reinsurance industry by optimizing its capacity. Under POJK 67/POJK.05/2016, the regulator also increased the minimum paid-up requirement for insurance and reinsurance companies, both conventional and sharia ones. With the more stringent regulatory requirements, we expect the industry to be able to further realize their business potential as well as absorb more risks.

Under the same regulation, the regulator is also encouraging growth in sharia insurance and reinsurance in the long run. Sharia business units must be spun-off into a separate legal entity if the value of the tabarru funds and participants' investment funds has reached at least 50% of the total insurance funds, tabarru funds and participants' investment funds. The process of spinning off sharia business units must start within 10 years after the enactment of the 2014 Insurance Law (or by October 17, 2024). Operating as a separate legal entity will bring advantages, in our view. We expect it to increase market attractiveness given the increased trust toward the sharia business, as the risks and operations will be fully separated from conventional principles.