Life Insurance: Stable Outlook Amid Challenges From Capital Market Volatility

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PEFINDO is of the view that the risk profile of the life insurance industry is moderate, with a stable outlook. Amid the continuing macroeconomic slowdown, we project the industry to slightly grow by around 2%-7% in the next 12-18 months. The industry growth is supported by low insurance penetration at only around 2% due to large untapped potential, Indonesia's large population, high consumption and growing middle class, as well as improving market awareness. Low penetration indicates the potential of untapped business, although at the same time also reflects lack of insurance literacy in communities. The industry growth is also constrained by intense competition level dominated by its largest players, as well as closer supervision by the regulator. Moreover, life insurance companies are constantly exposed to capital market volatility particularly the ones with high portion of guaranteed products. Given their business nature that unable the players to enjoy adequate underwriting result, life insurers are more aggressive in their investment activities to pursue higher yield. Unfavorable macroeconomic condition may affect investment performance and this could lead to liquidity pressure if it need to be monetized to repay the liabilities to the policyholders.

Market overview: major players, products and distribution channels

The life insurance industry is relatively concentrated among 10 large insurers, which dominance in the market is unlikely to change in the medium term. The top 10 insurers controlled more than 60% of total assets and premiums as of September 30, 2018 (9M2018).

Table 1. Life Insurance's Top 10

No	Company	Gross Written Premium (in IDR trillion)	Total Assets (in IDR trillion)
1	Prudential Life Assurance	17.9	68.5
2	Asuransi Simas Jiwa	13.3	33.6
3	Asuransi Allianz Life Indonesia	9.2	13.8
4	AIA Financial Indonesia	9.1	44.6
5	Asuransi Jiwa Adisarana Wanaartha	8.7	10.4
6	Indolife Pensiontama	8.1	28.7
7	Asuransi Jiwa Manulife Indonesia	7.0	44.4
8	AXA Mandiri Financial Service	6.2	26.5
9	Capital Life Indonesia	6.1	8.9
10	BNI Life	4.4	16.0
	Top Ten	90.0	295.4
	Total Life Insurance Industry	141.1	516.3
	Market share of Top 10 vs. Industry	63.8%	57.2%

Source: OJK statistic and company website, processed by PEFINDO, figures as of September 30, 2018

In terms of product, investment linked products dominated the market, at around 60% of the industry's total GWP. The products offer investment savings with valued protection benefits, where protection products such as life, personal accident, and health are sold as riders.

Product demand is also affected by stock market performance, which often yields in favorable investment returns during a bullish stock market, but may trigger redemption during negative investment returns amid a bearish stock market. At such time, insurers can anticipate the conditions by expanding traditional protection products, which are not as cyclical as investment linked products.

We are of the view that investment linked products with riders will still have a significant presence in the market. Indonesian customers will continue to prefer savings products which include protection, compared to solely protection focused products, although there remains risk that a stock market downturn may adversely impact the product investment returns. Aside from investment-linked products, we are of the view that endowment products will continue to benefit from continued demand for savings products. Protection products (term and whole life) will mainly be sold as riders to linked products, as customers will continue to prefer savings orientated products.

In terms of distribution channel, life insurance products are sold predominantly through the bancassurance channel and agency forces, at around 45% and 37% of the industry's total premium income, respectively. We are of the view that bancassurance will continue to make a significant contribution, with insurers' efforts to increase productivity, particularly due to their sizable spending in the partnerships, while with the insurers' banking partners leveraging their client base, this should provide easiness for insurers to generate premiums from the potential market.

We expect agents will continue to play a significant role in the foreseeable future, where face-to-face interaction may still be most consumers' preferred way to take up life insurance. As such, we project agencies will not necessarily shrink, while the digital channel will expand, but with its share likely to remain insignificant in the near to medium term. Digital channel represents a good opportunity for insurers and complements the traditional agency channel. Digital channel is still very small and has been used to promote simple products. It is something the industry needs to embrace as complement, enabling advisers to focus on their customers and upgrade their skills so they become more efficient and productive. Insurers have enabled their agents with digital tools and support them with digital leads, which should assist insurers to reach a wider geographic spread of Indonesian areas more efficiently, compared to expansion by opening branches.

Exposure from capital market volatility to financial profile

PEFINDO notes that life insurance companies are continuously exposed to capital market volatility, and this may affect their overall financial indicators. Given the long tenor and competitive nature of the industry, the overall loss ratio and combined ratio would tend to range above 100% and 120%, respectively, and therefore life insurers are depending on investment results to fund their operations. As mortality and morbidity statistics are well maintained, the loss ratio is more predictable than that of a general insurance business. Higher loss ratio may also be contributed from increasing claims and benefits from surrenders on unit-link policies amid lower investment return resulted from capital market volatility.

High-risk & high returns instruments such as stocks and mutual funds will continue dominate life insurers investment portfolio. As of 9M2018, most of the industry's investments were placed in mutual funds and stocks, at about 35.4% and 30.0%, respectively, followed by government bonds (13.6%), time deposits (8.3%), corporate bonds-including medium term notes (7.3%), and the rest placed in property and other investments. The new OJK regulation requiring a minimum placement in government bonds and securities (state-owned infrastructure bonds and mutual funds with government securities as the underlying) of 30% has affected investment composition, with placement in government bonds gradually increasing to IDR61.5 trillion as of 9M2018, up from IDR45.1 trillion as of FY2015. In our view, this regulation should somewhat improve the overall investment quality of life insurance companies, if the players maintain the portion of low risk instruments such as time deposits. Unfortunately, in some cases life insurers tend to reduce time deposits to compensate this minimum 30% required investment. Although credit risk is low, government bonds and state-owned corporate infrastructure bonds are still prone to market risk considering the bond price fluctuation.

Of the major players (see Table 1), none suffered a net loss in 2015–2017. Among the 54 life insurers, 16 suffered net losses in 2017, and 11 are smaller companies, with net premium production well below IDR100 billion. Therefore, the impact on overall insurance industry performance is limited. The Indonesian life insurance industry has been able to maintain a consistent performance even against the full impact of the 2008 global financial crisis, which led PEFINDO to believe that the industry has the capability to maintain its stable operating performance in the face of another global crisis.

Amid a difficult investing environment with rising interest rates, both equity and fixed-income securities are often negatively impacted. This is partly mitigated by the long tenors of some of the investments, giving some insurers more room to wait for economic recovery and regain investment losses. Exposure risk was evident in 9M2018, where some insurers suffered a comprehensive mark-to-market loss. PEFINDO is of the view that insurers will remain exposed to capital market volatility in the medium term, which may ultimately impact their bottom lines if they are forced to liquidate some of their investments in an investment downturn. Moreover, life insurance companies may also face the risk of an investment return gap to their policyholders, particularly the ones offering overly aggressive guaranteed returns. We are of the view that investment strategy and liquidity management policy are crucial to ensure insurers will have adequate liquidity to fulfill financial obligations when they become due.

Exposure to capital market is recently evident in PT Asuransi Jiwasraya (Persero) (Jiwasraya), which in October 2018 has postponed the repayment of IDR802 billion maturing saving plan product distributed by several banks. This was mainly due to plunge in share prices that has affected Jiwasraya investment valuation. As a state-owned company, Jiwasraya was unable to monetize the investment at loss as it may be considered a law violation. On the other side, the premium generation could not compensate its underperformed investment activities. Jiwasraya's total premium income was IDR21.9 trillion in 2017, but it has not even reached IDR8 trillion until 9M2018. Although Jiwasraya has offered to roll-over the principal and paid its interest obligations, the case has not been fully settled as some policyholders still demand for full principal repayment.

Before Jiwasraya, there were several cases where life insurance companies failed to repay its obligations to the policyholders due to meltdown in its investment portfolio, namely Asuransi Jiwa Bakrie, Asuransi Jiwa Bumi Asih Jaya, and Asuransi Jiwa Nusantara. We are of the view that it is very important for life insurers to closely monitor their investment holdings' performances and take precautionary steps in managing their portfolios, particularly amid a difficult investing environment. Capital market volatility, if it continues, could also dampen the profitability and liquidity of life insurers if the potential risks arise from it are not managed well, in our opinion.

Average capitalization

Capitalization of the life insurance industry is considered as average, mainly attributable to the modest size of insurers' overall equity, which leaves insurers with a low equity base more vulnerable to single event losses, and limited capacity to capture high-sum risks. As of 9M2018, the total equity of the industry was IDR80.4 trillion, -11.1% growth compared to IDR90.4 trillion as of FY2017. Although the industry recorded a high risk-based capital ratio of 430% as of 9M2018, far above the regulatory requirement of 120%, this was mainly concentrated to leading players with superior capital bases, mostly joint-venture life insurance companies. Moreover, some of the insurers, particularly the smaller ones with equity bases slightly higher than the minimum capital requirement struggled to survive, while those with large capital dominate market share. An option for smaller insurers with such difficulties is a sale, otherwise they may need to surrender their licenses.

Stable outlook for PEFINDO's rated portfolio

As of November 30, 2018, PEFINDO published the financial strength ratings of two life insurance companies: PT Asuransi Jiwa Taspen ($_{id}$A+/stable) and PT Heksa Solution Insurance ($_{id}$BBB+/stable). The number of rated life insurance companies is smaller than general insurers (10 published ratings), due to different business models as there are fewer life insurers who directly conduct partnerships with banks - who require a rating to reduce the risk weighted assets for their insured loans, compared to the general insurers.

The rating of Asuransi Jiwa Taspen reflects very strong support from and business synergy with its parent, TASPEN (Persero), its moderate capitalization and reserves, and the moderate asset quality of its receivables. However, the rating is constrained by its modest operating performance and exposure to capital market volatility. The Company provides life insurance products to groups and individuals, focusing on state-owned enterprises and civil servants.

The rating of PT Heksa Solution Insurance reflects its market from its strategic partner, adequate liquidity, and average asset quality. However, the rating is constrained by its modest capitalization and moderate operating performance. The Company is focused on credit life insurance for individual bank debtors. It also offers other products, such as a one-year life insurance coverage, personal accident insurance, and unit-linked products.