UNIVERSITI PUTRA MALAYSIA

LIFE INSURANCE DEMAND IN MALAYSIA

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LIFE INSURANCE DEMAND IN MALAYSIA

By

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Specially dedicated to

My beloved parents, brother and sisters,

for their invaluable love, sacrifices and support

to make this thesis possible in every way.

Abstract of thesis submitted to the Senate of Universiti Putra Malaysia in partial fulfilment of the requirements for the degree of Masters of Science.

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FEBRUARY 2002

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Malaysia has been identified as having the second highest saving in the world; however, less than 30 percent of Malaysia's total population of about 6.4 million is insured in 1999. The fact that a large section of the society remains uninsured means that any sudden loss of property or any personal misfortune will suffered a reduction in living standard and poverty. Besides that, savings generated by life insurance companies are crucial in providing long-term savings for sustainable economic development and growth of the nation. Nevertheless, the life insurance industry in Malaysia has not been thoroughly investigated. Therefore, the objectives of this study are to identify the factors contributing individual purchasing behaviour of life insurance in Malaysia, and to investigate the macroeconomic factors influence on the aggregate demand of life insurance in Malaysia. Since the demand analysis is an important component of an attempt to understand the forces driving industry growth – its past and future prospects.

The empirical findings of individual purchasing behaviour of life insurance indicated significant demographic variables including the presence of children in the household, the

age of the consumer, and their income level. While, the empirical finding of the multivariate Granger-causality test suggests that national income can be a stimulus to the life insurance demand in the short-run. The results of Granger-causality test also indicate that there is bi-directional causality between the price of life insurance and life insurance demand in Malaysia. Furthermore, the empirical results also showed that the interest rate significantly influence the life insurance demand in Malaysia. However, the causality tests of this study did not detect a significant short-run direct causal relationship between inflation rates and life insurance demand in Malaysia. Last but not least, the finding of the Data Envelopment Analysis (DEA) approach indicated the demand for life insurance in Malaysia is closely linked to the efficiency scores of insurance companies. Over the empirical years, most of the local constituted insurance companies operate in inefficiency state compared to the foreign insurance companies.

Abstrak tesis yang dikemukakan kepada Senat Universiti Putra Malaysia
sebagai memenuhi keperluan untuk ijazah Master Sains.

PERMINTAAN INSURAN HAYAT DI MALAYSIA

Oleh

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FEBRUARY 2002

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Malaysia dikenali sebagai tabungan kedua tertinggi di dunia. Akan tetapi, kurang daripada 30 peratus penduduk Malaysia, iaitu 6.4 juta penduduk Malaysia yang dilindungi insuran pada tahun 1999. Hakikatnya, kebanyakan masyarakat yang tidak dilindungi dengan insuran akan mengalami penurunan taraf hidup dan kemiskinan apabila berlaku kehilangan harta benda atau malapetaka. Di samping itu, tabungan yang diterbitkan oleh syarikat insuran adalah sangat penting dalam memperuntukkan tabungan jangka panjang untuk pengekalan perkembangan dan pertumbuhan sesebuah negara. Namun begitu, industri insuran hayat di Malaysia masih belum dikaji dengan begitu mendalam. Oleh itu, objektif kajian ini ialah untuk mengesahkan faktor-faktor yang menyumbangkan individu gelagat pembelian insuran hayat di Malaysia, dan untuk menyelidik faktor-faktor makroekonomi yang mempengaruhi permintaan agregat insuran hayat di Malaysia. Ini kerana analisis permintaan merupakan komponen penting dalam memahami kuasa yang memandu ke arah pertumbuhan industri – masa lampau dan pandangan masa depan.

Empirikal kajian individu gelagat pembelian insuran hayat ini menunjukkan bahawa pembolehubah yang bererti termasuk kehadiran anak dalam keluarga, umur pengguna, dan tingkat pendapatan mereka. Dalam pada itu, empirikal kajian bagi ujian multivariate Granger-causality mencadangkan bahawa pendapatan negara merupakan pendorong kepada permintaan insuran hayat dalam jangka pendek. Hasil kajian ujian Granger-causality juga menunjukkan bahawa terdapat hubungan dua hala di antara harga insuran hayat dengan permintaan insuran hayat. Tambahan pula, hasil empirikal juga menunjukkan kadar faedah mempunyai pengaruh yang bererti terhadap permintaan insuran hayat di Malaysia. Namun demikian, ujian causality kajian ini tidak dapat mengesan sebarang hubungan sehala yang bererti di antara kadar inflasi dengan permintaan insuran hayat di Malaysia pada jangka pendek. Akhir sekali, hasil daripada pendekatan Data Envelopment Analysis (DEA) menunjukkan permintaan insuran hayat di Malaysia mempunyai hubungan rapat dengan mata kecekapan syarikat insuran. Antara tahun kajian, kebanyakan syarikat insuran tempatan beroperasi secara tidak cekap berbanding dengan syarikat insuran asing

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CHAPTER I

INTRODUCTION

There is a dearth of empirical study published in the literature regarding the Malaysian life insurance marketplace. While the topic of the demand for life insurance has been studied extensively, the data utilised has not included the Asian markets. As there are few notable exceptions where international cross-sectional studies have incorporated Asian data, the unusual life insurance profile that Malaysia represents brings into question whether the results of such broad-based analyses can adequately describe the Malaysia market.

The need for understanding the dynamics of this marketplace never has been greater. Few markets, particularly financial markets, remain isolated in the face of an increasingly internationalised world economy. The bulk of what might be considered the traditional "industrialised economies" are found in the West, but this is gradually changing. Indeed, the economic growth of other regions of the world, notably Asia, in general has been higher than that of the West over the past two decades, with the possible exception of the past few years when an economic slump has slowed regional growth. Financial markets that were once isolated, either by choice or purely due to lack of outside interest are now finding themselves increasingly internationalised with the presence of foreign competitors and products. Because of this increased internationalisation, there is an increasing demand for a corresponding study, to which this study is seeks to contribute.

The Malaysian Life Insurance Market in an International Context

Given that the majority of the industrialised nations of the world come from the West, it may not appear unusual that the Western markets have received the mainstream of the attention in academic insurance literature. In actual fact, nearly 70 percent of the world's insurance premiums (both life and non-life combined) originate in North America and Europe as shown in Figure 1.1.

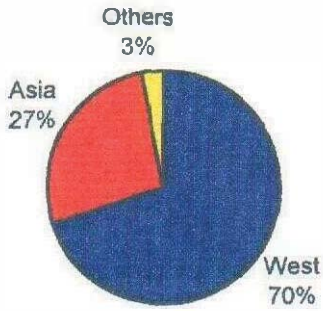

Figure 1.1: Market Share of World's Total Insurance Premium, 1998

Source: Swiss Reinsurance, Sigma, No. 7/1999

Asia generates approximately 27 percent of the world's insurance premiums and the remaining regions account for about three percent. As the market share dominance of the West in Figure 1.1 appears apparent when this information is separated into life and non-life figures, the characterisation of Western dominance dispel. After separated, one finds that the leadership position occupied by the West is fuelled by dominance in non-life insurance premiums. The West holds approximately 83 percent of this non-life market in 1998 while Asia holds another 15 percent. This finding is not necessarily unexpected since income and the level of industrial development of a country have been found to be significantly related to the demand for non-life insurance products. Moreover, the West, in these respects, is generally more developed than other regions of the world.

However, when the market share for life insurance figures are reviewed, they show the West dominates about a 60 percent market share compared to Asia's 35 percent (Sigma 7/1999). The greater parity in life insurance premium market share is obvious. Malaysia's market share represents approximately two percent of the Asian market share. In a larger context, Figure 1.2 describes Malaysia's market share on an Asian basis. It has been slipping over the past few years (in 1995 Malaysia held 2.6 percent of the Asian's market share). Together, Malaysia and Singapore comprise 28 percent of the Asian's life insurance market. The Malaysia life insurance market took in over $1,347 million USD in premiums in fiscal 1998 and had a total number of business-in-force of 6,972,647 policies at that time.

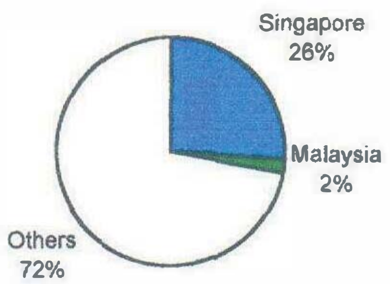

Figure 1.2: Market Share of Asian's Life Insurance Premium, 1998

Source: Swiss Reinsurance, Sigma, No. 7/1999

The following section will provide a more general description of the Malaysia life insurance marketplace. Background information will be provided on items such as the recent economic or market environment, competitors' market shares, types of products, and so on. It should be mentioned at this point that the expression "life insurance" has been employed loosely in this thesis. In fact, there is wide variety of products sold under the auspices of life insurance in the Malaysia marketplace. For the purposes of this thesis, the exprcssion "life insurance" refers to three major product lines of life insurance sold in Malaysia marketplace namely whole life, endowment, and temporary.

The Malaysian Life Insurance Market

In a variety of dimensions outlined below, Malaysian life insurance market appears dissimilar from the Western marketplace. For this reason, extrapolation of empirical results based on Western data to the Malaysian market appears tenuous. For the purpose of placing this study in context, a detailed description of the Malaysian life insurance market and the economic environment in which it exists is presented.

This section begins with a description of the international life insurance marketplace with emphasis on Malaysia's position. The discussion then turns inward, exploring Malaysian life insurance marketplace, and its relationship to the types of products. The empirical portion of this study examines data taken from 1963 to 1999 on a yearly basis. Both the suppliers and buyers of life insurance in Malaysia contribute descriptive profiles.

The International Life Insurance Market

Malaysia is by far the second highest saving in the world when measured by the ratio of Gross Domestic Saving (GDS) to the Gross Domestic Product (GDP). Since Singapore and Malaysia have the two highest saving ratio, a brief table comparing pertinent figures may serve to emphasize some significant aspects of each country's market.

Table 1.1: A Comparison of the Malaysia and Singapore Markets

	Malaysia	Singapore
Population (in thousands)	22,200	3,000
GDP (in millions)	$71,302 (39)	$85,425 (37)
GDP Per Capita	$3,241 (82)	$28,475 (9)
Gross Savings Ratio (Percent of GDP)	47 (2)	51 (1)
Life Insurance Premiums (in millions)	$1,347 (33)	$2,981 (28)
Life Premium Per Capita	$63 (42)	$7,702 (21)
BIF/National Income	118.9 percent (35)	127.0 percent (33)
Licensed Life Insurers	18	14

Source: OECD, 2001
Notes: World rank given in parentheses

A few points bear comment with regard to Table 1.1. First, the life premium per capita in Singapore is over 120 times the amount of that of the Malaysia. As a point of reference, Japan, which is ranked second in the world, as measured by premium per capita ($2,856.6), has a saving ratio of 32 percent. Second, the comparably huge Singapore market had three millions population in this marketplace in 1998 compared to over 22 millions in Malaysia.

The Domestic Insurance Market

Malaysian domestic insurance marketplace is commonly divided into two sectors namely life and general insurance. Life insurance undertakes to provide protection to the insured's family, creditors, or others against the loss of earning capability of the insured in the event of his death or serious injury. General insurance, which can categorise into various types, undertakes to indemnify the insured against losses arising out of damage to, or destruction of, the property insured. It also undertakes to pay damages to third parties for acts for which an insured is legally liable. The types of general insurance in Malaysia comprised of marine, aviation and transit insurance (MAT), fire insurance, motor insurance and numerous miscellaneous insurance including health insurance and accident insurance.

As with all other industries, the performance of the insurance industry in Malaysia was affected by the economic slowdown in 1998. The combined premium income of both the life and general sectors declined by 2.1 percent (1997: 14.6 percent) to RM10,902.9 million due to the negative growth in the general sector. Hence, the ratio of premium income to nominal gross national product (GNP) decreased marginally from 4.2 percent in 1997 to 4.1 percent in 1998. Life insurance premium continued to form the bulk, which is 57 percent of the premium income for the insurance industry.

The economic recovery, however, which was evident in 1999, had boosted the performance of the insurance industry. Data for 1999 showed that the combined premium income of both life and general business grew by 7.1 percent to RM11,681.8 million, accounting for 4.2 percent of nominal GNP of 1999. Total benefits and claims paid out increased by 6 percent to RM4,778.5 million, while total combined assets of insurance fund continued to grow at a double-digit rate of 15.6 percent to reach RM45,454.5 million as at the end of 1999.

Product Market Share

Figure 1.3 presents the life insurance product-market-share for Malaysian markets. Of particular note is the dominating position of the whole life and temporary product line in the Malaysian marketplace. The temporary policy in Malaysia is boosted by an encouraging recovery in credit-related policies sold via financial institutions. New premiums for credit-related policies increased significantly by 20.9 percent of RM194.8 million, partly attributable to the success of the Government's initiative to promote property sales through the Home Ownership Champaign. In terms of composition of life insurance in Malaysia, whole life policies is the most dominant class with a share of 28.4 percent of new premiums, followed by temporary and endowment policies with a share of 26 percent and 25.1 percent respectively.

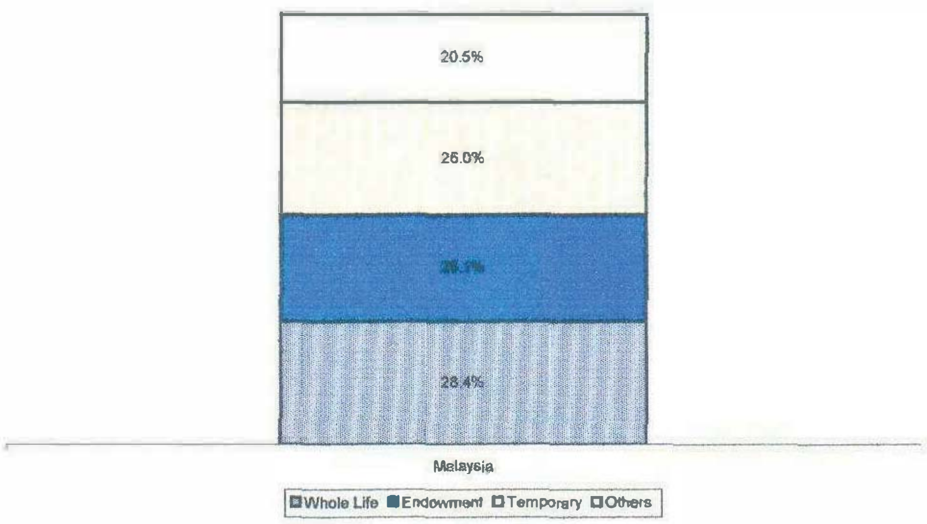

Figure 1.3: Malaysia's Life Insurance Portfolio

Sources: Ministry of Finance Malaysia, 1999
Note: Life Insurance figures for Malaysia are from 1998

These life insurance markets in Malaysia are dominated by the four foreign-incorporated insurers that increase their market share in terms of new business premiums and new sums insured from 41.6 percent and 31.8 percent in 1997 to 42.1 percent and 33 percent in 1998. These insurers dominance the whole life business, even though their total market share decreased to 70.3 percent and 75.4 percent (1997: 72.2 percent and 78.4 percent) in terms of new business premiums and new sums insured respectively. On the other hand, Malaysian-incorporated insurers commanded a larger market share of endowment and temporary policies, underwriting 62.5 percent and 79.1 percent of the new premiums respectively for these classes of business.

The Suppliers of Life Insurance Products

Competition in the Malaysian life insurance market can be said to come primarily from two sectors: licensed domestic competitors and foreign competitors. Foreign-incorporated insurers maintain the major share of life insurance business by controlling 46.7 percent and 57.5 percent of sums insured and annual premiums in force respectively. These foreign insurers successfully continued dominating the position in whole life policies with a market share of 77.5 percent and 73.1 percent of the sum insured and annual premiums respectively. On the other hand, Malaysian-incorporated insurers controlled a larger share of endowment and temporary policies, underwriting 58 percent and 81.5 percent respectively of the sums insured in force for these classes of business. Malaysian-incorporated insurers also commanded 63 percent and 48.2 percent of the education plans and medical riders respectively.

The five largest insurers, in which four of these were foreign-controlled in the industry, underwrote 64.7 percent and 73.1 percent of sums insured and annual premiums respectively. On the other hand, the five smallest insurers which are Malaysian-controlled only commanded 5.9 percent of sums insured in force and 2.6 percent of annual premiums in force in 1999. These small Malaysian-controlled insurers have a long way to go to acquire economies of scale through organic growth. Thus, Central Bank of Malaysia infers that it is imperative for the smaller insurers to reorganise their strategy through mergers and business amalgamation in order to leapfrog in a more liberalised and competitive market environment.