

Investment Risk for Takaful Operators

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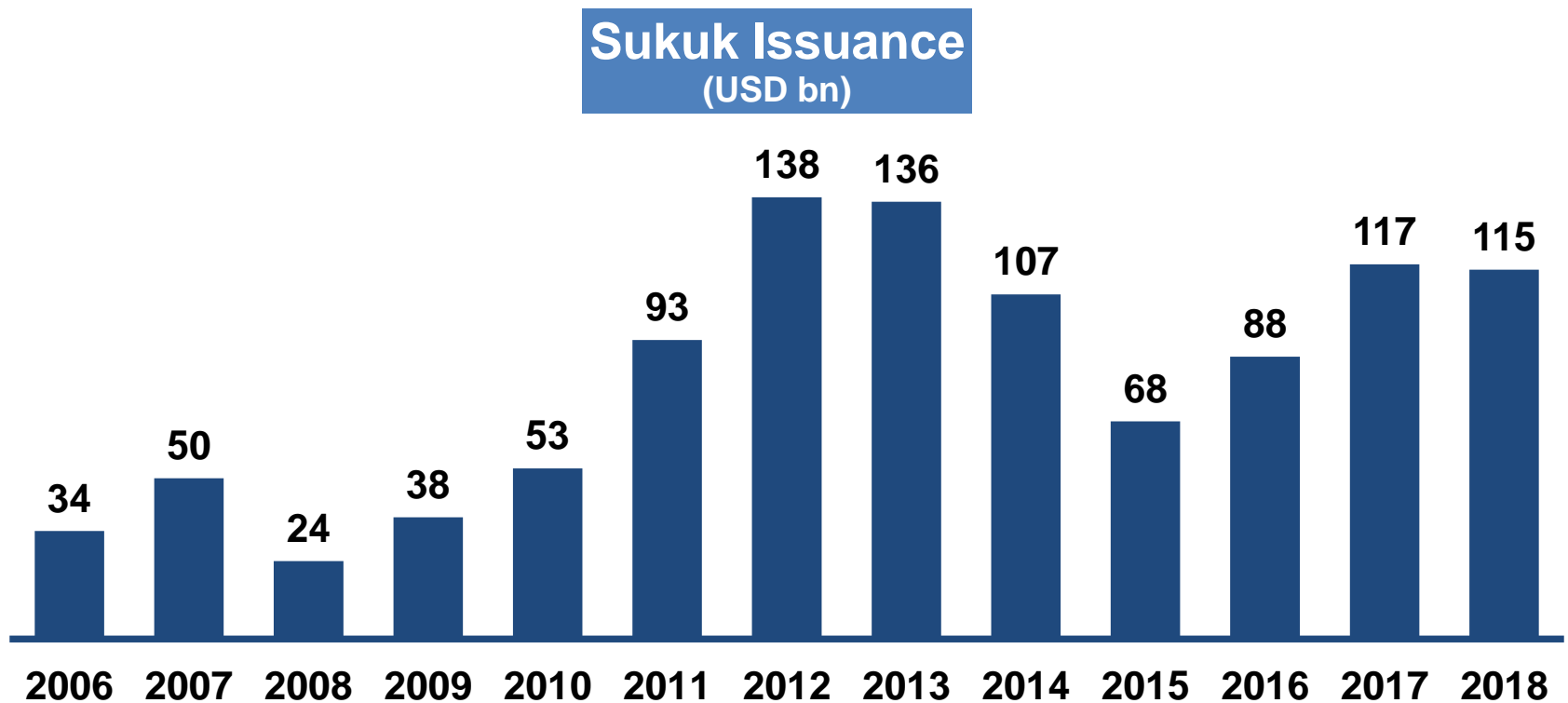
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Asset Restrictions for Takaful Companies

- Takaful companies have a requirement for their investments to be Sharia compliant
- Islamic concept of investment is based around cooperation and mutuality of risk and reward
- Key requirements for Sharia compliance:
 - Riba (usury/interest)
 - Loans should be backed by physical assets (similar to ABS)
 - Cooperation/mutuality
- Implications:
 - Equity instruments are fine as long as underlying business does not trade in 'unIslamic' goods and services
 - Sukuk replaces conventional bonds, as bonds have interest/coupon payments
 - Cash and short-term deposits to be kept in Islamic banks

Sukuk Issuance Healthy

- Sukuk issuance has fluctuated but remains healthy
- 2019 expected to be similar to 2019

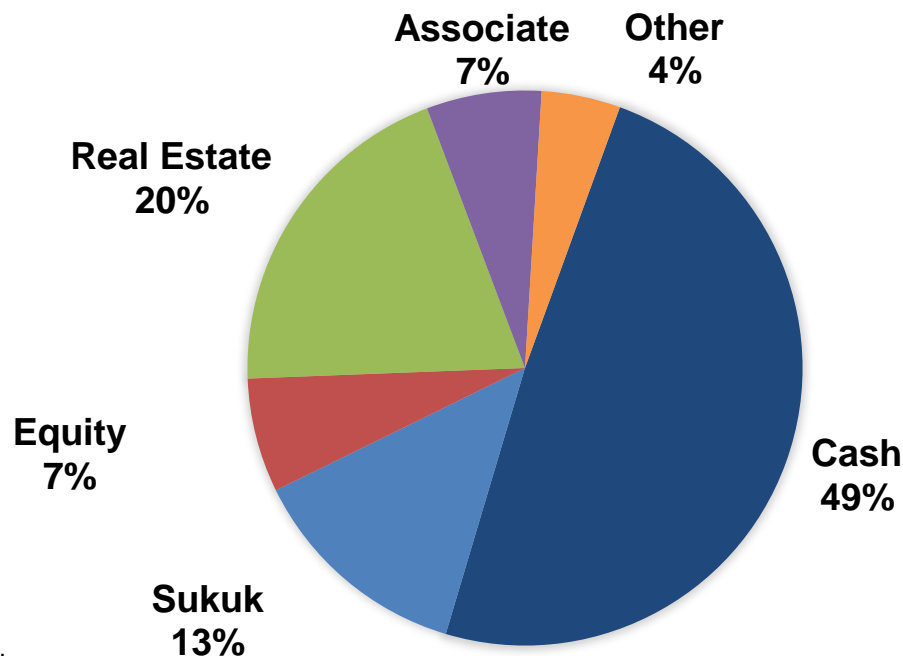


Source: IIFM, AM Best research

Asset Mix – Takaful Operators (Middle East)

- Balance sheets – reasonably liquid, with high levels of cash
- However, sukuk exposure limited, with material exposures to high risk assets (equity, real estate)

Investment Allocation – Middle East Takaful Operators (2018)



Note: Excludes Saudi Arabia

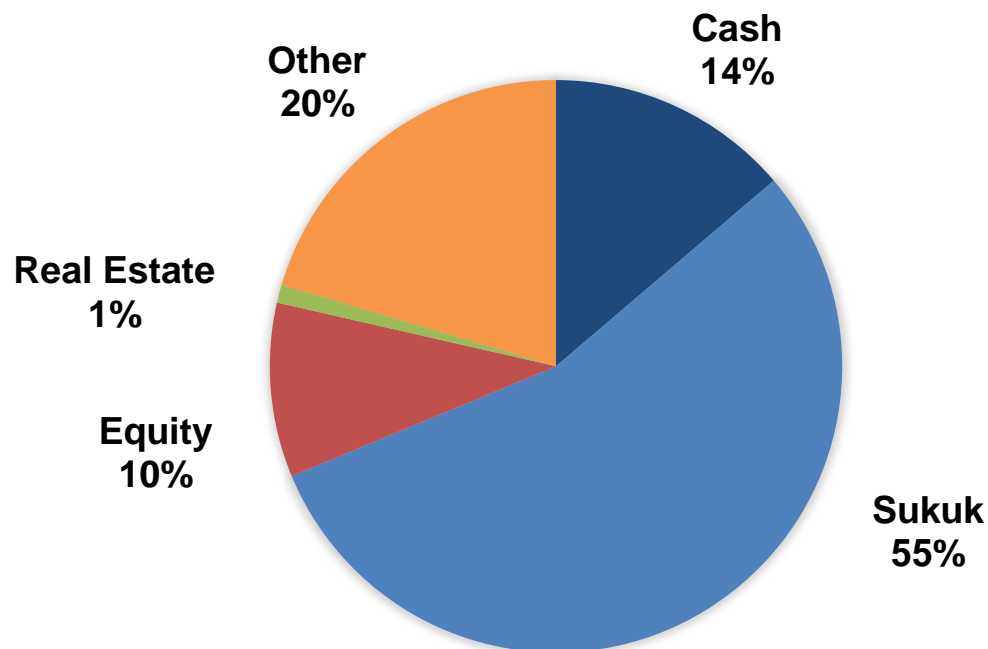
Source:  Best's Financial Suite - Global, AM Best data and research



Asset Mix – Takaful Operators (Malaysia)

- Malaysian takaful operators exhibit low risk investment strategies
- Majority invested in sukuks and cash

Investment Allocation – Malaysian Takaful Operators (2017)



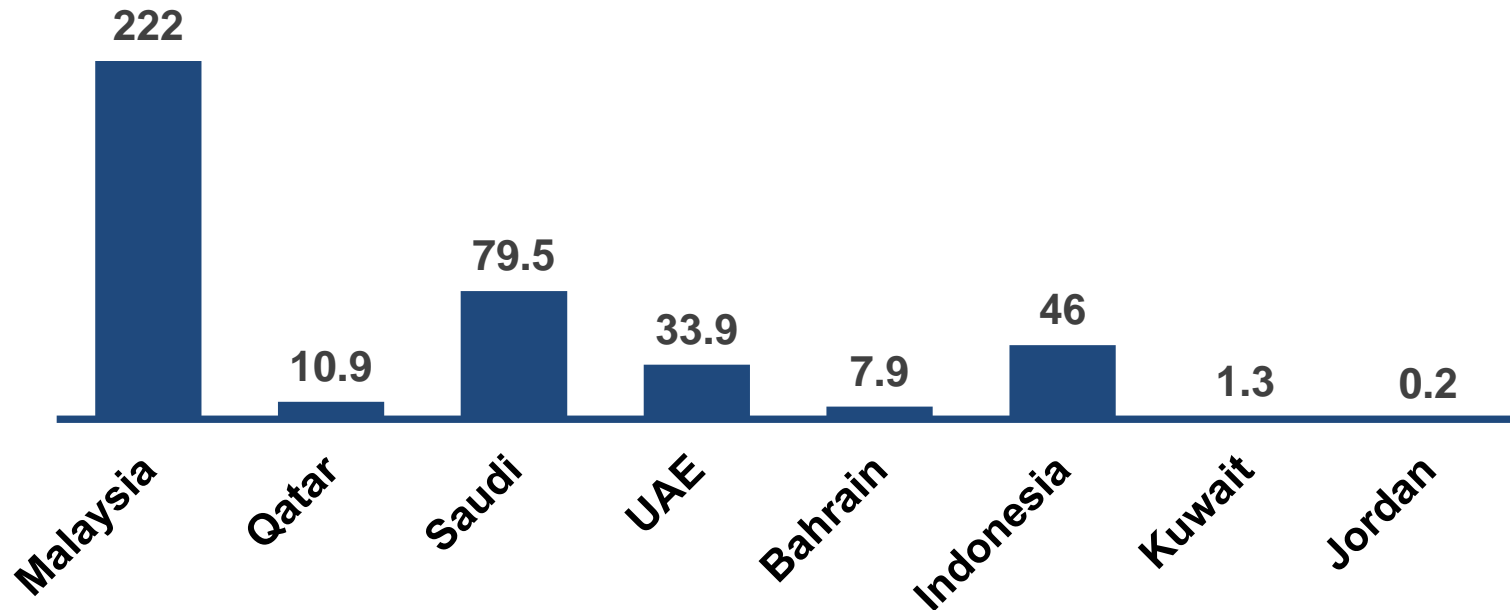
Source:  Best's Financial Suite - Global, AM Best data and research



Sukuks Concentrated in Malaysia

- More than 50% of sukuks are in Malaysia
- GCC much smaller, but still healthy
- GCC sovereign sukuks vary in credit quality

Outstanding Sukuks by Country (2017)

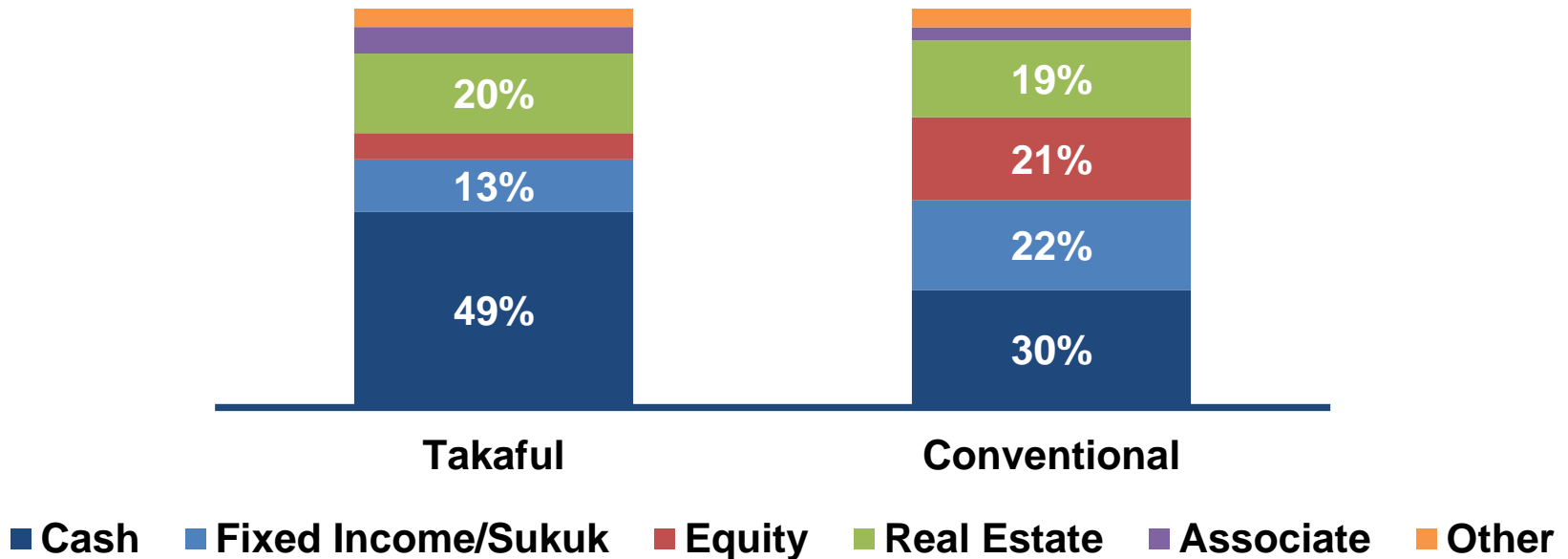



Source:  Best's Financial Suite - Global, AM Best data and research

Takaful vs Conventional

- Asset mix of Middle Eastern takaful operators slightly more liquid and conservative relative to conventional counterparts
- Both overexposed to real estate
- Look to use investment returns to offset underwriting losses

Middle East Insurance Asset Mix (2018)



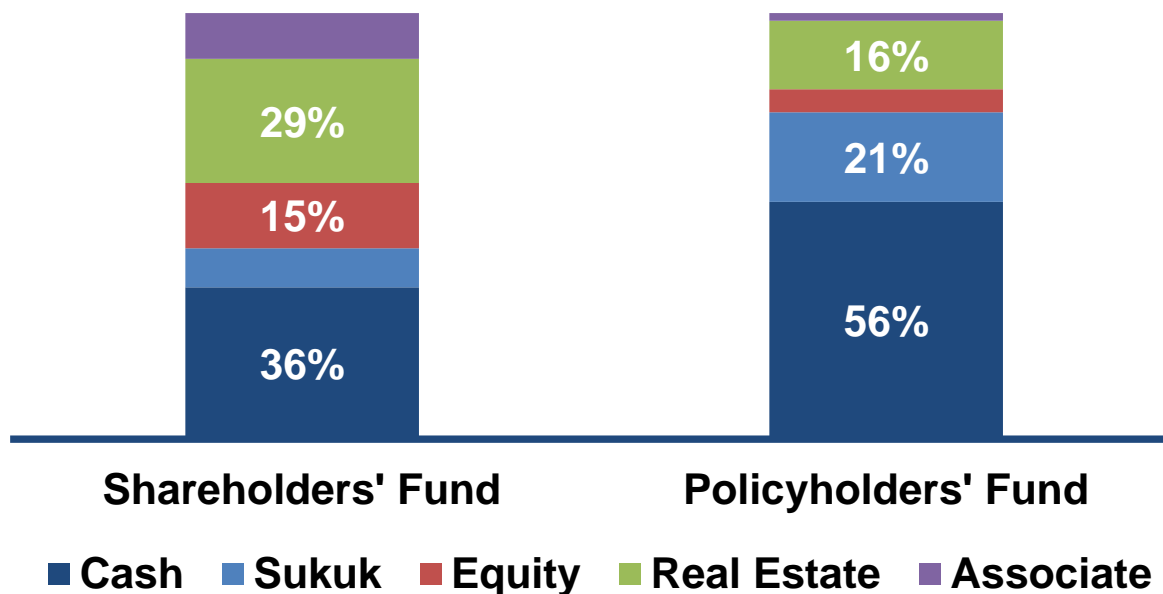
Source:  Best's Financial Suite - Global, AM Best data and research



Policyholder assets

- Most of high-risk assets are kept in Shareholders' Funds, with Policyholders' Funds more liquid
- However Policyholders' Funds still have material allocations of real estate and equity

Asset Mix by Fund (2018)

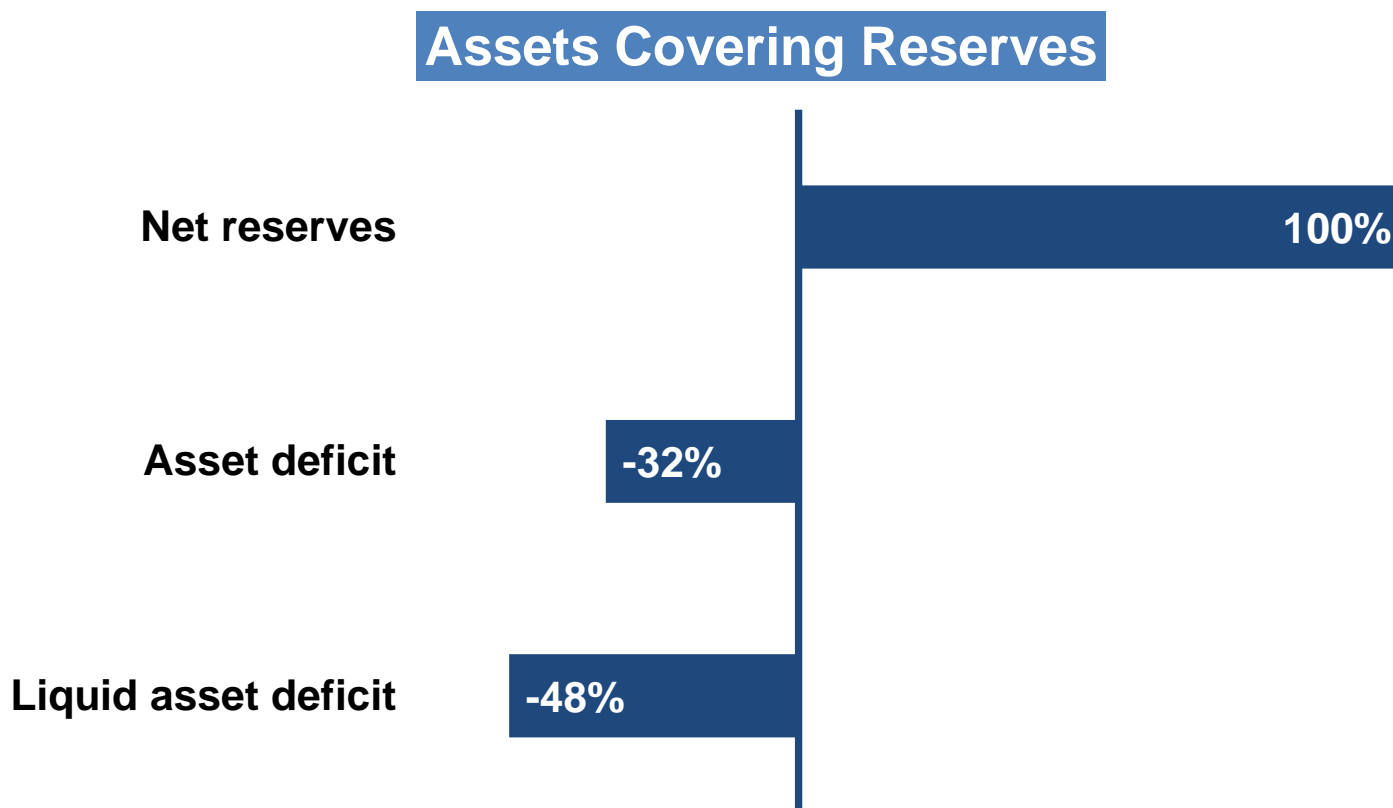


Source:  Best's Financial Suite - Global, AM Best data and research



Policyholder Assets

- Enough ring-fenced assets to cover reserves?



Source:  Best's Financial Suite - Global, AM Best data and research



Rating Implications

- Sukuks are broadly treated as fixed income under AM Best's Best's Capital Adequacy Ratio (BCAR) capital model
- High risk assets like real estate and equity are charged higher
- Charges go up for concentration risk

Environmental , Social, Governance (ESG) Considerations



- ESG becoming increasingly important globally
- Some overlap between Halal investing and ESG
- However, ESG is broader and more holistic
- Currently, ESG doesn't appear to be part of the investment thesis of takaful companies

Q&A

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