Developments in the malaysian reinsurance market

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For a number of decades, Hongkong and then Singapore were the dominant reinsurance centers in Southeast Asia. More than 25 professional reinsurers are still registered in Hongkong, although it was reported that probably only half are actively operating. On the other hand, more than 50 international professional reinsurers have branch offices or subsidiaries in Singapore. When you add the number of international reinsurance brokers with offices in either or both countries as well as the locally-incorporated intermediaries who engage in both direct and reinsurance broking, you can readily appreciate the enormous reinsurance capacity that is available within the region. Probably except for some very specialized or large risks, direct writing companies in the region do not have to go to London or Europe or the United States to place their surplus reinsurance risks. Theoretically, they don't even have to leave their desks to find capacity with the number of regionally-based reinsurers or brokers who visit their markets and knock on their doors.

Given this situation, it is not at all surprising that the reinsurance market in the region has been and continues to be extremely competitive. "Soft market" and "overcapacity" have been terms long used to describe the situation in the area.

Reinsurers and brokers scramble and battle for business in a region where reinsurance market conditions have become very difficult and profit margins have eroded due to, among other factors, high acquisition costs, inadequate premiums, high retention levels and local reinsurance placements mandated by government insurance supervisory authorities. The effects of the so-called "hard market" in Europe, the USA and other areas have just begun to be felt in the region and even so, certainly not in a pervasive manner.

Against this backdrop, it is interesting to observe the developments in the Malaysian reinsurance market. As part of its efforts to promote the country, and in particular the island of Labuan in East Malaysia, as new financial center, the Malaysian government has opened its doors to international reinsurers and brokers.

These entities, though, have to comply with the provisions of either the Malaysian Insurance Act or the Financial Offshore Act. The latter was promulgated to govern the development of Labuan as the newest financial center in the region. Various incentives and benefits have been offered to attract overseas companies to set up operations in this free port where no sales tax, surtax, excise or import and export duties are levied.

Among the overseas reinsurers who applied for and were granted licenses under the Malaysian Insurance Act to operate in Malaysia, based in the capital city of Kuala Lumpur are the Munich Re, the Swiss Re, Employers Re, Hannover Re and Gerling Global Re and Toa Re. These reinsurers are also expected to develop and bring in offshore or non-Malaysian business as the intention is for their operations in the country to be regional in scope, rather than entirely being focused on writing Malaysian business. They are now familiar fixtures in the local reinsurance market scene along with the domestically-incorporated Malaysian National Re, one of three domestic professional reinsurers.

Other reinsurers have also been licensed to operate in Malaysia under the Financial Offshore Act. Among other provisions under this law, the reinsurers involved (and other non-insurance entities who apply and qualify for a license) must maintain a registered and manned office in Labuan. Presently, these reinsurers are allowed to maintain a marketing office in Kuala Lumpur, subject to manpower restrictions and other regulations. Among the international reinsurers who have received licenses to operate in Malaysia under this act are the AXA Re, Copenhagen Re, Labuan Re, Sumitomo, SCOR, Tokio Marine Global Re and Partner Re.

The Labuan International Insurance Association lists as its members a total of 48 reinsurance, insurance, broking, investment and other insurance-related entities.

Physical proximity of the local offices of international reinsurers to the Malaysian insurance companies obviously gives these reinsurers a great advantage over non-registered overseas reinsurers in terms of access to Malaysian reinsurance business.

In addition, the guidelines issued by the Bank Negara, the insurance supervisory authority in Malaysia, on general reinsurance arrangements to be followed by the Malaysian insurance companies (issued 21st April 2000 and effective 1st June 2000) can be regarded as working in favor of the locally-registered reinsurers.

These guidelines were issued, in the words of the Bank Negara, to "promote the development of a sound and stable insurance industry, in particular, a mature and dynamic reinsurance market; and to "preserve the integrity of the Malaysian insurance market by protecting insurers and ultimately policy owners, from solvency threats arising from difficulties encountered in recovering reinsurance balances from reinsurers." The major sections of the guidelines cover the topics of Appropriateness of Retention Levels; Security of Reinsurers; Spread of Reinsurers; and Appropriateness of Reinsurance Contracts. Among the salient provisions of these guidelines are:

- The reinsurer must be legally set up in accordance with the laws of its home country and has been authorised to carry on reinsurance business in other countries and Malaysia is not precluded.
- The use of various tools and publications to assess the capacity and financial strength of the reinsurer. In the case of overseas placements, insurers must ensure that the reinsurers they use for such placements must have a minimum of *"A" rating* by an accredited rating agency or have a combined paid-up capital and surplus of at least USD 150 million.
- Total reinsurance cessions (facultative and treaty) to foreign reinsurers should not exceed 50% of the direct-writing company's total reinsurance premium.
- No one foreign reinsurer shall hold more than 25% of a risk in the case of a lead reinsurer and 10% of a risk in the case of other participants.
- "In general, insurers shall ensure that their reinsurance arrangements fall in line with national aspirations and to the extent possible, accord priority to optimisation of the Malaysian insurance capacity followed by Labuan, before securing foreign reinsurance support."

With the capacity generated by the locally-based reinsurers and the increased financial strength of the Malaysian direct writing companies, it is estimated that facultative risks with sums insured of RM 800,000,000 (around USD 200,000,000) can be fully absorbed by the local market. Also, Combined Liability Excess of Loss covers are retained almost 100% within the country. Hence, even without restrictions on the amount and kind of business which can be reinsured overseas, it is apparent that less and less business will come out from the Malaysian market.

With the strengthening of the Malaysian domestic reinsurance market, the next question is whether Malaysia, through its locally-registered reinsurers and intermediaries, be able to attract inward business from overseas to be able to challenge Singapore and Hongkong and become the newest regional reinsurance center for Southeast Asia? ■

Companies consulted by the author:

- Malaysian National Reinsurance Berhad, Malaysia.
- Labuan Reinsurance (L) ltd., Malaysia.
- Munich Reinsurance Company, Malaysia Branch.
- Arig Reinsurance Company, East Asia Regional Office, Malaysia.