midf RESEARCH

27 September 2018 | Sector Update

Insurance and Takaful

***Maintain* POSITIVE**

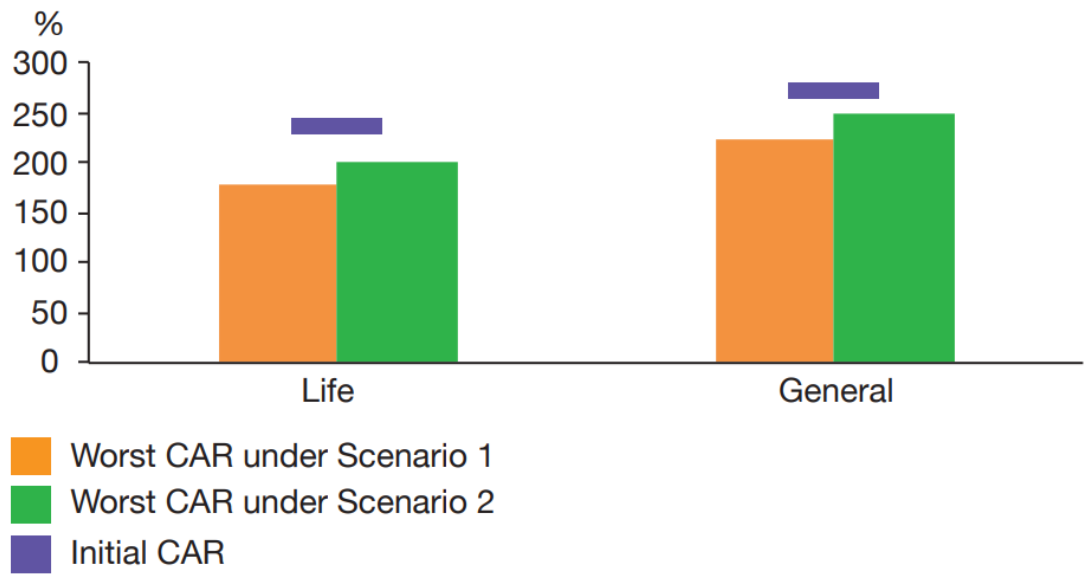
Long-term outlook seems bright

INVESTMENT HIGHLIGHTS

- **Strong Capital Structure, a positive for growth**
- **Profitability remained, but investment slightly impacted**
- **New business growth points towards healthy yearly performance**
- **Maintain POSITIVE on the sector, based on resilient trend**

Based on the BNM's mid-year performance report, the foundational structure of insurance and takaful industry continued to remain healthy, supported by strong capital position and sound profitability. We noted that the sector's CAR stood at 239.3% as of 1HCY18, growing by +630.0bps from CY17. Additionally, its financial strength was apparent through the stress test result, whereby the post-stress CAR stayed resilient above the regulatory minimum of 130%. Following this evaluation, we believe it signals positive tone on insurance and takaful business as it moves forward to grow premium income.

Exhibit 1: Insurance Sector – Results of Stress Test on Capital Adequacy Ratio (CAR)



Source: BNM

Charting a new high. In terms of new business, life insurers and family takaful operators recorded a higher growth in premium at +7.7%yoy in 1H18 (1H17: +6%yoy). This was driven by the rise in credit-related insurance and takaful products (i.e. Mortgage Reducing Term Assurance and Takaful insurance policies), on the back of higher housing loans disbursed. We are positive on the trajectory charted by life insurers and family takaful operators, in which new business premium continued to be uplifted by the resilient demand of life policies among domestic households. Moving forward, we expect wide headroom for further growth to remain due to the low penetration rate of insurance policies in Malaysia.

Direct channel is gaining traction, a positive for new market. In the same period, we are encouraged to see more new protection term products being distributed through direct channels, growing faster at +12.3%yoy (vs +9.8%yoy in 1H17). While the introduction of direct channel was recently regulated in July 2017, this signalled a more meaningful progress for the sector given the lingering challenges in reaching wider and underserved domestic market. Recall that direct distribution channels refer to distribution of products through the head office and branch premises, or an online platform.

In the general segment, medical and health segments has grown its gross direct premium by +9.0%yoy in 1H18, owing to the rising demand for group medical policies. Moving forward, we expect the continuous increase in medical and healthcare costs will continue to fuel the demand in the long-term. Recall that Malaysia's medical and healthcare inflation is the highest in the region, growing by +11.5%yoy and +12.7%yoy, in 2016 and 2017 respectively. At this juncture, we believe it is important to point out that government is already mulling on the possibility of raising consultation fees for medical practitioners. This will be applicable to private clinics and hospital with new charges ranging from RM30.00 to RM125.00. Assuming this will go through, we will not be surprised to see the demand for medical insurance policies to rise, hence benefiting the sector.

Shedding light on the off-shore oil related business. While the segment only accounted for less than 5% of total gross direct premiums, we believe that there is a potential uptick in growth. This is stemming from the recovery of global oil price, which has posted YTD average growth of +25.05yoy. Following this, our house view opine that there is a high possibility for oil companies to start rolling out new business activities, providing new opportunities for insurers to expand their income in this segment.

Weaker investment return due to uncertainties. We are cognizant of the fall in overall profitability contributed by weaker investment returns in 1H18. Notably, this was in line with the negative performance of domestic financial market post GE14. While this has weight down earnings, we remain positive on the fundamental structure of insurers and takaful operator's investment, whereby blue chip stocks continued to account a significant portion of total equities. As such, we believe earnings will start to improve once clarity and confidence is gained from the new government. We noted that Budget 2019 will be announced in early November, which will provide more precision towards the government's fiscal direction in the near term.

Maintain POSITIVE. Overall, we believe the sector is optimized to make further gains on the back of strong capital position and huge protection gap in the population. Given our view, we are maintaining our stance with positive overtone on the takaful sector. We opine the underlying demand for takaful products will continue to be driven by (1) the continuous growth of Islamic financials products and services, and (2) under-tapped participation of non-Muslim market, which we believe will continue to outpace the growth of conventional insurance. Accordingly, we continue to favour **Syarikat Takaful (TP: RM4.44)** as our top pick.

Exhibit 2: Insurance Peers Comparison

Stocks	Mkt Cap (RM'm)	Last Price (RM)	P/E	P/B	ROE (%)	Dividend Yield (%)
Syarikat Takaful Malaysia Keluarga Berhad	3,173.2	3.85	14.1	3.4	26.1	3.9
LPI Capital Berhad	6,772.5	17.00	21.6	3.3	16.3	3.7
Tune Protect Berhad	586.4	0.78	11.6	1.2	10.2	3.9

Source: MIDFR, Bloomberg

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MIDF AMANAH INVESTMENT BANK : GUIDE TO RECOMMENDATIONS	
STOCK RECOMMENDATIONS	
BUY	Total return is expected to be >10% over the next 12 months.
TRADING BUY	Stock price is expected to *rise* by >10% within 3-months after a Trading Buy rating has been assigned due to positive newsflow.
NEUTRAL	Total return is expected to be between -10% and +10% over the next 12 months.
SELL	Total return is expected to be <-10% over the next 12 months.
TRADING SELL	Stock price is expected to *fall* by >10% within 3-months after a Trading Sell rating has been assigned due to negative newsflow.
SECTOR RECOMMENDATIONS	
POSITIVE	The sector is expected to outperform the overall market over the next 12 months.
NEUTRAL	The sector is to perform in line with the overall market over the next 12 months.
NEGATIVE	The sector is expected to underperform the overall market over the next 12 months.