

VIS

Credit Rating Company Limited

SECTOR OUTLOOK INSURANCE

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INTRODUCTION

Insurance is a financial product that provides protection against potential future losses or risks. It involves paying regular premiums to an insurance company, which in return agrees to compensate for specified financial losses, damage, illness, or death. The system pools risks among many individuals, making it more affordable and manageable for policyholders. The insurance sector in Pakistan holds significant importance as it functions as a cornerstone for the nation's economic resilience and growth; the same plays a pivotal role in mitigating various risks, thereby providing a safety net for individuals, families, and businesses. By offering protection against unexpected financial losses due to accidents, health issues, or natural calamities, insurance promotes a sense of security and stability. It also facilitates economic activities by enabling businesses to manage risks more effectively, encouraging entrepreneurial ventures and innovation. Additionally, the insurance industry is instrumental in mobilizing savings and channeling them into productive investments, contributing significantly to the nation's capital formation. Moreover, the sector creates numerous employment opportunities, fostering skill development and boosting the economy. Notably, it also contributes to government revenues through taxes and investments in government securities, playing a role in the overall financial health of the country. Thus, the insurance sector in Pakistan is not just about mitigating risks but is integral to the economic fabric, supporting growth and development in various dimensions.

GLOBAL INSURANCE OUTLOOK

The current macroeconomic environment is characterized by persistently high inflation rates in several jurisdictions, tighter monetary policy and increased interest rates across many regions. Financial market sentiment remains fragile, with high degree of volatility and uncertainty. Despite building macroeconomic challenges, the insurance industry continued to grow both globally and in Pakistan. In 2022, the global insurance sector experienced significant growth. The total insurance premium income reached nearly EUR 5.6 trillion. The growth rate was around 4.9%, set against a backdrop of a global inflation rate of 8.6%. The three main segments of the industry; life insurance, property and casualty (P&C), and health insurance; showed varied growth patterns. P&C insurance experienced robust growth of 8.7%, health insurance grew by 4.9%, while life insurance saw more modest growth at 2.4%. In addition, claims increased as high inflation increased the cost of repairing buildings, motor vehicles and other fixed assets that are usually covered by insurance. This led to continued rise in premium rates to cover the expenses. However, elevated interest rates augmented the investment income for insurers across the globe.

LOCAL PERSPECTIVE

Pakistan suffered from political and economic turmoil during the outgoing year; the same is characterized by persistently high inflation, import restrictions, hike in interest rates and exchange rates. Moreover, despite the unfavorable circumstances, gross written premiums for insurance industry (life and non-life) were recorded higher at Rs. 480.2b (9MCY22: Rs. 367.1b) with substantial growth witnessed in conventional & takaful and non-life segments; the same grew by 24% and 46% respectively. The aforementioned augmentation is largely on account of upward revisions in premium prices in line with soaring inflation across all segments as opposed to noteworthy expansion of client base. Owing to a few major claims pertaining to power plants and a textile company as opposed to sizable claims incurred in the SPLY, the net claim ratio of industry improved slightly to 56.8% (9MCY22: 59.3%). The sector reaped benefits of an increase in the interest rate that led to augmentation of income derived from investments to Rs. 20.7b (9MCY22: Rs. 8.1b). However, with a projected decline in interest rate a shift towards 12-month PIBs and floating-rate medium tenor securities will

become essential to add support to the bottom line. Lastly, insurance sector continued its profitability in the ongoing year with profits reported at Rs. 20.4b (9MCY22: Rs. 7.4b). Going forward, due to the prevailing slowdown in economic activity and stressed macro financial conditions, the growth trajectory in non-life premiums is expected to be uncertain while the growth in the life sector will continue to largely depend on traction in the health insurance programs. Moreover, the SECP has issued instructions of phase wise implementation of IFRS 17. The implementation is expected to translate in sizable provisioning burden for the industry; however, the actual impact of the same on industry capitalization is yet to be ascertained. No final timeline for the same is announced yet. On the other hand, with implementation of pricing tools as per international standards, profitability and business of local reinsurer will flourish.

SECTOR DYNAMICS

The insurance sector in Pakistan is multifaceted and dynamic, with several factors critical for its survival and growth. To ensure competitive advantage, companies need to stay abreast with technological advancements to streamline operations and enhance customer service. Moreover, an improvement in the market penetration by introducing products that are tailored to the unique needs of Pakistani market will fuel the growth of the sector; the same will also require presence of skilled labor that will contribute to the product development and innovation in the market. Furthermore, efficient and competitive pricing, along with accessibility of products, plays a key role in penetrating a market with relatively low insurance awareness and coverage. Externally, the Pakistani insurance sector is influenced by global trends and practices, particularly in reinsurance where dependence on global players is significant. With an increase in reinsurance premium, an impact on the sector's profitability will be evident. Government policies, regulatory framework, and economic stability will significantly influence the sector's growth. Socio-cultural aspects, such as public perception and understanding of insurance, also affect market penetration and proper education and training by companies will remain essential to address this issue.

RECENT DEVELOPMENTS

Recent developments in Pakistan's insurance sector include the implementation of a comprehensive five-year strategic plan by the Securities and Exchange Commission of Pakistan (SECP) and a significant push towards embracing technology and innovation, particularly through insure-tech. The SECP's strategic plan aims to expand insurance coverage, enhance policyholder protection, and increase the sector's contribution to the national economy. This plan focuses on addressing challenges such as low penetration rates and the need for more diversified insurance products. Additionally, the emphasis on insure-tech is set to revolutionize the sector by integrating advanced technology, which is expected to streamline processes, enhance customer service, and introduce innovative insurance products. The impact of these developments on the insurance sector in Pakistan is potentially transformative. The strategic plan's focus on broader coverage and improved policyholder protection is likely to increase the public's trust and participation in the insurance market, thereby enhancing the sector's overall growth. By leveraging technology, insurance companies in Pakistan can expect to see improved efficiency and customer engagement, leading to a more dynamic and competitive market. These advancements will also likely attract new entrants into the market, further stimulating competition and innovation. In summary, these developments are poised to not only increase the penetration and diversity of insurance in Pakistan but also to modernize the sector, aligning it with global trends and making it more responsive to the needs of the Pakistani population.

ISSUES

The insurance sector in Pakistan faces a myriad of challenges that hinder its growth and efficiency. One of the primary issues is the low penetration and density of insurance, a significant portion of the population and businesses remain uninsured or underinsured owing to limited awareness among the general public about the benefits and importance of insurance. Moreover, there's a perceived complexity and lack of trust in insurance products due insufficient customer service and transparency. Another significant challenge is the regulatory environment that requires further refinement to promote industry growth and protect policyholders. The sector also struggles with a lack of innovation and product diversity, often failing to meet the varied and evolving needs of the modern consumer and business landscape. This situation is further exacerbated by limited use of technology, resulting in inefficiencies in service delivery and customer engagement. Furthermore, the industry faces challenges in addressing specific sectors such as agriculture and health that are crucial for the country's socio-economic development. Agricultural insurance, for instance, is not widespread, leaving a large segment of the population susceptible to natural calamities. Similarly, health insurance coverage remains inadequate that is a cause of concern for a country with sizable health-related expenditures. These issues, combined with an overall inefficient taxation regime, create a challenging environment for both existing and potential new players in the insurance market.

FUTURE OUTLOOK

As per estimated forecasts, the global insurance market grew by 10% from 2021 to 2022, reaching almost 6 trillion U.S. dollars. Following this, it is predicted that the industry will grow at a compound rate of around nine percent per year, reaching almost 8.4 trillion U.S. dollars in 2026. However, the global insurance industry is navigating through a landscape marked by several challenges and opportunities. Insurers are increasingly integrating advanced technologies to streamline processes, improve the risk assessment and enhance customer experience. Moreover, with an increase in the frequency and severity of natural disasters a need is arising for the insurance companies to revise their existing risk models and innovate in terms of their risk coverages. Moreover, digital transformation has led to susceptibility to cyber-attacks and a demand for cyber-insurance products is evident; the same is yet to be crafted by insurers without exposing themselves to excessive liabilities. Economic uncertainties, including fluctuations in financial markets and geopolitical tensions, can impact investment returns for insurers and alter consumer spending patterns. Going forward, a decline in policy rate is expected therefore an incorporation of fixed income and medium-term debt instruments in the investment portfolio will be essential to generate favorable investment incomes. Lastly, in order to thrive in this sector as a local insurer, it is imperative that the companies launch micro insurance products; the same will cater to the needs of low-income households of Pakistan that are in abundance. Furthermore, companies need to educate and boost awareness regarding the benefits of insurance to address the insurance penetration issues prevalent in the country; the same will translate to a growth in the business going forward.

SECTOR OUTLOOK

In conclusion, the insurance sector in Pakistan is undergoing a period of significant transformation and growth. With the introduction of SECP's five-year strategic plan and the increasing focus on insure-tech, the sector is poised for modernization and expansion; the same is expected to address existing challenges such as low insurance penetration and limited product diversity, and it will enhance the overall efficiency and competitiveness of the market. Future growth in the global insurance market, coupled with advancements in technology and a need for innovative insurance solutions,

presents both challenges and opportunities for the Pakistani insurance sector. On the backdrop of aforementioned factors, this sector is assigned a 'stable' outlook. Going forward, an improvement in penetration, growth in business and introduction of innovative products that cater to needs of the masses will remain essential indicators for assigning a 'positive' outlook to this sector.

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