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Asian economic outlook – robust, but risks still remain

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Asian economic outlook – robust, but risks still remain

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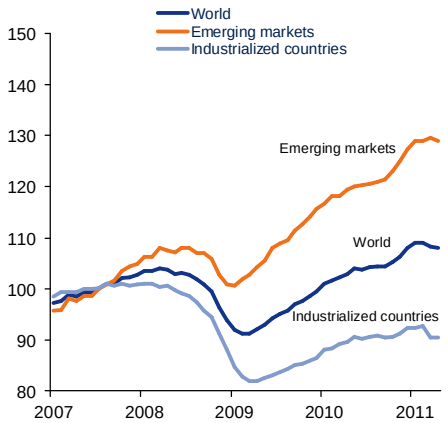
1. GLOBAL ECONOMIC BACKDROP

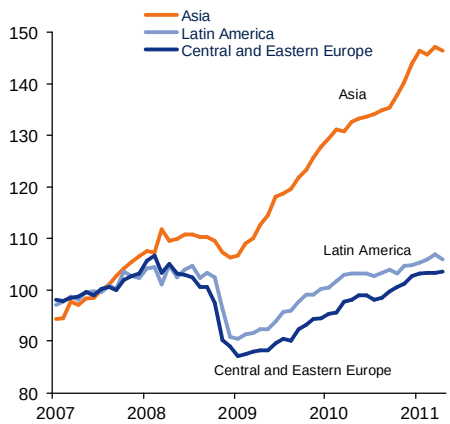
The massive economic slump seen in the winter of 2008/2009 was followed by what was in part a very strong rebound in the world economy that has persisted to date. Global output rose by 4.1% last year, having tumbled 2.1% in 2009. However, the scale of the recovery varied widely among the individual countries and regions. Growth in the emerging markets was particularly dynamic, above all in Asia where industrial production is now a good 46% up on its 2007 level. For comparison: the industrial countries have still not made up the production losses caused by the crisis, with industrial output currently still almost 10% below its 2007 level.

High momentum in emerging markets

Global industrial production
Index, 2007=100



Emerging market industrial production
Index, 2007=100



Source: CPB Netherlands Bureau for Economic Policy Analysis.

Following the robust start to the current year, the global economy is likely to have cooled in the second quarter. Two factors were chiefly to blame: Firstly, the natural and nuclear catastrophe in Japan disrupted supply chains around the globe. Secondly, the steep rise in commodity prices took a nasty chunk out of the real incomes of both households and businesses. In addition, the escalation of the sovereign debt crisis in Europe is likely to have at least dampened economic expectations slightly. Although we see the economic upswing continuing around the globe, it is likely to be more moderate than in the past 1½ years. World trade will continue to expand but not at the pace seen in the immediate aftermath of the global economic slump. And the ongoing consolidation drives in many industrial countries are likely to weigh on growth there at least in the short and medium term. All told, global output is likely to increase by 3.3% this year.

Without doubt the risks to the global economy have risen in recent months. First and foremost, these are:

- Further escalation of the sovereign debt crisis in Europe and in the USA
- Renewed surge in the oil price in the shadow of the upheaval in North Africa and the Middle East
- Renewed and pronounced economic weakness in the USA

- Inflationary developments in the emerging markets (particularly in China)
- New spate of production outages in Japan

2. ASIA: PACE OF GROWTH MORE SUBDUED FOR TIME BEING

The past few years have seen Asia's emerging markets steadily ratchet up their share of global output – thanks primarily to the strong expansion witnessed in China. In the period between 2000 and 2010, this share grew from 10.4% to the current level of 18%. Developments in 2009 and 2010 proved particularly dynamic, with Asia registering an annual increase in its slice of the output cake to the tune of 1½ percentage points. By way of comparison: the average gain made in the five years leading up to the global financial and economic crisis came in at "only" 0.8 percentage points a year.

At the peak of the "Great Recession" in the fall of 2008, when global trade sank into a state of shock, a growing chorus of voices started pointing to the need for the Asian emerging markets to make fundamental changes to their growth models to ensure continued rapid growth in the future, too. These calls referred to moves to boost domestic demand and, in particular, private consumption, in order to reduce these countries' heavy reliance on the export sector. In 2010, "year 1" after the severest global economic slump witnessed since the Second World War, the economic growth of Asia's up-and-coming economies had already bounced back to 9.5%, actually marginally topping the average annual growth rate in the period prior to the crisis (2003 to 2007: 8.9%). So were the calls for adjustments to the Asian growth model overdone, and will the region simply return to a growth path that it merely temporarily strayed from as a result of the crisis? Probably not. Instead, there are a good number of signs suggesting that, as early as this year, Asia's emerging markets will be unable to match the strong growth seen in 2010. At this point, we would like to delve into only the main reasons behind this development:

- Last year, Asia reaped considerable benefits from the strong recovery in global trade, which, by the fall of 2010, had already made up for the preceding massive slump. Although world trade will continue to expand in 2011 and 2012, the momentum will almost certainly fail to live up to the 2010 levels.

- The rapid, very dynamic recovery witnessed in Asia's emerging economies from 2009 onwards owed itself not least to the very fast and aggressive reaction to the crisis on the monetary and fiscal policy front. In the majority of these countries, the fiscal policy measures were phased out at the end of 2010, meaning that we can no longer generally expect any positive impetus in this respect. At the same time, numerous Asian central banks have been adopting an increasingly more cautious stance in the face of high inflation rates and signs that their economies might be overheating. The Indian central bank, for example, started to tighten the monetary policy reins back in March 2010. Since then, it has gradually jacked up its key interest rate from 4.75% to its current level of 7.5%.

- Current economic indicators, such as the purchasing managers' indices, as well as data on industrial production and external trade, suggest that economic momentum slowed in the second quarter of 2011. In China, the national purchasing managers' index for the manufacturing sector in the month of June was down for the third time in a row. At 50.9 points, the index is now at its lowest level since February 2009 and is only just above the 50-point expansion threshold. Values above the threshold point towards growing economic activity, while values below the threshold signal that things are slowing down. The economic slowdown seen in the

spring is likely to be attributable, among other things, to the natural and reactor catastrophe in Japan. The Japanese disaster not only disrupted production chains between the Asian countries, which enjoy extremely close economic ties, it also had global consequences. Taiwan was among the hardest hit by the interruption of the international supply chains, with Taiwanese industrial production in March to May 2011 down by a cumulative 5.1% on February. The current rapid recovery evident in Japan, however, suggests that most of the production losses suffered in the spring can be made up for as the year progresses. In addition to the Japanese catastrophe, the steep rise in commodity prices is also likely to have played its part in the more tepid Q2 development, taking a nasty chunk out of the real incomes of private households and businesses alike.

All in all, we expect the Asian region to grow by 7.9% in real terms this year, a good 1½ percentage points less than last year. Looking ahead to 2012, we forecast an increase of just under 7½%. This rate corresponds more or less to our medium-term growth forecast for Asia's emerging markets, well below the growth rates seen prior to the crisis.

Growth rates in Emerging Asia

- real GDP, percentage change over previous year -

	2008	2009	2010	2011[1)]	2012[1)]
China	9.6	9.2	10.3	9.3	8.5
India	6.2	6.8	10.3	8.5	8.0
Indonesia	6.0	4.6	6.1	6.0	6.0
Malaysia	4.7	-1.7	7.2	4.3	5.0
Singapore	1.5	-0.8	14.5	5.5	4.5
South Korea	2.3	0.2	6.1	4.3	4.7
Thailand	2.5	-2.3	7.8	4.0	4.5
Emerging Asia	**6.9**	**5.9**	**9.5**	**7.9**	**7.4**

1) forecast.

The slowdown in the pace of growth in the coming years is primarily attributable to China, where economic policy has been attempting, for some time now, to combat economic overheating (real estate boom, situation in the financial sector given the excessive lending seen in recent years, sharp rise in consumer price inflation). The measures involved are alone enough to rein in growth to a certain extent, at least in the short term. What is more, China has witnessed a change of economic policy mindset in the recent past as far as its very export-focused growth model, as mentioned above, is concerned. This rethink should, if actually put into practice, translate into more moderate growth rates in the medium and long term. This shift in the Chinese government's economic policy thinking becomes particularly apparent if we compare the individual priorities and objectives set out in the old five-year plan (2006 to 2010) with those described in the new five-year plan (2011 to 2015). In the past, China has sworn by the mantra of "growth at all costs". This strategy is now giving way to a more development-oriented approach that puts the economic, social and ecological sustainability of economic activity at the forefront. Talk of aiming to double nominal per capita GDP within a ten-year period, which still featured in the old five-year plan, has been banished. Instead, China is looking to achieve stable, but nevertheless relatively rapid economic growth. The new plan makes explicit reference to changes in the country's economic make-up, the aim being to expand the service sector and modernize industry. The statements made on private consumption are of key significance: its share in GDP is to increase rapidly, with household incomes to grow in tandem with the economy, and wages in line with productivity. China is also aiming to lift the incomes of its low-earners and boost the proportion of the population in the middle-income bracket.

All of these plans are aimed at achieving an overriding objective, namely to spur domestic demand and, in doing so, reduce the Chinese economy's reliance on foreign trade.

Although the Asian region as a whole is unlikely to be able to match pre-crisis growth rates in the future, it is important to bear in mind that the very opposite will be the case for a small group of countries. Indonesia is a prime example. Thanks to successful moves to stabilize the economy in recent years, the country is now on a higher growth path than before the crisis and is likely to remain so in the medium term as well. Below, we will take a closer look at the economic outlook for a small number of selected emerging markets in Asia for both this and next year.

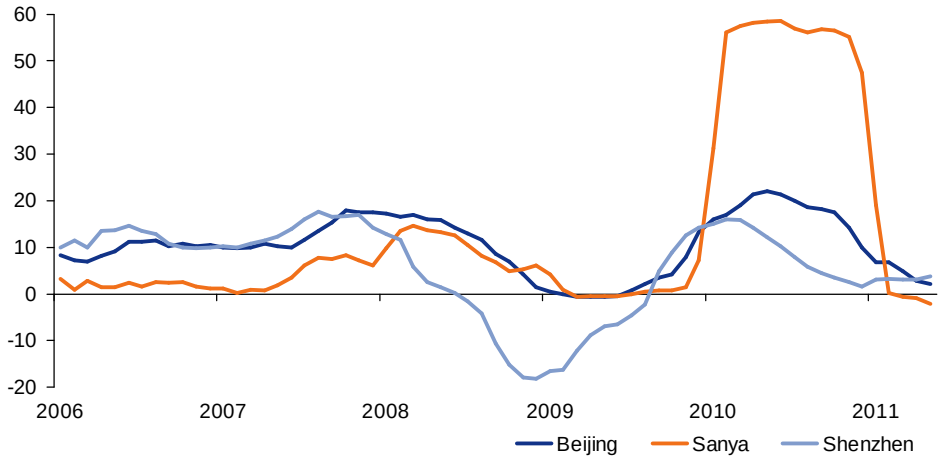
China: Controlled growth slowdown

What was already being flagged by various economic indicators, such as the purchasing managers' index for the manufacturing industry (see above), was confirmed by the latest economic growth figures, at least as far as the underlying trend is concerned. In mid-July, the Chinese National Bureau of Statistics announced a slight slowdown in economic growth in Q2 2011, with real GDP 9.5% up on a year earlier. In the first quarter of the year growth had stood at 9.7%, and at 9.8% in the final quarter of 2010.

The fact that economic momentum has eased, particularly when compared with the 2010 growth rates, is due not least to Chinese economic policy, and is therefore entirely intentional. In the course of last year, the government had already started to take targeted action to combat signs of overheating in individual sectors. Initially, the measures were aimed in particular at reining in the mushrooming lending on the part of banks, together with interventions in the real estate market, with the aim of curbing rocketing real estate prices in major cities. At least as far as the most recent developments in lending and real estate prices are concerned, the state intervention appears to be working. In June, the lending volume was up by "only" 15.2% on a year earlier, the weakest growth seen since November 2008. By way of comparison: when Chinese banks opened the lending floodgates to stimulate the economy back in 2009, the lending volume grew by an annual average of almost 29%. The trend in real estate prices has also cooled off appreciably. In Sanya, where prices for new residential property in the fall of 2010 were around 50% up on a year earlier, prices are now actually on a slight downward trend. But even if clear signs of a correction are now evident on the lending front and in the real estate sector, the risks associated with this sort of overheating are still likely to be lurking. The banking sector, for example, still faces the threat of a drastic increase in non-performing loans, a problem that could actually be exacerbated by the drive to slow growth down.

Correction on Chinese real estate market

Prices for new residential buildings, percentage change on year earlier

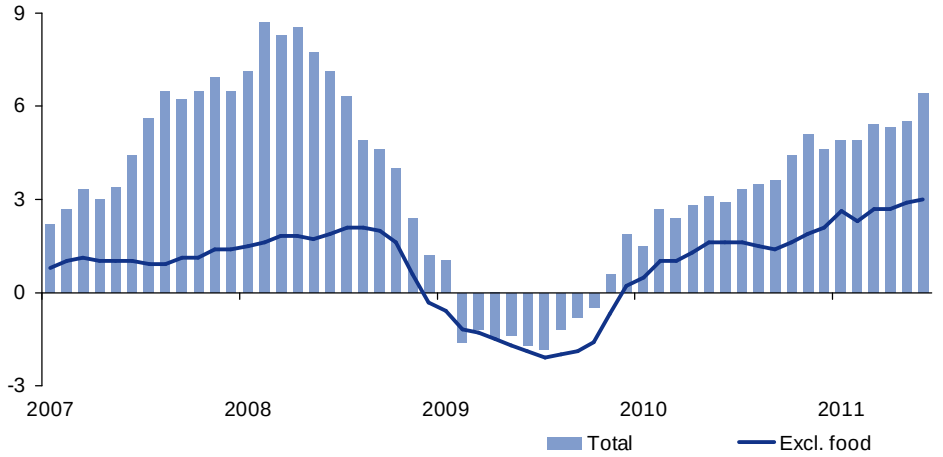


Source: National Bureau of Statistics of China (EcoWin).

But, at present, one of the main headaches for Chinese economic policy is, without a doubt, the steep rise in consumer prices. In June, they increased by 6.4% year-on-year, the steepest rise for three years. The main culprit is the rapid increase in food prices, which recently came in at 14.4%. More striking still, however, is the slow but steady rise in consumer price inflation after stripping out food, which recently touched the 3% mark, the highest level since the start of the time series in 2002. The fact that wage development has picked up speed is certainly one of the main reasons behind this trend. Ever since last year, in particular, minimum wages in many provinces have been lifted considerably. In October 2010 the Chinese central bank started to gradually nudge its key interest rate up in response to the rising inflationary pressure. The rate currently stands at 6.56%, 125 basis points above its level at the start of the current tightening cycle. In tandem with the increases in the key interest rate, the central bank has also been steadily raising the minimum reserve ratio for banks. The minimum reserve ratio for major banks currently stands at 21.5%, 600 basis points higher than at the beginning of 2010.

Sharp rise in inflationary pressure in China

Consumer price inflation, percentage change on year earlier



Source: National Bureau of Statistics of China (EcoWin).

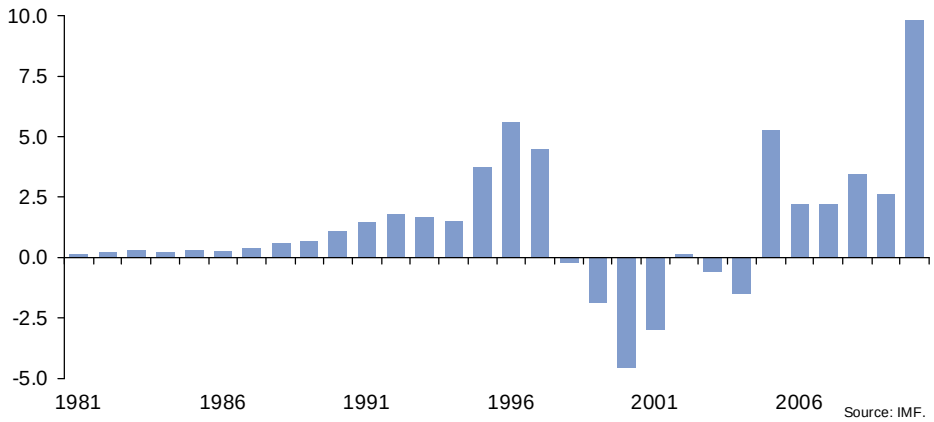
We expect consumer price inflation to pass its peak in the summer. Given the most recent developments in energy and food prices and bolstered by the economic policy measures, the rate of inflation is expected to start drifting back towards the 4% mark in the second half of 2011. Looking at the year on average, this would result in an increase of 5% over 2010. We also expect the trend towards more moderate growth rates for the Chinese economy to continue as the year moves on. In all probability, the Chinese economy is not heading for a sudden collapse in growth, a so-called hard landing. While the government's measures to combat domestic overheating will certainly eat into growth, the expected return to more dynamic global development in H2 (catch-up effects following the production outages in Japan, relief from the latest developments in commodity prices) is likely to provide positive economic impetus. All in all, this means that real gross domestic product can be expected to grow by 9.3% this year, compared with 10.3% in 2010. Next year economic growth is likely to ease to 8.5%. As mentioned above, the Chinese government has announced substantial changes to the country's growth model. This also includes more sustainable economic development that will alleviate, rather than exacerbate, existing imbalances. However, such a development is not compatible with growth rates of 9% and more in the long run.

Indonesia: Growing confidence among international investors

Economic development in the heavily export-reliant countries of south-east Asia was shaped largely by the rapid rebound in global trade. Most of these countries had already made up for the preceding economic slump in the course of 2010. Only one of the major countries in this group diverged from this economic pattern, namely Indonesia. In 2009, the year when the global recession struck, the region's largest economy bucked the general trend by reporting robust economic growth of 4.6%. In addition to the country's expansive economic policy, Indonesia owed this success first and foremost to its relatively low dependence on exports, as well as to its large and robust domestic market. Following real GDP growth of 6.1% last year, we predict growth on a similar scale this year. The country is quite evidently reaping increasing benefits from the political stability established over the past decade. Private consumption is being buoyed by rising incomes and falling unemployment. Investment activity is one of the main winners of this new stability, which creates a stable foundation for long-term entrepreneurial decisions. Investment has also been given a leg up by the marked increase in capital inflows from abroad. Last year, the inflow of net foreign direct investment totaled USD 9.8bn, the highest figure recorded since the start of the time series 30 years ago and testimony to the marked increase in the attention that international investors are paying to Indonesia.

Indonesian FDI inflows reach record levels

Net direct investment, USD bn

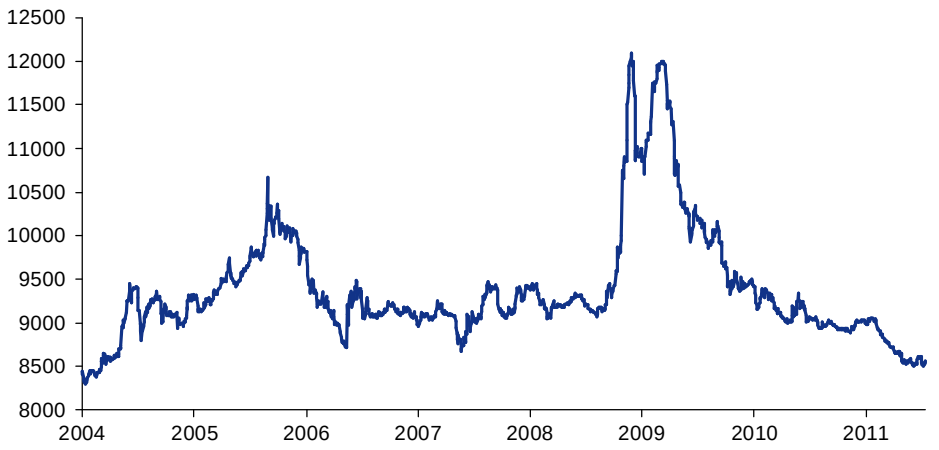


Source: IMF.

The Indonesian central bank was relatively late in reacting to the appreciable increase in inflationary pressure, a trend that had already started to emerge in 2010. Having kept its key interest rate constant at 6.5% since August 2009, it lifted it to the current level of 6.75% in February 2011, the sole hike implemented to date. When the decision was made, inflation had already been hovering at around 7% year-on-year for some months. One of the main reasons why the central bank was so hesitant is likely to have been the strength of the Indonesian currency. Having swooned from August 2008 to March 2009, the rupiah has since gained around 40% against the US dollar. One US dollar is currently worth around 8,500 rupiahs. The last time Indonesia's currency was this strong was in early 2004. With inflationary pressure currently on the wane and the rupiah still in good shape, we expect to see only one or two further interest rate hikes of 25 basis points in each case, bringing the interest rate up to a maximum of 7.25%, in the current economic cycle.

Strong rupiah

IDR/USD



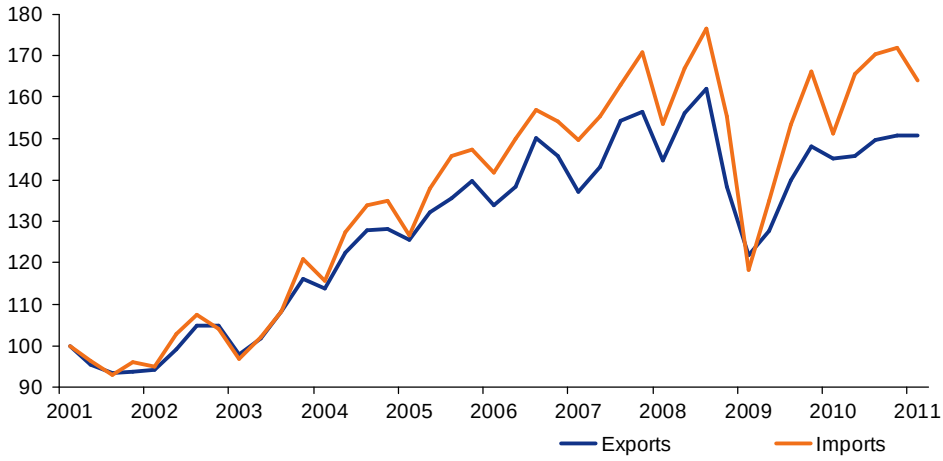
Source: EcoWin.

Malaysia: Inflationary pressure remains moderate

With a goods export ratio brushing the 84% mark of late, Malaysia is one of the Asian economies that is most heavily reliant on foreign trade. In this respect, it actually appears surprising, at first glance, that the economic slump that hit Malaysia in the wake of the global recession was no more pronounced than in other countries in the region. In actual fact, Malaysian economic output fell by "only" 1.7% in 2009. One of the reasons behind this phenomenon is likely to lie in the fact that the proportion of total imports that are export-induced is very high in Malaysia. Consequently, Malaysia requires a considerable volume of intermediates from abroad for its exports, meaning that when export demand tails off, the country's imports drop accordingly. Since import and export developments more or less mirror each other, the contribution to economic growth from net exports fluctuates far less dramatically than in a country with a substantially lower proportion of export-induced imports.

Malaysia's imports driven strongly by exports

Real exports and imports of goods and services (Index, 2001 Q1 = 100)

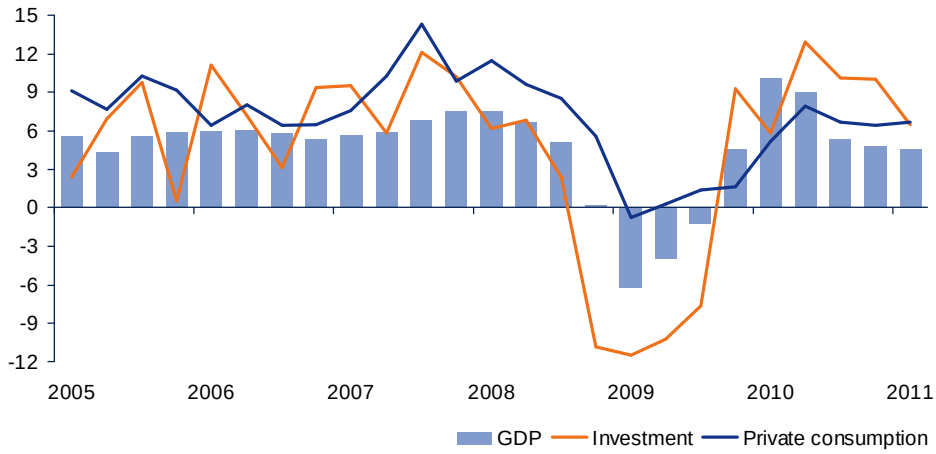


Source: Department of Statistics, Malaysia (EcoWin).

Largely thanks to very brisk investment activity and robust private consumption, the Malaysian economy was able to bounce back from the recession last year, reporting the strongest real GDP growth seen in ten years, at 7.2%. If nothing else, base effects will ensure that this year's economic expansion will be far more moderate. In the first quarter of 2011, real GDP was up 4.6% on a year earlier. Production losses sparked by interrupted supply from Japan are likely to have put at least a temporary damper on economic development in the second quarter. These losses are, however, unlikely to have much impact on growth for 2011 as a whole, as they will probably be offset as the year progresses. All told, we expect to see economic growth of 4.3 % this year, with investment and private consumption remaining the main drivers. The latter will continue to be buoyed by the positive development in labor income and the low unemployment figures.

Robust Malaysian domestic demand

GDP components, percentage change on year earlier



Source: Department of Statistics, Malaysia (EcoWin).

Although Malaysia has also seen inflation being pushed up by rising food and energy prices in recent months, the trend in Malaysia remains fairly moderate compared with other countries. In June, consumer prices were up by 3.3% on the previous year. The south-east Asian country has traditionally enjoyed a high degree of price stability, with

annual inflation rates more on a par with those in the world's advanced economies than those that prevail on emerging markets. There is no doubt that this is also due to the country's economic policy, with its emphasis on stability. The Malaysian central bank had already started to normalize key interest rates back in March 2010 and, by July of last year, had lifted its key rate from 2% to 2.75% in three steps. This was followed by a hiatus that lasted until May 2011, when the central bank tightened the reins again, bringing the interest rate up to the current 3%. We see another two interest rate hikes by the end of 2011. With key rates then at 3.5%, this should, however, signal the end of the tightening cycle.

Malaysian economic outlook – in brief

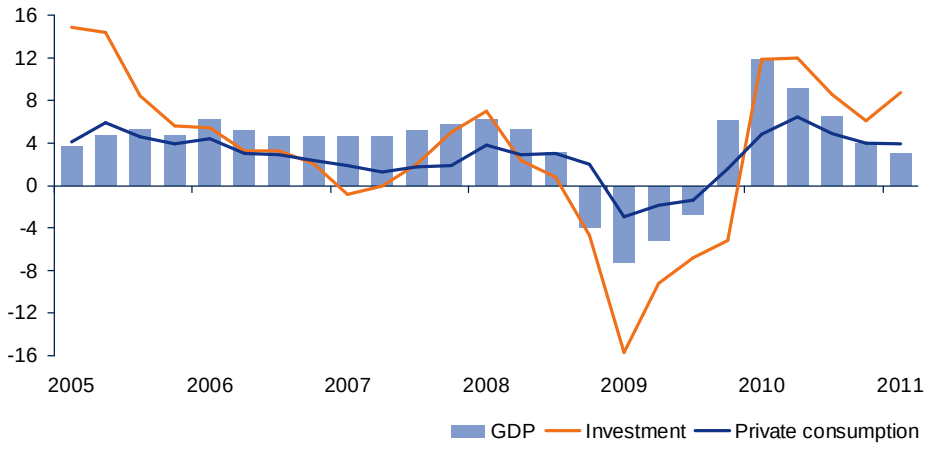
- Economy to grow by 4.3% this year, 5% next.
- Ongoing boost from foreign trade, however momentum set to moderate.
- Positive development in labor income and favorable labor market situation form basis for ongoing brisk private consumption.
- Investment momentum set to ease. One of the reasons is that Malaysia is increasingly losing out in terms of foreign direct investment to countries such as Vietnam and Indonesia where production costs are lower.
- Should political uncertainty linger or indeed intensify, this would have a substantial negative impact on the real economy.

Thailand: Temporary slump in capacity utilization

The performance of the Thai economy has resembled a roller coaster ride over the past 2½ years. Up until the summer of 2008, regardless of the occasional flare-up in political tension, real GDP notched up solid year-on-year growth of between around 4.5% and 6%, quarter in, quarter out. In the second half of 2008, the financial and economic crisis then culminated in the economic slump that reached its absolute low point in the first quarter of 2009. At that time, real gross domestic product was down by more than 7% on a year earlier. We then saw a very rapid rebound in the Thai economy and, by the fourth quarter of 2009, the country had already made up the cumulative 7.5% blow to production inflicted by the crisis. Last year, economic growth came in at 7.8% – driven by humming export demand and a lively domestic economy – the sort of growth last seen back in the mid-1990s.

Thailand's economic roller coaster ride

GDP components, percentage change on year earlier

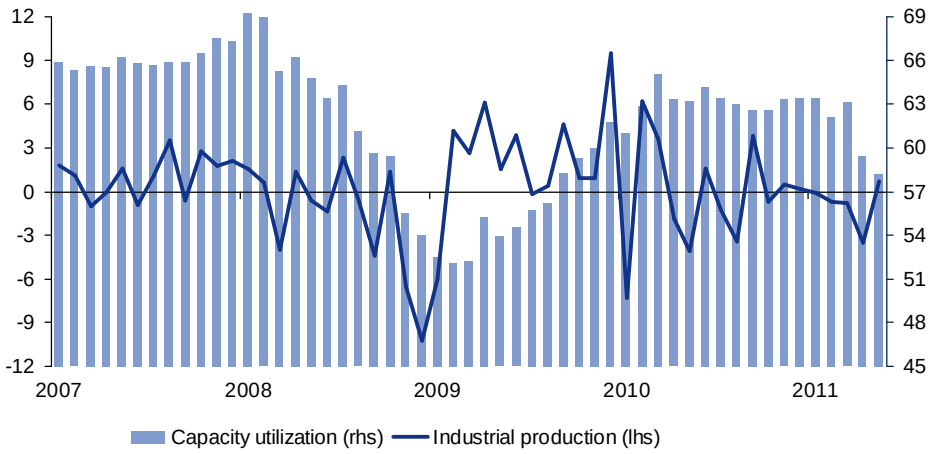


Source: Office of the National Economic and Social Development Board, Thailand (EcoWin).

This year, growth looks set to slow considerably. In the first quarter of 2011, real GDP rose only 3% on a year earlier. The second quarter is likely to have seen only modest economic development as well. This is due in the main to disruptions affecting automotive production as a result of the natural and reactor catastrophe in Japan. In April, Thai industrial production slipped by 3.5% month-on-month in seasonally adjusted terms, as did capacity utilization. A decline in capacity utilization on this scale in the space of only one month is very unusual, but shows just how dependent the Thai economy is on Japanese intermediates. There is no doubt that the economy will be able to make up for most of the recent production losses as the year progresses, suggesting that economic development will pick up speed in the second half of the year. Furthermore, the fact that the unemployment rate has now hit a record low of less than one percent, coupled with what remains upbeat consumer confidence, means that private consumption should be able to deliver sustained positive economic impetus. All told, we expect to see real economic growth of 4% this year, picking up slightly to 4.5% in 2012.

Thailand hit by Japanese production outages

Industrial production* (% change m-o-m, sa) and capacity utilization (%)



* Only manufacturing.
Source: Ministry of Industry of Thailand (EcoWin).

After inflation rates had steadily declined in the course of last year, consumer prices have been accelerating again since the spring of 2011. In June, inflation stood at 4.1 % compared with the previous year. The Thai central bank aims to keep inflation at between 0.5% and 3%. It started to gradually raise the key interest rate in July 2010 in reaction to the rising inflationary pressure. It recently hiked the key rate by 25 basis points in July, bringing it up to 3.25%, meaning that the key interest rate has been increased by a total of 200 basis points since the beginning of the tightening cycle. At the end of this year, we see it at 3.75%.

Thai economic outlook – in brief

- Economy to grow by 4% this year, 4.5% next.
- Ongoing boost from foreign trade, but momentum set to ease.
- Favorable situation on labor market and upbeat consumer confidence point to ongoing brisk consumption – despite temporary pickup in inflation.
- Investment will increase further but less strongly than last year when government investment projects led the way.
- Political uncertainty likely to fade gradually following recent elections. This is also essential if corporate sector investment is to get back into gear.

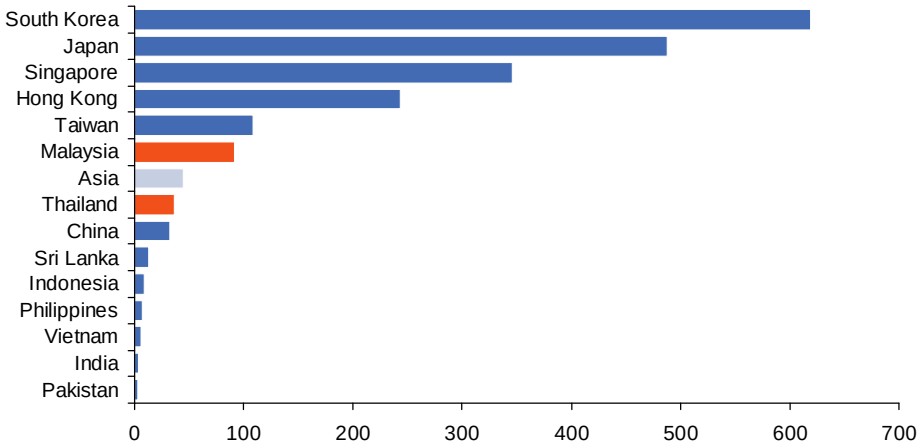
3. NON-LIFE INSURANCE MARKETS IN ASIA – LOW COVERAGE AS GROWTH DRIVER

Due to economic growth on one hand and currently still very low acceptance and penetration of non-life insurance in many emerging markets on the other, Asian non-life markets will be among the most dynamically growing markets worldwide. Per capita expenditures for non-life insurance products in Thailand are expected to at least double by 2020.

Total premium income in the Asian emerging markets will nearly treble by 2020. The main driver of this development is China which will then be – not least due to the economic catch-up process in its western and other interior provinces – one of the biggest non-life insurance markets worldwide after the US. Furthermore, non-life insurance markets in most Asian emerging markets are still in their infancy. In Thailand, for example, only every fourth person had insurance coverage in 2009. In order to foster private insurance coverage against natural catastrophes, especially in agricultural business, and property and casualty insurance in general, the Thailand government initiated the so-called National Insurance Masterplan. Despite political turmoil, non-life insurance market growth amounted to 12.4% in 2010 after a marked drop in the years before due to the financial crisis. However, insurance density, i.e. the amount an average Thai spent on non-life insurance in 2010, was only EUR 39. Against this background, Thailand's non-life insurance market has a high growth potential in both the medium and the long term.

Non-life insurance density

Gross written premiums per capita (2010, in EUR)

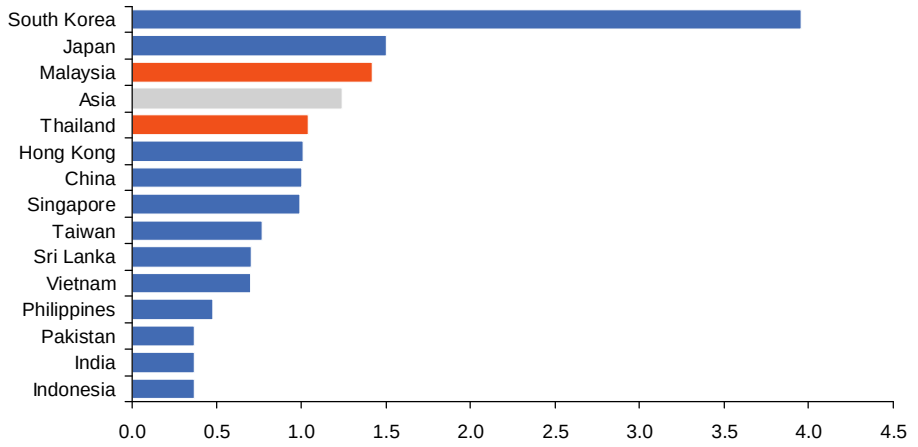


Sources: Axco, national insurance associations, IMF, UN Population Division.

With a growth rate of 8.6 %, market development in Malaysia was less dynamic than in Thailand. However, average spending per capita on non-life insurance of EUR 94 was more than double that of Thailand. This reflects the fact that the general level of wealth in Malaysia – expressed in GDP per capita – is markedly higher than in Thailand, with the average GDP per capita amounting to EUR 6633 in Malaysia and to EUR 3666 in Thailand. The second marker for the stage of development of an insurance market, insurance penetration, i.e. gross written premiums as a percentage of GDP, stood at 1.4% in Malaysia in 2010 and was thus not only 40% higher than that in Thailand but was also above the average insurance market penetration of all the Asian markets covered, which stood at 1.2%. Against this background, indicating that Malaysia's insurance market is more mature than that of Thailand, Vietnam or Indonesia for example, we expect future average growth of the Malaysian non-life insurance market to be somewhat lower than in Thailand.

Non-life insurance penetration

Gross written premiums in percent of GDP (2010)



Sources: Axco, national supervisory authorities, IMF, UN Population Division.

Taken as a whole, the Asian non-life market is one of the most attractive markets worldwide, with expected average growth of 7.8% a year until 2020. Growth will be driven

especially by those markets where insurance coverage of the majority of people is still markedly low. Besides Thailand, countries like China, India and Vietnam fall into this category. Growth rates in relatively mature Asian non-life insurance markets, like South Korea, Taiwan or Malaysia, will report less dynamic growth of an average 5.4% over the next decade.

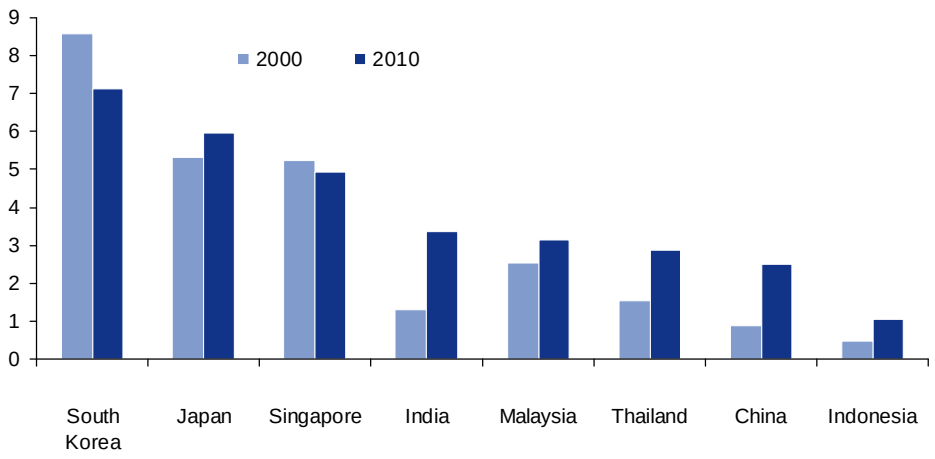
4. LIFE INSURANCE MARKETS IN ASIA STOP FOR A BREATHER

Instead of dealing a blow to life insurance markets in the region, the financial crisis offered them something of a temporary respite. With the exception of Hong Kong, Malaysia and Singapore, all markets in the region reported positive growth in the crisis-ridden year of 2009, in most cases even reaching up into the low double digits. What is more, life insurance markets in the region as a whole actually outpaced the growth in general economic output, with Asia's emerging markets making a key contribution in this regard. Last year, gross written premium growth came in at around 8%, back to just shy of the pre-crisis level of a good 9%.

In terms of total gross premiums, Japan is still the largest life insurance market in Asia, but the catch-up process in the Asian emerging markets is unstoppable. From 2015 China will be the leading market in Asia and India will have overtaken South Korea. Annual growth in premiums over the past ten years had already been well over 10% in many markets and in China, India and Indonesia average annual growth rates were actually over 25%. Premium growth in the emerging economies easily outstripped GDP growth, with the result that penetration rates in the region have moved substantially more into line over the past ten years. South Korea and Singapore, where insurance coverage is already very high, were the only countries to see a drop in penetration. However, this does not mean that insurance premiums stagnated. On the contrary: average annual growth still came in at 4.9% and 5.9% respectively.

Life insurance – penetration in emerging markets already up markedly

Gross written premiums in percent of GDP



Sources: Axco, EcoWin, National Insurance Associations.

Over the next ten years most emerging markets will manage to catch up with penetration levels in the developed economies of the region. Nonetheless, even in 2020 the growth potential of the Asian emerging markets will still not be exhausted. This is exemplified by a look at gross written premiums per capita. Hong Kong, where per capita premiums total EUR 2,384, leads the field here, with Taiwan, Japan and Singapore hot on

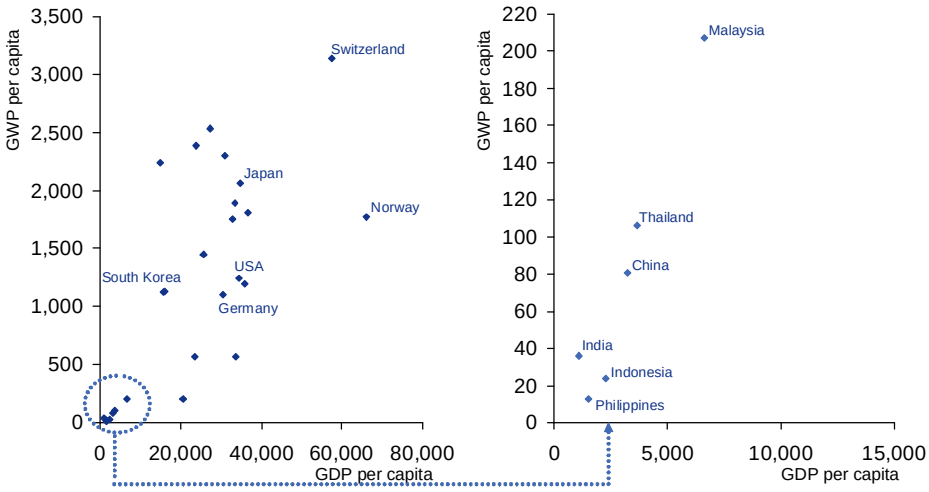
its heels. The gap over the less developed life insurance markets is much more marked than with penetration rates: China's premiums per capita stand at only around EUR 80 and even by 2020 will not exceed EUR 400. In India, per capita life insurance premiums will have climbed to just under EUR 97 in ten years' time, whereas the same figure in Indonesia will be just short of the EUR 60 mark.

A country's economic development and, above all, its prosperity level are key factors behind demand for insurance products. As a rule, once GDP per capita crosses a threshold of EUR 10,000, demand for insurance and asset management products rises sharply. Above all, as incomes rise, so do the sum insured and the premiums per policy. However, among the Asian emerging markets, only Malaysia might exceed this threshold in 2020. This means that the catch-up process still has some way to go.

Demographic change in the region is a further driver of growth in life insurance demand. Although population growth in the region is declining sharply, many economies are still fairly young societies. Up to 2050 the group of 30-60 year-olds will rise steeply and it is in this very age group that demand for life insurance products is strongest. In addition, we are also witnessing a slow rethink in retirement provision, with a greater emphasis on private provision.

Life insurance – growth potential in emerging markets still far from exhausted

GDP and GWP per capita, in Euro 2010



Sources: Axco, EcoWin, National Insurance Associations, UN.

Thailand

Total premium income on the Thai life insurance market has almost doubled since 2004, totaling around EUR 7.2bn at the end of last year. Thanks to the growing significance of bancassurance and the fact that the tax incentive for spending on life insurance products has been doubled to THB 100,000 (EUR 2,473) a year, the market managed to clock up growth of just under 16%, even at the height of the crisis in 2009. Growth in premium income was slightly less spectacular in 2010 and, at 14.7%, actually lagged behind the average for Asia's emerging markets.

Back in 2001, the *Office of the Insurance Commission* (OIC) launched the *National Insurance Masterplan*, which was revamped in 2006 and will run up to the end of 2011. One of the aims of this master plan is to give insurance companies greater financial stability and to make them more efficient and professional. Insurers are also to play more of a role in raising awareness of the need to save for retirement provision among the population at large. More stringent consumer protection standards are to be put in place to support these plans.

Today, Thais invest EUR 106 a year in life insurance products, meaning that the penetration rate has risen from 1.5% to almost 2.9% over the past decade. The *National Insurance Masterplan* , it would seem, is starting to bear fruit. A glance at insurance density/penetration, however, suggests that the country still has a long way to go before it can catch up with the world's industrialized nations. Consequently, the life insurance market is likely to continue reporting growth in the low double digits over the next 10 years, outstripping the growth in general economic output.

The market is dominated by three insurance companies, AIA, Thai Life and Muang Thai Life, who accounted for more than 53% of the market in 2010. Ayudhya Allianz CP Life was ranked sixth with a share of 6.1%. A total of 24 insurance companies are involved in the life insurance business.

Malaysia: Private pillar added to pension system

The insurance market in Malaysia is heavily concentrated, with the three largest insurance companies cornering close on 60% of the market. But in contrast to many other markets in Asia, foreign insurance companies dominate the scene with a market share of 77% (2009).

With a premium volume of just under EUR 5.8bn, Malaysia´s life insurance market is only marginally bigger than Indonesia´s but, given its lower population, Malaysia has per capita premiums of around EUR 200, well in excess of the Asian emerging market average of approximately EUR 100.

With 32% of premium income, investment-linked products, which have made a return to double-digit growth following a slump in 2008, replaced "whole life" insurance products as the most sought-after product group in 2010. Endowment insurance policies, which are often taken out as an additional component of retirement provision, have also been accounting for an increasing proportion of total premium income over the last three years. Since 2006, however, the highest average growth rates of over 25% a year have been recorded by Takaful products which now account for almost 7% of premium volumes. After a further license was created last year, there are now as many as nine Takaful providers in Malaysia, which are keen not only to serve the more than 13 million Muslims in Malaysia, but are also vying to become the “Takaful hub” in the region.

Like many other Asian and western countries, Malaysia is also grappling with the problems of an ageing society and the pressure that this is putting on the pension system. The existing funded pension system is based on what is known as the Employee Provident Fund (EPF). This a fund managed by the public sector into which employees and employers a like make a compulsory contributions totaling 11% and 12% of the employee's salary respectively. Additional voluntary contributions can also be made. Around two million self-employed Malaysians, however, are not members of this fund. The government has now decided to launch a voluntary private pillar at the end of this year, giving both the self-employed and salaried employees with sufficient financial

resources behind them an additional option for retirement provision. Therefore, the future growth perspectives remain positive.

Takaful – Sharia-compliant insurance

Estimates show 1.57bn followers of Islam worldwide – almost one quarter of the global population. Takaful is a community of insured people which shares out both risks and profits. The insurance company acts merely as an administrator. According to Sharia law, although profits are allowed, interest earnings, on the other hand, are not, with the result that many devout Muslims are unable to use conventional insurance products aimed at providing retirement provision and asset formation. In order to serve this large market, the first Sharia-compliant insurance products emerged in the early 1980s. But the real boom in Asia did not begin until 2004 in conjunction with rising oil prices and the economic upswing in Asia and the Middle East.

With Takaful life insurance products, insurance companies pay into a fund built upon Islamic principles which distributes the lion's share of profits. For instance, there are special funds which invest only in company stocks which have no connection with alcohol, pork or tobacco.

Market data on the global Takaful market are scarce. 2007 estimates assumed a figure of EUR 4.6bn, with Saudi Arabia and Malaysia the biggest markets.. Demographic developments in the Asian countries, rising incomes, greater individual awareness of the need to put more aside for retirement and the growing range of Sharia-compliant banking and insurance products will, however, fuel demand considerably over the next few years.

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