Growth expected, but challenges await

Philippine Life Insurance Association (PLIA) president **Benedict Sison** talks about some of the trends and regulatory changes facing the country's life insurance industry.

Decreasing volatility from single premiums

The predominance of single premiums (SP) in its past production performance has contributed to the industry's vulnerability to market disruptions and difficulty in producing growth when the investment environment falters. Recent indications, however, show a favourable shift away from SP toward increased regular premium plans.

Chart 1

Variable unit-linked share to total premium

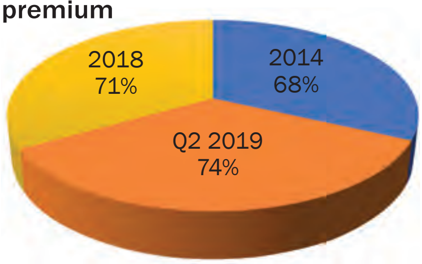
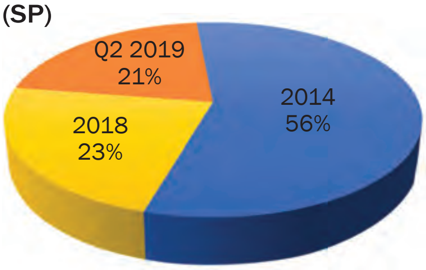


Chart 2

Declining share of single premiums (SP)



In the last five years there has been a continuing significant share of variable unit-linked (VUL) to total premium, being at 68% in 2014 then increasing to 71% in 2018 and at 74% as of 1Q2019 (see Chart 1).

The increasing trend in VUL share is accompanied by a similarly improved contribution of regular premium plans, as single premium share in the mix continued to contract from 56% in 2014 to 23% in 2018 and 21% as of first half 2019 (see Chart 2). This augurs well for the industry's growth sustainability as it means more renewing future premiums.

Increasing contribution of bancassurance

Now having a share of 34% of total premiums, the bancassurance channel is continuing to develop into a significant source of growth for the industry (see Chart 3).

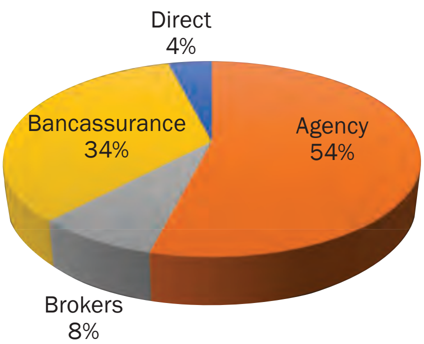
Of the 30 life insurance companies operating, 12 are now engaged in bancassurance arrangements. Of the 2018 top 15 universal and commercial banks, nine are engaged in bancassurance arrangements with life insurance companies.

Financial framework strengthening

As we continue to push for growth, the industry has been pursuing the strengthening of its financial operating environment. In 2017, the industry shifted from reserve valuation to the gross premium valuation method and adopted an RBC2 framework. This is a supplemental capital adequacy mechanism to the

Chart 3

2018 distribution channel mix



mandatory staggered increase in the minimum net worth requirements.

The last two tranches for the minimum net worth progression schedule mandated under the amended Insurance Code was an increase to PHP900m ($17.7m) by end 2019, and to PHP1.3bn as final build-up by end 2022.

The industry is also now in the thick of preparations for the shift to IFRS17 insurance contract reporting standards by 1 January 2023, the local implementation deadline set forth by the Insurance Commission (IC) which is an extension by one year from the international cutoff date.

Regulatory challenges

Life insurance companies are contending with a number of regulatory challenges across various fronts that are expected to create significant disruption in their operating landscape if not successfully fended off or managed.

1 Pending bill on collective investment schemes (CIS) law in Congress

Under this bill, the separate variable account of a VUL product will be classified as a collective investment scheme along with unit investment trust funds and mutual funds. This will split regulation of the insurance and investment components of a VUL between the IC and the Securities and Exchange Commission (SEC), respectively. The SEC will become the sole regulator of all CIS after three years of capacity building from the bill's approval into law.

2 PLIA court case vs the Credit Information Corporation (CIC)

The CIC is a 'government-owned and controlled corporation created to be the leading provider of independent, reliable and accurate credit information'. In a circular, the CIC mandated insurance companies to report policy loans, insurance premiums and insurance contract as being credit data that reflect on the creditworthiness of policyholders. Failing to convince the CIC, despite several dialogues, of the industry's contrary position and argument that this requirement runs counter to the Data Privacy Act, PLIA decided to bring the issue up to the court. A favourable ruling was issued to PLIA in February 2019. The case is awaiting the court decision on CIC's motion for reconsideration.

3 IFRS17 implementation

Local implementation was extended by the IC to 1 January 2023. Associated transitioning costs to IFRS17 are overlapping with financial pressure on smaller companies to meet the scheduled minimum capitalisation build-up to 2022. A number of smaller companies still have not started on transition preparations when, ideally, they should already have completed gap analysis by now to be in alignment with the 2023 implementation.

4 Mandatory minimum capitalisation build up

The industry trusts that when the final 2019 data on net worth is released, the five companies in a vulnerable position based on mid-2019 figures would have successfully passed the PHP900m hurdle; and with a three-year window to work with to lift their net worth to the PHP1.3bn level, the 13 companies still with shortages are expected to become compliant by then.

The PHP1.3bn end-state minimum net worth requirement appears significantly disproportional when the premium volume of the Philippines is compared with the more developed ASEAN markets, as illustrated below:

Country	Ratio of Philippines' premium to country's premium volume	Minimum capitalisation Philippines' required 2022 level vs country's minimum capital requirement
Indonesia	21%	2.4x
Malaysia	26%	1.0X
Singapore	14%	3.5x
Thailand	16%	1.5x

Against these four countries, the relative premium volume of the Philippines reaches only a range of 14%-26% of any one country's and yet its target capitalisation would run up to 1.0 to 3.5 times of these countries.

5 Controversial Supreme Court decision on contestability of a life insurance policy

The subject claim involves death within two years from issuance of the policy, wherein there was concealment of an adverse medical history that became the grounds for claim denial.

The court ruled the claim payable, that "the death of the insured within the two-year period will render the right of the insurer to rescind the policy nugatory. As such, the incontestability period will now set in". The case is still on second motion for reconsideration status. If this decision becomes final, the industry will have increased exposure to fraud risks.

Industry outlook

Depending on how the ongoing regulatory challenges play out, the industry may have to go through 2020 with a greater degree of challenge, with the risks associated with the CIS bill being the single most potentially prejudicial to the market.

If the CIS bill gets passed into law, the ensuing dual regulation complications from the IC regulating the protection component of the VUL product and the SEC regulating its investment component will unduly impact policyholders, the sales force and the insurers all together.

It is hoped that amid this unfavourable outlook, the projected recovery in the country's economic growth prospects beginning 2020 will become a balancing factor. The World Bank, in its Philippines Economic Update October 2019, declared as follows:

"The Philippines' growth outlook is weakened by a difficult external environment and domestic challenges, as growth is expected to slow from 6.2% in 2018 to 5.8% in 2019, before recovering to 6.1% in 2020 and 6.2% in 2021. Both fiscal and monetary policy remain supportive of growth, while a weak global economic environment and a slow recovery in public investments constitute the main downside risks."

With a positive market outlook for VULs from the expected growth improvement in 2020, the industry would be in a better position to manage adjustments that may be required from the possible passing into law of the CIS bill.