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Islamic Insurance: Not a Question of Faith

Insurance in conformity with Islamic law has existed for hundreds of years. Now its comeback could help Southeast Asia better deal with natural disasters and catastrophes.



Employees of Sham bank, a newly opened Islamic bank, stand in front of an ATM machine at the bank's headquarters in Damascus in August 2007. Islamic finance and insurance is growing at double digit rates (Photo: Reuters)

In December 2004, a massive earthquake in the Indian Ocean triggered tsunamis that devastated coastal regions of many countries in the region. Over 300,000 people were killed or were reported missing, and economic losses reached between 13 and 14 billion dollars, according to Munich Re and Swiss Re. Only between 2.5 and 4 billion dollars of this damage was insured.

Billions of dollars worth of property was simply lost, because many small businesses were not insured or did not have adequate coverage. One of the countries hardest hit by the tsunami was Indonesia. Only 6 million of Indonesia's 240 million people have individual life insurance policies.

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That means that only around 2.5 percent of Southeast Asia's most populous country is covered. According to Rianto Djojosingito of Allianz Indonesia, poverty is the main reason for this sparse coverage, but the situation is aggravated by a lack of information.

"In general, people in the cities know about insurance products, but if you go to the villages, people don't know enough; they just don't know about insurance," says Djojosingito.

A lack of knowledge is reinforced by distrust, especially among Muslims. Insurance, in its conventional, Western form, is forbidden by Sharia law. Islamic scholars say it resembles gambling, and includes interest rates,

which are shunned by the Koran.

Still, Muslims have known something similar to insurance for hundreds of years. Over time, Islamic scholars developed an elaborate system of insurance in conformity with Islamic law, also known as Takaful. While conventional insurers charge money to cover the risks of the insured, Takaful policies spread the risk and eventual rewards among all participants, creating a system of mutual insurance.

"It is basically a different way of risk transfer," says Djojosingito. "With the Takaful approach, the insurance company is becoming more like a facilitator and administrator for this risk sharing."

Premiums from Islamic insurance may also not be invested in sectors such as gambling, pornography, and alcohol. Whether or not an insurance product really conforms to Sharia Law differs from country to country, explains Martin Hintz, responsible for Islamic Microinsurance at Allianz Indonesia.

"The interpretation of what Sharia principles and Takaful really are varies a bit from country to country," says Hintz. "So, an approval from the Sharia Supervisory Board in Indonesia is only valid for Indonesia."

Growth from Bahrain to Britain

Despite the vagueness, Islamic insurance is growing by over 15 percent annually, with premiums reaching up to 4 billion dollars, estimates the consultancy Oliver Wyman. Malaysia has been at the forefront of the business, but Takaful has spread to almost every Arab and Far Eastern country. Solidarity, the world's largest Takaful provider based in Bahrain, even expects massive growth in Western countries with growing Muslim populations.

Indonesia, however, has lagged behind. Takaful insurers in Malaysia, a country of only 27 million, hold assets worth some 2 billion dollars. Their counterparts in Indonesia, with nearly ten times the population, only manage assets worth 95 million dollars. In 2003, Indonesians spent only about eight dollars per capita on non-life insurance. Measured in terms of GDP, Indonesia had an insurance penetration rate of 0.83 percent for non-life business compared to over 15 percent in the United Kingdom.

Ethics beyond creed

While this will not change overnight, Hintz believes that Sharia insurance could help overcome some Indonesian reservations about insurance. "Takaful will not be the panacea for low insurance penetration in Indonesia," he says. "But about five percent of the financial market, especially the microfinance market, is now done on a Sharia basis. Now with the Sharia insurance and Sharia microinsurance, we can service this five percent, which is also growing steadily. So yes, it will help."

Once an insurance product is deemed to be in conformity with Islamic law, it can also be sold by non-Muslims, says Kiswati Soeryoko, who is responsible for Sharia products at Allianz Indonesia. "The buyers of Takaful products are also not always Muslims," says Soeryoko.

"They see that the results of the investments are good, and that it is not involved with gambling, alcohol, and interest, and so they feel comfortable with these principles." Weighing the risks, it seems, is not entirely a question of faith.

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