Exclusive Interview

Habib Insurance

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Syed Ather Abbas

Chief Executive Officer

Habib Insurance Co. Limited

ICMA: Please briefly highlight the contribution of the insurance sector toward economic development?

Ather Abbas: In recent decades, the insurance sector saw a consistent improvement in terms of structure and growth. Macroeconomic stability and high economic growth played a vital role in this regard. Specifically, higher per capita income, expansion in the trade sector, and the growing private sector credit spurred exceptional growth in the insurance sector. Importantly, this growth was broad-based, as both the life and non-life insurance sectors witnessed double-digit growth although the life insurance sector continues to dominate the insurance industry.

The insurance industry in Pakistan is relatively small compared to its peers in the region. The insurance penetration and density remained very modest as compared to other jurisdictions while the insurance sector remained underdeveloped relative to its potential. The Pakistani insurance market has undergone major structural changes in the last few years through mergers of companies to meet the increased statutory requirement of minimum paid-up capital as per Insurance Ordinance 2000.

ICMA: What types of risks are faced by an insurance company and how these risks are managed by the Boards?

Ather Abbas: Risks faced by insurance companies are quite numerous to mention. The important activities of an insurance company are Underwriting and Investment. The risk involved in these two activities can shake the foundation of the company and when combined with other risks, it accelerates or accentuates deterioration and even demise of the company. Credit Risk is inherent in lending and investment. It can also be caused by reinsurers, brokers, agents, and clients. Market Risk is the risk that arises from market movements and volatility of prices of equity or currency and changes in interest rates in the deals including derivative contracts. Liquidity risk in life insurance arises out of the surrender of a large number of policies and in general insurance due to non-renewal of the policies and/or large claims. Actuarial risk arises in pricing (premium rate) due to variance in mortality rate, perils, hazards, etc. projected with actual position, (say early termination of the policies, catastrophe, etc.)

Asset Liability Management risk does not imply that assets should be matched as closely as possible to liabilities but the mismatch shall be effectively managed to contain the damages if any arising therefrom. The operational risks in insurance include human failure, fraud, technology failure, and failed systems and procedures. Violation of environmental laws and regulations. The risks may be systemic risks or un-systemic risks. Systemic risk is industry-wide, market-wide, or even countrywide, like, as recession, high inflation, civil disorder and chaos, war, etc. Un-systemic risk is a company-specific management failure, huge fraud, etc. Another important risk is an asset-liability mismatch.

The cost of defending your enterprise against the above-mentioned risks is not child's play. Insurers have to do diligent research and study and also have to reinforce their own systems and resources to remain resilient and ensure adequate protection against these risks.

ICMA: The claim ratio of the general insurance business is quite high. What are the reasons?

Ather Abbas: General insurance companies have a high loss ratio because most of the insured properties, at times, experience devastating events like floods, cyclones, or hailstorms. In such situations, these ratios surpass the 100% mark, and the companies pay much higher than the premium they collected in that period. There is fierce competition with so many insurance companies operating in the market due to which client leverages on gaining substantial discount so the risk pricing at times isn't adequate resulting in higher combined operating ratios of the general insurance segment.

ICMA: What are the key elements of an effective risk management strategy, especially in an insurance company?

Ather Abbas: Risk management is the identification, assessment, and prioritization of risks and the subsequent coordinated and economical application of resources to minimize, monitor, and control the probability and impact of losses. Effective risk management activities create value and should be an integral part of the decision-making process. It has four key elements that are tied together in a Risk Management Plan viz. Risk Identification; Risk Assessment; Risk Action Management; and Risk Reporting and Monitoring.

Risk management strategy in insurance includes the following:

- Alignment of the pricing market strategy and reinsurance arrangements to the organization's risk appetite as well as optimizing the goals of the organization
- Assist clients to recognize risk events and changes to claim rates earlier, to move towards a more market responsive, risk-based pricing approach which ensures the efficient deployment of capital and a reduction in extreme risk event losses.
- Enhance the feedback mechanism from claims function to underwriting and product development processes to improve the performance and profitability of these processes.

ICMA: How do you make assessments of risks in various segments of insurance contracts?

Ather Abbas: An insurance contract has various business class-wise segments. The assessment begins with COPE analysis which is the type of construction, occupancy of the premises, and protection against potential hazards and Exposures. Based on the above, the underwriters determine the optimum pricing of the risk and extent of participation. Often the risks are potentially high exposures and/or having hazardous occupancies are often underwritten on either a coinsurance basis or ceded out through facultative reinsurance arrangement.

ICMA: What is the role of underwriting and reinsurance cover in mitigating the risks of insurers?

Ather Abbas: The insurance underwriter analyzes and assesses the risks in providing insurance to individuals and companies, and establishes the pricing of the insurance premium. Underwriters use software, data from actuaries, and statistical analysis to evaluate the risk of a future event that would require the insurance company to compensate an insured.

Keeping in view the size and nature of the risk and the underwriter's want to potentially underwrite, he may seek reinsurance help to decrease risk. When an insurance company singularly ensures a large number of clients and their property, they take on a huge amount of risk. Reinsurance is a great strategy to reduce that risk, placing some of the burdens on a reinsurance company instead of shouldering the burden completely alone.

ICMA: Do you think a diversified portfolio of investments is the best strategy for mitigating credit risk?

Ather Abbas: Yes, portfolio diversification is the risk management strategy of combining different securities to reduce the overall investment portfolio risk. It can help mitigate risk and volatility by spreading potential price swings in either direction across different assets. Correlation is a key variable in portfolio diversification. A well-diversified portfolio will reduce its volatility because not all investments move together. Therefore, holding a variety of low or no correlation assets can reduce unsystematic risk.

ICMA: Are Pakistani insurance companies investing in risk management technology and data analytics? Do you think that adoption of technology can help in improving risk assessment in insurance companies?

Syed Ather Abbas, Chief Executive Officer, Habib Insurance Co. Limited is receiving shield from Mr. Aamir Ijaz Khan, Executive Director ICMA

Ather Abbas: With the rise of new risks, the use of data analytics and other advanced technologies have become more important than ever. Incorporating data analytics in risk management is key. The risk management approach must embed technologies across the entire risk management process, starting from identification to assessment to mitigation to monitoring. Each step of the process presents a great opportunity for leveraging the power of analytics.

Insurance companies in Pakistan are not directly investing in technologies for risk management but rather relying more on the expertise and systems of various consultancy providers for their assessment. I strongly advocate direct investment by the insurance companies in this segment so that they can have hands-on knowledge of the real-time risk management data available in their databases.

ICMA: Can we insure agricultural crops in Pakistan?

Ather Abbas: Crop Insurance is a vital part of the Pakistan agricultural industry and a key risk management tool for the modern farmer. The Crop Insurance Company agrees to indemnify the insured (farmer or grower) against losses that occur during the crop year. Losses must be due to perils that are unavoidable or beyond the insured's control such as drought, flood, and disease. Keeping in view recent floods which have affected over 2 million acres of agricultural land, I personally feel that there is a strong need at the state level to make crop insurance mandatory in Pakistan. Though state banks in collaboration with insurance companies have already introduced loan-based schemes which are insured to protect the interest of the farmers the sector still needs the involvement of the state to take up this matter on a national level.

ICMA: Do our insurance companies have adequate re-insurance arrangements with international insurers to make payments on flood-related claims of recent massive floods in the country?

Ather Abbas: Indeed, all major market players have separate arrangements in their reinsurance treaties to cover catastrophic events like floods, earthquake the adequacy of which is established based on historic data. Keeping in view recent major floods which have majorly affected rural areas of Sindh and Baluchistan which has quite negligible insurance penetration hence the initial assessment of insured losses in these areas is quite trivial.

*The Editorial Board thanks **Syed Ather Abbas, Chief Executive Officer, Habib Insurance Co. Limited** for giving his exclusive interview for Chartered Management Accountant Journal.*