



THE LIBERALISATION OF MOTOR INSURANCE IN MALAYSIA

NICHOLAS ACTUARIAL SOLUTIONS

MAY 2017

SUCCINCT WHITE PAPER 003

This white paper sets out our views of how the motor insurance market in Malaysia will develop as it progresses towards a fully liberalised and competitive market. This is a succinct, conceptual summary. We welcome discussions and collaborations.

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INTRODUCTION

In the past, motor insurance products are standardised, and motor insurance premiums are calculated according to a rather arbitrary formula, that has little regards to consumers' price elasticity of demand nor the risk profile of the car or the driver. This is an inefficient market and unfair to both consumers and insurance companies.

WHAT IS LIKELY TO HAPPEN?

Two market segments shall emerge. With insurance renewal an annual event, it will take some time for the average consumers to realise that they could get a bigger bang for their buck by shopping around. Insurance companies will benefit from this segment of price-insensitive consumers and would maintain or increase prices to maximise profits. On the other hand, the segment of price-sensitive consumers will be bargain hunting from day one. A price war between insurance companies will ensue. Two profound humps will emerge at either end of the price elasticity curve. Over time, there will be more price sensitive customers, with increasing awareness, facilitated by technology such as online purchases and aggregator websites. Nonetheless, **we believe price insensitive consumers will remain the larger of the two segments** as consumers are sticky to their insurance agents, and the price differential between two motor insurance products will not be too significant.

Product differentiation for the price sensitive segment. Insurance companies need to attract price sensitive segment as market share is critical in an insurance market which profitability levels are high and economies of scale are in abundance. However, **price leadership by itself is not sustainable, as predatory pricing will become rampant.** Product differentiation through distinct rating factors or a usage-based insurance programme will cherry pick good risks, aligning demand and supply at this end of the elasticity curve, whilst erecting a weak entry barrier.

Demand-based pricing not risk-based pricing. Whilst it is a necessity for insurance companies to quantify the risks they underwrite, relying solely on **risk-based pricing is likely to lead to a double whammy** – loss of profits from the price insensitive segment and loss in business volume from the price sensitive segment. Prices need to be aligned to consumers' demand and price elasticity, utilising a combination of demand-based pricing model and common business sense.

Winners and losers. Strategically astute insurance companies stand to benefit. Others will make costly mistakes and fail. Likewise, savvy consumers will benefit whilst the less savvy consumers will be exploited.

BACKGROUND

"The liberalization of motor insurance in Malaysia" is our third issue of succinct white paper. Our objective of issuing succinct white papers is to enable our thought leadership to reach a wider audience, and make a larger positive impact. Our white papers are publicly available and we do not claim any proprietary intellectual property on the contents.

The impending liberalization of the motor insurance market in Malaysia brings about uncertainty for the insurance companies as well as the consumers. This paper sets out what we believe to be the most likely scenario.

ABOUT US

Nicholas Actuarial Solutions is founded as a platform to collaborate with like-minded businesses and individuals to make a difference. Our interests are wide and varied, with our core focus being the actuarial field.

Our mission is to develop and implement novel and cutting edge solutions to make our clients more successful.

It is our vision to achieve global recognition of our thought leadership and innovative solutions in the actuarial field.

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