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Market Segment Outlook: Indonesia Non-Life Insurance

The outlook improves from Negative to Stable owing to economic resilience, growing demand for motor insurance, favourable investment income, and ongoing regulatory improvements

AM Best has revised its outlook for Indonesia's non-life insurance segment from Negative to Stable. Supporting factors include:

- Economic resilience is driving robust growth prospects across key lines of business.
- Motor insurance demand is expected to benefit from a proposed design to make motor third-party liability insurance compulsory.
- While transitional challenges remain, ongoing regulatory changes are expected to enhance the non-life sector's long-term financial stability.
- Favourable investment income is supported by high domestic interest rates.

Moderating factors include:

- Underwriting conditions in core business segments remain under pressure, despite implementation of remedial measures.
- Pricing risk is elevated owing to the rapid growth of the electric vehicle (EV) market, possibly mitigated by future pricing differentiation between EVs and non-EVs.

Robust Growth Prospects amid Economic Resilience

Indonesia's non-life insurance segment reported robust top-line results in the first quarter of 2024, continuing the growth momentum from 2023. Key drivers include property, credit, health, and motor insurance.

Indonesia's economy grew by 5% in 2023 and is likely to remain robust over the near term, supported by steady domestic demand, rising business investment, and fiscal spending. Indonesia's investment climate is also expected to remain favourable as the government maintains policies aimed at attracting foreign direct investments.

In line with the government's "Golden Vision 2045" to transform the economy, strategic plans for infrastructure development, including the establishment of a new capital city, modernisation of existing infrastructure, and an increase in renewable energy production, are expected to drive higher demand for commercial insurance over time.

Proposed Mandatory TPL Insurance to Boost Motor Insurance Demand

A regulatory proposal to make motor third-party liability (TPL) insurance compulsory is expected to bolster demand. Motor TPL insurance is currently bought on a voluntary basis. Given the regulatory push to implement the policy in 2025, motor insurance demand is expected to grow significantly over the medium term and help narrow the country's insurance protection gap. While aimed at alleviating policyholders' financial burdens, successful implementation will

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require effective product design, robust risk management, and adequate pricing strategies to mitigate potential underwriting challenges.

Regulatory Changes Expected to Enhance Financial Resilience over Time

At the close of 2023, the Financial Services Authority (Otoritas Jasa Keuangan, OJK) issued OJK Regulation Number 23 of 2023, implementing a two-phase increase in minimum capital requirements for non-life insurers. By year-end 2026, non-life insurers must meet a minimum equity requirement of IDR 250 billion (USD 16.1 million). By year-end 2028, the minimum requirement will increase to either IDR 500 billion or IDR 1 trillion, subject to various conditions. While the implementation specifics are being clarified, the planned increase in insurers' capital bases is expected to bolster the industry's financial resilience in the long term, despite medium-term challenges.

Additionally, OJK Regulation Number 20 of 2023 aims to enhance the governance and risk management of credit insurance. Key changes include mandatory risk sharing between financial institutions and insurers, revised policy coverage periods, acquisition costs, and underwriting data disclosure requirements. These measures are expected to improve pricing adequacy, promote informed underwriting, and reduce adverse risk selection against insurers. This regulatory change addresses pandemic-era credit insurance losses attributed to poor economic conditions and, more importantly, inadequate underwriting risk management, aiming to mitigate future risks in similar financial scenarios.

Favourable Investment Income Supported by High Domestic Interest Rates

Indonesian non-life insurers' investment income is expected to remain favourable over the near term, supported by high domestic interest rates. Given that term deposits and fixed-income instruments constitute the majority of the segment's investments, the favourable interest rate conditions are expected to benefit the overall earnings as non-life companies reinvest their assets into higher yielding fixed-income instruments upon maturity.

While domestic monetary policies may ease prospectively, the trend will be influenced by various factors, including the domestic inflation rate, global monetary policy, and wider macroeconomic conditions.

Underwriting Conditions in Key Business Lines Remain Under Pressure

Headwinds remain for core business lines, including property, health, and credit insurance. For property and engineering lines, companies face higher reinsurance costs from the tight reinsurance market conditions locally. More restrictive terms and reductions in reinsurance commissions are likely to weigh on the underwriting performance. Additionally, health insurance claims have been adversely impacted by high medical inflation, driven by rising medical costs and increased claims frequency. Although insurers have implemented remedial measures, including pricing adjustments, performance volatility may persist over the near term.

Credit insurance loss experience may further deteriorate over the medium term, given the uncertainty around claim reserve adequacy for this long-duration line of business. Paid loss experience has continued to show adverse development in recent periods, driven by an increase in non-performing loans, with the losses likely stemming from older policies. Future reserve strengthening remains probable, though likely to be less significant given the time elapsed since the pandemic.

Increased Pricing Risk for EVs amid Growing Adoption

Pricing risk for EVs is growing given the increasing prevalence of EVs in Indonesia. Whilst currently a small percentage of the overall motor vehicle market, the number of EVs in Indonesia is increasing, supported by government incentives that promote their use. At present, EVs are subject to the same motor insurance tariff rates as internal combustion engine vehicles. However, this approach inevitably leads to high pricing risk due to potential mismatches in the underlying risk profiles of EVs compared with non-EVs, relative to the premiums charged. Regulatory refinements currently under consideration may alleviate pricing risk over the near term by introducing pricing differentiation between EVs and non-EVs.

GUIDE TO BEST'S MARKET SEGMENT OUTLOOKS

Our market segment outlooks examine the impact of current trends on companies operating in particular segments of the insurance industry over the next 12 months. Typical factors we would consider include current and forecast economic conditions; the regulatory environment and potential changes; emerging product developments; and competitive issues that could impact the success of these companies.

A Best's Market Segment Outlook can be Positive, Negative, or Stable.

Best's Market Segment Outlook	
Positive	A Positive market segment outlook indicates that AM Best expects market trends to have a positive influence on companies operating in the market over the next 12 months. However, a Positive outlook for a particular market segment does not mean that the outlook for all the companies operating in that market segment will be Positive.
Negative	A Negative market segment outlook indicates that AM Best expects market trends to have a negative influence on companies operating in the market over the next 12 months. However, a Negative outlook for a particular market segment does not mean that the outlook for all the companies operating in that market segment will be Negative.
Stable	A Stable market segment outlook indicates that AM Best expects market trends to have a neutral influence on companies operating in that market segment over the next 12 months.

We update our market segment outlooks annually but may revisit them at any time during the year if regulatory, financial, or market conditions warrant.

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BEST'S MARKET SEGMENT REPORT

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