

# The Tendency to Subscribe Takaful: A Proposed Conceptual Framework

Mohd Farid Asraf Md Hashim<sup>1</sup>, Mohamad Naim Abd Halim<sup>2</sup>

<sup>1</sup>Tunku Puteri Intan Safinaz School of Accountancy, Universiti Utara Malaysia, Malaysia

<sup>2</sup>Islamic Business School, Universiti Utara Malaysia, Malaysia

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## Abstract

Takaful market is expected to become one the important aspects that contribute to Malaysian economic growth and social development. Despite many forms of incentives provided by the government to inculcate its demand, it is undeniable that the level of penetration by Takaful providers is still relatively low. It is recorded that the growth of the market penetration for the past ten years (2005-2014) is no more than 15%. The available literatures have shown that the issue of awareness and misconception of Takaful are among the reasons that might have hindered the progression of Takaful. Thus, the main purpose of this study is to discuss the plausible factors that influence the tendency to subscribe with the Islamic Insurance (Takaful). A conceptual framework consists of three factors namely the demographic factors, awareness and knowledge, and performance of Takaful operators is proposed. This article contributes to both the body of knowledge and practice by offering insights on the factors that may affect the demand for Takaful especially from the perspective of developing nation, Malaysia.

**Keywords:** *Takaful, Insurance, Islamic Insurance, Islamic, Malaysia.*

## 1. Introduction

Generally thought as an Islamic insurance, Takaful is based on the concept of responsibility and mutual cooperation among participants. In Takaful system, participants make voluntary contributions (Tabarru') to a fund (participants' fund), which in turn provides financial aid to those that suffer a loss. The Islamic Insurance Company of Sudan, established in 1979 and BEST Re, launched in Tunisia in 1985 are among the earliest Takaful and retakaful operators in the world.

According to Ernst & Young Global Takaful Insights 2014, global gross Takaful contributions (excluding Iran) grew at a compounded annual growth rate (CAGR) of 22% for the period of 2007 to 2011 and 14% over the period of 2012-2014. Saudi Arabia and South-East Asia (including Malaysia) dominate the global Takaful market with gross Takaful contributions of US\$6.8 billion and US\$4.24 billion respectively in 2014. By the year 2017, it is expected that the global Takaful industry may reach over US\$20 billion, with the major markets contributed by the Gulf Cooperation Countries, Malaysia and Indonesia.

Although the global Takaful industry is making good progress in terms of acceptance and outpacing the growth of conventional insurance, its untapped potential market remains

enormous.<sup>1</sup> Despite Muslims constituting approximately a quarter of the global population, Takaful contributions account for less than a percent of total insurance premiums. As noted above, insurance industry registered marginal growth despite challenges in the competitive environment and close rivals of Takaful companies. Even the insurance landscape has shown the development of more Takaful-related products and extensive promotion, Takaful penetration manages to achieve only seven percent compared to 40 percent by traditional insurance in the past decade (MHB Annual report, 2008).

From the Malaysian perspective, conventional insurance is still in their dominant position which accounted around 89% from conventional net premiums and Takaful net contributions combined in the year 2009 (Ernst & Young, 2015). Despite the economic and financial setting have experienced transformation in the last decade, the insurance industry continues to sustain strong performance amidst challenges in a competitive environment. The conventional net premiums in Malaysia reported at RM29.2 billion in 2009 while the Takaful net contribution is at RM3.5 billion for the same period (Ernst & Young, 2015). However, Takaful industry in Malaysia is still low as compared to the conventional insurance industry. The family Takaful manages to climb RM2.7 billion in 2009 while the general Takaful net contributions reached RM0.8 billion (Ernst & Young, 2015).

The first Takaful company known as Syarikat Takaful Malaysia was established in 1984 and the Takaful industry is supported by its standalone act which is known as Takaful Act 1984. Even though that the Takaful business has been introduced in Malaysia for more than two decades, the penetration rate of Takaful sector (family Takaful) remains low with only 14.5% in the year 2014 (Ernst & Young, 2015). Obviously, this amount is relatively insignificant due to fact that the majority of Malaysian populations are Muslim. It is indeed that the penetration of family Takaful market is rather way behind if compared to the conventional life insurance which stands at 41.2% for the year 2014. It is shown that the total net contribution income of Takaful for the year 2014 is RM6.3 billion, while the conventional insurance had successfully obtained net premiums of RM42.5 billion (Ernst & Young, 2015). Nevertheless, opportunities do not come by a flick of a finger. A number of crucial issues have to be addressed to ensure credibility and acceptability for a brighter future of Takaful.

For this reason, Takaful providers should be wise in positioning themselves in term of product design that can satisfy the needs of the market and respond well to the other mitigating factors that might reduce the tendency of potential Takaful subscribers.

Furthermore, the awareness on the Takaful related product that is still low in Malaysia ("Takaful penetration rate still low at 5.2%," 2017) should be among the paramount concern by the Takaful provider. Besides, there is a perception that Takaful is similar to the conventional

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<sup>1</sup>Based on the report by Ernst & Young (2014), the global gross Takaful contribution for the year 2014 is USD14.029 billion. Statista (2017) reported that the global gross insurance premiums for the year 2014 stand at USD4.75 trillion.

insurance. In fact, many of Malaysian has little knowledge on how the Takaful works (Ernst & Young, 2015).

The above-given background has triggered the need for further investigation on the contributing factors that might influence the tendency to subscribe Takaful plan or products. As the low market penetration signifies that there is a potential for growth, it is indeed essential for the Takaful operators to respond to the volatile and uncertain business environment in ensuring the sustainability of the expansion of Takaful industry in Malaysia. Thus, this paper proposes a conceptual framework for the plausible relationship between demographics factors, awareness and knowledge of Takaful, the performance of Takaful operators and the tendency to subscribe Takaful.

## 2. Literature Review

In 1985, the Islamic Fiqh Academy of Organization of Islamic Conference 1985 in Jeddah, Saudi Arabia has resolved that conventional insurance is Haram (prohibited) and cooperative insurance (Takaful) is permissible and fully aligned with Shariah principles. Takaful provides risk protection in accordance to Shariah by applying the principles of Ta’awun (mutual assistance), charity, brotherhood, piety and prohibits elements such as *Gharar* (uncertainty) and *Riba’* (usury/ interest). In fact, in June 1972, the National Fatwa Committee of the Malaysian Islamic Affairs Council declared that conventional life insurance is contradicted with Islamic principles.

While Takaful has continued to evolve, several misconceptions about Takaful have becoming big challenges for the Takaful industry due to the lack of knowledge and awareness on the insurance and Takaful operation itself. Some of the misconceptions are listed in figure 1 as follow (Bank Al Jazira Takaful Taawani, 2001).

<b>MISCONCEPTIONS</b>	
1.	Risk Protection (insurance) is not aligned with the concept of Taawakkul which is the total dependence upon Allah SWT.
2.	Risk protection (insurance) is Haram and prohibited.
3.	All insurance is forbidden in Islam since it is a form of gambling or wagering.
4.	All Insurance seeks to maximize profits. Thus, it will take benefits away from policyholders such as raising prices and denying claims.
5.	<i>“All Takaful operators are the Same”</i>
6.	Insurance schemes are perceived as a modern-day invention even though that social arrangement for pooling of risks has been introduced centuries ago.
7.	There is no need for Insurance or Takaful

**Source: Bank Al Jazira Takaful Taawani (2001)**

**Figure 1: Misconception of Takaful**

Nevertheless, Takaful operations provide an effective method to accumulate the savings of individuals for the collective good of the community and becoming the driver for economic growth and development by channeling its funds into Shariah approved investments. Moreover, participants may gain benefits (Hammond, Houston & Melender, 1967) as insurance will protect the beneficiaries from facing financial difficulties when there is unexpected death especially the breadwinner of the family.

However, it was found that Malaysian is still taking for granted and not fully aware on the importance of insurance coverage for their future life (“Tahap kesedaran perlindungan insurans rendah,” 2016). Besides, there are still consumers which are unable to differentiate between Takaful and conventional insurance (Ernst & Young, 2015). Perhaps, this phenomenon will not assist Takaful to grow further and less developed.

As a start of the discussion, Kumar (1995) discovered that from 6545 individuals who bought long term insurance coverage, about 1248 of the respondents refused to buy insurance when they were approached by the insurance agents. On top of that, it was indicated that demographic factors such married status and low level of education have a negative relationship with the buying decision while factors such as gender and income seem to have a positive relationship with buying decision of insurance policy. As such, the tendency to subscribe with Takaful schemes, could be linked to the black box model in the sense of buying behavior (Kotler, Ang, Leong & Tan, 1999), which include buyer’s characteristics or demographic factors (gender, marital status, educational level and income of the respondent). Reviewing the proposal by Arifin, Yazid and Husin, 2014, the comprehension on the factors that can encourage the tendency and demand for Takaful related product are vital for the Takaful operators since the market is still under-tapped. Two main factors were seen as important determinants for both conventional and Islamic insurance namely the economic and social-demographic (Curak, Dzaja & Pepur, 2013; Arifin et al., 2014).

The following chapter will focus on the propositions on the tendency to subscribe with Takaful product. For the purpose of better understanding on the plausible factors of Takaful subscription’s tendency, this study also applies the conventional insurance literature as it has been extensively discussed and debated.

### **3. Propositions**

#### **3.1 Demographic factor**

##### **3.1.1 Gender**

Women pay more for equivalent insurance coverage than men do. This is due to the reason that women between ages of 19 and 55 often use more medical services, regular checkups and more likely to visit doctors than their counterparts. However, the differences in rates for men and women are not due to the cost of maternity care (Pear, 2012). In addition, Lo, Cheung and Law (2011) discovered that women have a higher propensity to buy insurance rather than men.

This is in line with the postulation brought by Gamage and Al Huq (2016) that male household head is less likely to purchase life insurance policy than women.

From a different perspective, Lewis (1989) proposed that demands for insurance policy depend on who earns for a living in the family. Since the future of the family depends on the capability of a husband to support the family, male could be one of the potential factors of subscribing to the insurance policy. However, contrary to the above arguments, Curak et al. (2013) claimed that there is no correlation between gender and the demand for life insurance. Based on the above discussions, it is proposed that gender is a plausible determinant that may influences the tendency to subscribe Takaful.

**P1a:** There is a relationship between gender and the tendency to subscribe Takaful.

### **3.1.2 Marital Status**

Basically, insurance related to a mutual arrangement among the participating members for the purpose of risk management. Previous studies on conventional insurance found that the demand for insurance comes from married individuals when dealing with risk management. A study on Marital Status and Health Arizona Residents 2006 for instance, showed that married adults share a lower risk of mortality than unmarried individuals.

Married persons make less use of inpatient hospital care than the unmarried. Married persons are less likely to engage in risky health behaviors, including heavy drinking and smoking than unmarried counterpart. Besides, the premiums charged by insurance companies are higher for unmarried male or female drivers. Evidently, the insurance companies have taken into account on the presence of a spouse and the effects of discouraging certain unsafe behaviors such as 'drinking' and driving or speeding (Mrela, Bender & Torres, 2008). The report also indicated that unmarried males have a higher rate of uninsured for health care rather than married male. The report is somehow aligned with a study done by Kong (2010). The study confirmed that married adults have a much higher probability of having insurance rather than single or divorced adults.

Yet, the investigation by Curak et al. (2013) portrays that there is no relationship between marital status and life insurance demand. Thus, based on these considerations, marital status could be a plausible factor for customers to subscribe with any available Takaful scheme.

**P1b:** There is a relationship between marital status and the tendency to subscribe Takaful.

### **3.1.3 Educational Level**

Educational level should be considered as one of the determinant factor of Takaful demand (Remli, Muda & Rosman, 2017). Curak et al. (2013) for instance posited that there is a relationship between education level and the demand for life insurance. They argued that highly educated individuals are more familiar with risk management and this might affect the

demand for the product. In addition, the low demand for insurance in India occurred due to the low level of the education of its population (Sen, 2009).

In different vein, Akhter and Khan (2017) discovered that in South East Asia (ASEAN) and Middle East, education and Takaful demand are significantly related but in a negative direction. They also found that education is positively related to the demand for conventional insurance for both ASEAN and Middle East sample. However, Gamage and Al Huq (2016) illustrated that education level is not the deciding factor for life insurance's demand. Therefore, it's understandable that the level of education of consumer will probably give an impact to the tendency of subscribing a Takaful scheme. Thus, it is proposed that:

**P1c:** There is a relationship between educational level and the tendency to subscribe Takaful.

#### **3.1.4 Income**

In general, the likelihood that an individual has health insurance is increases with income. As postulated by Lo et al. (2011), persons with higher income are more likely to adopt risk reduction strategy such as the purchase of insurance policy. In fact, the 2004 Current Population Survey (CPS) has indicated that 12 percent of individuals in families with income between \$50,000 and \$74,999 were uninsured in 2003, while only 7 percent of individuals in families with income of \$75,000 or more were uninsured (Fronstin, 2005).

In addition, discussions by Campbell (1980), Mullis and Schnittgrund (1982) and Gamage and Ul Haq (2016) have proposed that income determines the demand for insurance policy. However, recent study from the perspective of South East Asia (ASEAN) countries suggesting that income is negatively related to the demand for Takaful (Akhter & Khan, 2017). From the above discussion, it is suggested that:

**P1d:** There is a relationship between income and the tendency to subscribe Takaful.

#### **3.2 Awareness and Knowledge on Takaful**

It is suggested that customer's awareness on the existence of a new product in the market is the first stage in the buying decision process (Schiffmann & Kenuk, 1994). Furthermore, insurance buying decision depends on the customer's knowledge on how the insurance can fulfill their needs and benefit their life (Myers, 1995). Thus, insurance providers have to build knowledge as well as to nurture awareness among potential subscribers towards their products.

From the context of the Malaysian small medium enterprises (SME), a qualitative study by Ismail et al. (2012) shows that majority of them are aware of the existence of insurance product. However, most of the respondents are not aware of the availability of Takaful product. In the other part of the world, health insurance products have been roughly for 20 years in



India but still, the penetration level is barely 2 per cent of the population. There is a low level of awareness of health insurance among the population (Sen, 2009).

By taking the idea through the discussion of literature and proposition made by Arifin et al. (2014), awareness, knowledge and understandability of Islamic financial product or service might affect the demand for Takaful. However, based on their empirical result, it seems that this notion is insignificant. Thus, by referring to the above discussions, it is proposed that:

**P2:** There is a relationship between awareness and knowledge and the tendency to subscribe Takaful.

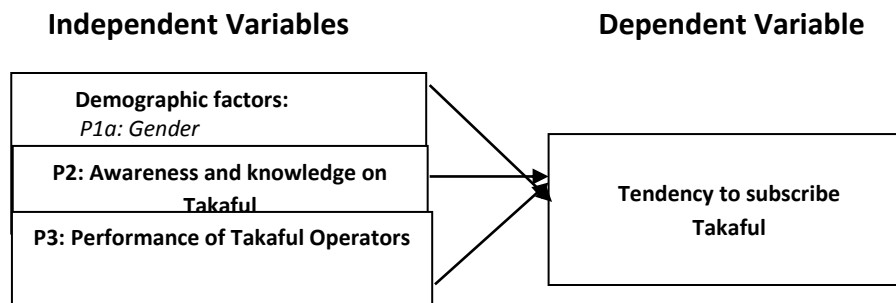
### **3.3 Performance of Takaful Operators**

Globally, insurance providers are faced with key challenges across their value chains which include customers, distributors, and workers (Karen, 2009). Thus, customers' trust and loyalty by the agents should be fostered and built. Furthermore, beside regulation and financial performance, Karen (2009) mentioned that the main concerns for insurance companies are superior customer experience, efficiency, and effective distribution management. In fact, companies' financial stability together with the service quality provided will be deliberated by customers before making a judgement in subscribing to an insurance plan (Greene, Trieschmann & Gustavson, 1992).

Additionally, insurance players as well as Takaful operators are now facing the a generation of current and potential customers which are presume to interact with the insurance providers through sophisticated and personalized online medium. Many existing and older customers are also drawn to the ease of the internet (self-service model). Thus, insurance service providers should engage and promote the online based services for sales, service, and claims to accommodate customers' demand (Karen, 2009). Fair and fast action in processing the claims and the willingness to give consultation when needed, influences the public perception (Dorfman, 1992) towards the insurance provider. Not limited to the above arguments, reputation and image of the takaful providers do positively influence the demand for Takaful (Arifin et al., 2014). On top of that, Halim, Hashim and Ali (2013) suggested that there is a positive correlation between Takaful providers' performance and the tendency to subscribe with Takaful. Thus, from the previous literature, it is suggested that:

**P3:** There is a relationship between Takaful operators' performance and the tendency to subscribe Takaful.

Based on the pertinent literature discussed earlier, a conceptual framework for the determinants of the tendency to subscribe with Takaful is proposed as follows:



**Figure 2: Conceptual Framework**

#### **4. Conclusion**

Takaful market penetration rate in Malaysia is still below market potential and way behind if compared to its counterpart, the conventional insurance. Few issues that contribute to this phenomenon such as the low level of awareness and the misconception on the importance of risk protection by the public should be taken seriously into consideration by the Takaful operators. Thus, this paper proposes a conceptual framework which composed of three plausible factors that might influence the tendency to subscribe with Takaful. The factors include demographic factors, awareness and knowledge on Takaful and Takaful operators' performance. Even though these variables have been tested in conventional insurance related studies, it is worth to revisit these factors together with the latest data available, especially from the context of Takaful and developing nation. Additionally, this article enriches the literature of Takaful as well as providing insight for the decision makers to formulate appropriate strategies to increase the demand for Takaful products.

#### **Corresponding Author**

Mohd Farid Asraf Md Hashim

Lecturer

Tunku Puteri Intan Safinaz School of Accountancy,

Universiti Utara Malaysia, 06010, Sintok,

Kedah Darul Aman, Malaysia.

Email: hasfar80@gmail.com

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