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Sector
Note

15 Jul 2022

Insurance

NON-RATED

New insurance law 2022

Congress passed the new Insurance law 2022 on June 16th 2022. The draft of this new law was first introduced around February 2021 (refer here). After receiving feedback from experts at many meetings, the Law was approved with the rate of 94.18%. The effective date will be January 1st, 2023.

In general, the new law retains the same ideas and spirit as the proposed draft, adding some clarifications and changes which are positive for sustainable development and long-term industry outlook.

Foreign ownership can be up to 100%

The new law stipulates the percentage of foreign investors' ownership is up to 100% of charter capital in insurance or reinsurance enterprises. The unlimited ownership of foreign capital will certainly attract the attention of foreign investors. Then, the competition will increase and be the driver of industry growth. We expect more participation of foreign players, especially in the non-life segment.

Applying risk-based capital (RBC)

The addition of capital management based on risk groups helps accurately reflect the risk size that the insurers own. This point can improve financial safety and prevent major risks. But, it will require insurers to uplift their capital to be able to keep receiving more contracts or bigger risks. At the same time, risk-based capital also relieves the pressure of small and medium insurers to maintain capital up to regulated thresholds. For customers, insurance premiums can be more competitive when insurers' investment resources are expanded.

More freedom in investment choices

The investment regulation in new law changes the basis from an allowable list to a restricted one. As a result, insurers will be able to diversify their portfolios including financial instruments with higher profitability than current options.

New law impacts on insurance market

We see a positive outlook for the insurance industry in the medium and long term. In the short term, the insurance market is still developing well, the insurance premium growth rate is as similar as in previous years and faster than other countries in the region. The medium-term will expect to see M&A deals, and strategic cooperation from foreign insurers, reinsurers, or foreign insurance ancillary organizations to develop market depth and increase competition. The long-term outlook is also secured with the introduction of risk-based capital and greater flexibility in investment.

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Foreign ownership can be up to 100%

Regarding the increase of foreign investors' ownership in insurance enterprises, there has been a move since the end of 2021 when the insurance industry was included in the "Unrestricted" list of industries with conditional market access on foreign investors (refer here). In the new Law, the foreign investor's ownership ratio is regulated up to 100% of the charter capital of an insurance or reinsurance enterprise.

The unlimited ownership of foreign capital will certainly help attract the attention of foreign investors because the growth potential of the industry is still quite large due to the low insurance penetration rate of only about 3% compared to the rate of 8-9% in emerging countries. In addition, Swiss Re's premium growth forecast for emerging markets (excluding China) is outperforming other regions, expecting 5.1% year-on-year premium growth in 2022-23F (Table 1).

Currently, the non-life insurance market is fragmented with a large number of companies and most of them are domestic. Contrary to the image of the life market with the dynamic and exciting competition with foreign players participating (only Vietnam's representative Bao Viet Life competes in the top 5). The competition is necessary to be able to promote rapid market growth and we appreciate this characteristic from foreign players. Therefore, we expect more participation of foreign insurers in the non-life segment.

Table 1. Insurance premium growth forecast, global regions (%)

	Total		Non-life insurance		Life insurance	
	2021	2022-23F	2021	2022-23F	2021	2022-23F
World	**3.4**	**3.2**	**3.3**	**3.5**	**3.5**	**2.8**
Advanced markets	**3.3**	**2.4**	**2.8**	**2.4**	**4.1**	**2.3**
North America	2.3	2.4	2.7	2.4	1.2	2.2
EMEA	4.9	2.0	2.3	2.3	6.9	1.7
Asia-Pacific	3.9	3.2	4.6	2.9	3.8	3.3
Emerging markets	**3.4**	**6.4**	**5.8**	**8.2**	**1.4**	**4.6**
Excluding China	5.7	5.1	4.7	4.7	6.9	5.8
China	1.5	7.0	6.4	10.3	(2.8)	3.6

Source: Swiss Re Institute, KISVN.
Note: Total is non-life and life insurance combined.

Database and IT infrastructure

The new law also mentions the goal of building a database that the Ministry of Finance will be responsible for developing and managing. Accordingly, insurers, reinsurers, insurance brokers as well as organizations providing insurance ancillary services will be responsible for providing information about the buyer, the insured, insurance subject, insurance agent, and other information. At the same time, it is also necessary to ensure confidentiality, information security, and purpose of use.

Having a common database helps the regulator and management body to quickly grasp the market situation and make necessary and timely adjustments. Further and essential application is that insurance companies can access the information about the claim history of insurance buyers in order to verify the legitimacy of the claim and limit profiteering insurance stemming from a lack of communication between companies in the industry. In developed countries, the exchange of information between insurance companies is common and comprehensively regulated by law.

To achieve the goal of building a database, the Law also requires related enterprises to establish, maintain and operate an appropriate and responsive information technology system that satisfies the requirement to perform technical tasks of statistics, processing, and storing information.

Autonomy in new product development

Up to now, the State has played the role of providing capital and resources, and state-owned insurance enterprises have played a leading role in the insurance market. But with the new law, the State will not uphold this goal but will focus on encouraging and creating an open and transparent environment for insurers to research and develop technologies and products.

This point is also consistent with plans to divest state capital in insurance enterprises and promote cooperation plans with foreign strategic investors. Thereby, it will blow a new breath of expertise, products, and approaches into the domestic insurance market.

Under new law, The Ministry of Finance only approves the method and basis for calculating premiums, not insurance products. Thus, insurers will have more autonomy and will be responsible for their business activities, minimizing the bottleneck situation when the Ministry of Finance has to receive, review and approve a large number of products or amendments. From there, businesses can actively compete with each other better by launching trendy and improved products.

Risk-based capital will be applied (Risk-based capital, RBC)

The next noteworthy point is the official approval of capital regulations for insurance enterprises. The implementation provisions of these capital regulations will **take effect from January 1, 2028.**

The current capital regulation has existed since the first-generation insurance law (2000), which requires insurers to always maintain a charter capital not lower than the legal capital level, depending on the type of business and insurance products provided. This point creates great pressure for businesses to maintain a fairly high capital level right from the start, regardless of the level of risk that the business is taking. The surplus capital compared to legal capital will be significantly smaller (especially in small and medium enterprises), leading to reduced financial investment resources.

The new Law stipulates that insurers will need to monitor the following types of capital:

- Minimumum charter capital
- Owners' equity, including charter capital
- Real capital
- Risk-based capital, including:
  - Insurance risks: due to fluctuations of technical factors in risk assessment
  - Market risks: market risk towards investment activities
  - Business risks: from operational processes and management
  - Other risks

The addition of risk-based capital helps accurately reflect the risk scale that the insurance enterprises own. This point helps to improve financial safety and prevent major risks, but it will require businesses to prepare larger capital sources to be able to take on larger and broader risks. At the same time, the plus point of this change is that businesses that are receiving a small amount of responsibility will be able to reduce the pressure to maintain capital. Insurance premiums can be more competitive for customers because insurers can consider reducing premiums as financial investment resources are expanded.

Change the basis for determining the scope of investment

Currently, the allowed portfolio is limited and mainly focuses on financial instruments with stable and moderate returns, including:

- Government bonds
- Certificates of deposit
- Stocks, corporate bonds, fund certificates, capital contribution to enterprises (Limited from 20-35% of Idle capital, depending on the type of insurer)
- Real estate investment (Limited from 10-20% of Idle capital, depending on the type of insurer)

In the new Law, the list of investment fields is changed to regulate investment activities that are restricted, **effective from January 1, 2028**. The exclusion list includes:

- Real estate, except for the following: investing shares of real estate enterprises listed on the stock market, public fund certificates; owning real estate for office use; holding real estate due to the disposal of bonds secured by real estate within 03 years from the date of holding;
- Invest in precious metals and gems
- Invest in intangible fixed assets, except for insurance business activities
- Invest in derivatives, except for the purpose of hedging risks arising from insurance and reinsurance contracts and from the investment portfolio

At the same time, the investment principle will also limit some notable activities as follows:

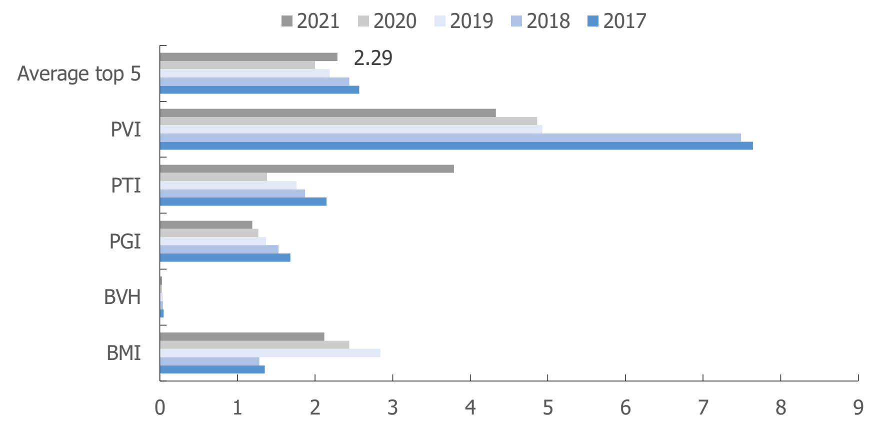
- Not allowed to use borrowing for stock investment, putting in investment trusts
- Do not invest more than 30% of investment capital in companies in the same group of companies with mutual ownership relationship
- Not to buy corporate bonds issued with the purpose to restructure the debt of the issuing company

More freedom in investment choices

The first point we want to mention is the limitation of real estate business because this change attracts the attention of investors. In our view, this is a necessary change and does not negatively affect the investment prospects of insurance companies for the following reasons:

- Firstly, the proportion of investment property holdings to total assets in insurance companies is not large. The average ratio in the top 5 companies is 2.57%, and 4 over 5 enterprises have a lower holding rate of 2.15%. In particular, the insurance company with the largest total assets, Bao Viet, holds only 0.05%.
- Second, insurers will have limited ability to develop real estate businesses because this is their main profession. Profit from real estate business (if any) is expected to come from market price increase after a period of holding, not the ability to develop value/ecosystem for real estate. Therefore, the real estate business may not be effective for insurers in the short-medium term and for the real estate industry in the long term.
- Finally, the new Law restricts direct real estate business but does not mean restricting capital flows from insurers into the real estate industry. Insurers can invest indirectly through shares listed on the exchange, fund certificates (REITs), or buy real estate corporate bonds. The benefit from the development of the real estate industry is completely guaranteed.

Figure 1. Investment properties holding ratio over Total assets



Source: Company data, KISVN.

Another positive point in the Amended Law on Investment is the removal of the maximum limit on investment in stocks and corporate bonds. In addition to allowing investment in trust funds, the financial activities profits of insurance companies are promising to benefit from the growth of the stock market, one of the investment channels with good returns and liquidity.

More attention to microinsurance, agro-forestry-fishery insurance

The definition of microinsurance is insurance aimed at low-income individuals and households to protect them against risks to life, health, and property. The feature of this type of product is a concise, easy-to-understand design with simple insurance appraisal procedures or no appraisal required. The development of microinsurance contributes to increasing the penetration rate of insurance to the people, contributing to ensuring the State's social and security policies.

The new law removed the cap on microinsurance premium (not exceeding 6% of the annual per capita income of the near-poor line in urban areas) to ensure the technical efficiency of the products (weighing the balance between the insurance premium and the amount of liability received). Accordingly, the insurance amount and annual premium for each insured person will be regulated by the Government.

To encourage the development of micro-insurance and agro-forestry-fishery insurance products, the State will support simplifying administrative procedures, propagating policies, and partially supporting on insurance premiums. Insurance companies will have more incentive to deploy these insurance products. Thereby, it creates habits and understanding about insurance for more groups of customers.

New law impacts on insurance market

Most of the experts' comments agreed with the need for the upcoming law in the context that Vietnam's insurance market has formed and developed during the past 20 years. The Insurance Law 2022 will take effect from January 1, 2023. In particular, some provisions on capital management, risk-based capital, and restricted investment list will be applied from January 1, 2028.

The revised Law also has many points that have not been specified in detail and will require discussions and documents under the Law to guide its implementation. But in general, with the above changes, we see a positive outlook for the insurance industry in the medium and long term. In the short term, the insurance market is still developing well, the insurance premium growth rate is similar to previous years and faster than in other countries in the region. The medium term will expect to see M&A deals, and strategic cooperation from insurers, reinsurers, or insurance ancillary organizations to develop market depth and increase domestic competition. The long-term outlook is also secured with the introduction of risk-based capital and greater flexibility in investment.

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