

**Lunch Talk of The Hong Kong Federation of Insurers  
21 April 2016**

**Speech by Dr Moses Cheng, Chairman, Insurance Authority**

*“Insurance in new economy: scaling new heights with IIA”*

Chairman Mike, Honoured Guests, my friends, Ladies and Gentlemen, Good afternoon!

I am indeed most grateful to the Federation of Insurers for inviting me to this lunch gathering, to meet with all of you and to share with you the mission of the Independent Insurance Authority and the challenges it faces in paving the way for scaling new heights with the insurance industry of Hong Kong in the new economy.

2. When I was first approached to consider taking up the appointment as the inaugural Chairman of the Authority, I felt deeply honoured but equally worried. It is always a daunting task to set up a new organization; and more so the independent authority for the insurance industry. It was after deep thoughts and prayers that I agreed to take up the invitation to work with all of you in embarking upon this new venture.

3. Since taking up the Chairmanship about four months ago, I have been meeting with many practitioners of the industry. They have asked me a lot of questions and raised with me their concerns. There are two frequently asked questions. The first one is whether I will be high-handed. This is a relatively

easy question. My answer is that I am right-handed.

4. By the way, in assessing the success of a regulatory regime, it is not so much about leniency or harshness in its approach. Rather, it is about doing the right things and doing things right, in the eyes of all stakeholders. A lot of it is about establishing credibility. And credibility is founded on accountability, impartiality, transparency, fairness and reasonableness.

5. In regulating any profession or industry, I am always reminded of the story of the little boy holding a bird in his hand. If he grasps it too tightly he would suffocate and kill the bird, too loosely the bird would simply fly away. Ladies and Gentlemen, it is all about achieving the proper balance.

6. The second question I was frequently asked is how would the Authority facilitate the growth of the Hong Kong's insurance industry. This is a much more difficult question in respect of which I must confess that I do not yet have a ready answer. However, it is my firm belief that the close collaboration between the industry and the Authority would undoubtedly promote the growth of the industry.

7. Allow me to make it clear. Whilst in regulating the industry some may perceive that the industry and the Authority might not be on the same side of the fence, yet in promoting the growth and further development of the industry, the Authority's stand is no different to that of the industry.

8. As pointed out by Niall Ferguson,

*“Evolution in financial services occurs within the regulatory framework”<sup>1</sup>.*

A sound regulatory framework, whilst protecting the interests of policyholders, is facilitating growth of the industry through healthy evolution and innovation within such framework. Again, the challenge, as always, is how to strike the reasonable balance.

9. Ladies and Gentlemen, the key to business growth in this age of competition, speed, crisis and absurdity, in my humble submission, is the ability to adapt to changes. We need to understand the changing forces in the first place before mapping out strategies for growth by adapting to the changes. I understand that a consultant from PricewaterhouseCoopers has identified five major changes that are shaping the future of the insurance industry. These five aspects are summarized as “STEPP” which stands for Social, Technological, Environmental, Economic and Political.

10. Socially, aging population would continue to pose a lot of challenges and opportunities. A US Census Bureau report has recently ranked Hong Kong as having the third highest projected percentage of aged population 65 years or above in 2050, at 35.3 per cent<sup>2</sup>. The Census and Statistics Department also projects that the elderly population aged 65 or above will more than double from 1.07

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<sup>1</sup> Niall Ferguson, “The Ascent of Money – A Financial History of the World”.

<sup>2</sup> Ranking and projected percentage of aged population of other major jurisdictions in 2050: Japan (1<sup>st</sup> at 40.1%); South Korea (2<sup>nd</sup> at 35.9%); Taiwan (4<sup>th</sup> at 34.9%); Germany (19<sup>th</sup> at 30.1%); US (48<sup>th</sup> at 22.1%).

million in 2014 to 2.58 million in 2064. Hong Kong people are definitely living longer. Among the elderly people now aged 65, 60% are expected to live to the age of 85 or above and 40% to over 90. These figures translate into a growing silver market for retirement products.

11. We are also facing higher customer expectations. Advances in technology and communication, combined with the explosive growth in data availability and information, would facilitate consumers in making more informed and better choices. Customers are looking for value to be clearly demonstrated, reflecting a balance of price, product features and service tailored to their personal needs. Once they have made their choice and established a relationship with a service provider, they expect the provider's products and services to live up to their expectations.

12. Customer expectations would, of course, evolve hand in hand with technology. The "service now" mentality and crowd-sourcing of information and solutions have facilitated the emergence of new market players in the financial services sector, notably smart phones and internet giants. But I am more fascinated by the extent to which technologies transcend insurance business to the next level. Just think of how Uber, the world's largest taxi company – and a taxi company owning not a single taxi, has shaken up the global taxi industry. If you do a Google search on "financial technologies (or "Fintech") in the insurance industry", there are lots of interesting stories including peer-to-peer insurance, and motor insurance which can be offered on a variable rate according to miles driven. It is clear that more and more innovative Fintech ideas would emerge for the insurance industry. As for our regulatory framework, it needs to be technology-

neutral as well as technology-embracing.

13. Environmentally, the insurance industry is so prone to the impacts of climate change. With catastrophic events becoming more frequent and severe, the industry would be overwhelmed with increasingly uncorrelated catastrophic events thus reducing capacity and escalating prices. Besides, this would pose challenges to assessing and managing risks. On the other hand, a lack of adequate understanding of climate risks by businesses may result in a protection gap. This is particularly true in Asia. According to the Geneva Association, an international think tank on insurance, less than 10 per cent of natural catastrophe losses in the region are covered by insurance, compared with more than 50 per cent in the United States.

14. Economically, the World Economic Outlook issued by the International Monetary Fund earlier this year forecasted diminished prospects in the global economy: a generalised slowdown in emerging market economies, mainland China's rebalancing, lower commodity prices, and the gradual exit from extraordinarily accommodative monetary conditions in the United States. Notwithstanding that, we still see sturdy economic growth in the Mainland and the Asia Pacific region. And with gradual enhancement to the economic infrastructure in developing economies, the benefits from reforms to governance and business conditions could help offset the effects of slow growth.

15. As for political changes, there have been political calls for tighter regulatory oversight to avoid recurrence of the 2008 financial crisis. The result is enhanced communication and cooperation among regulators of different

jurisdictions. Some of you might be worried by new international regulatory initiatives like the Group-wide Supervision and identification of insurers as Global Systemically Important Insurers. However, we must appreciate that these enhanced regulatory measures are not meant for stifling the growth of the industry, but for enhancing its stability. Hong Kong, as an international financial centre, would be expected to adhere to these international standards.

16. Ladies and Gentlemen, these are indeed “STEEP” changes! But is it not imperative upon the industry to identify how would these changes be impacting upon its business? Or how to sustain growth amid these changes?

### **Pillars to sustainable growth**

17. As I said earlier, I don't have a ready answer to these questions. But I would venture to share with you some of my observations. I believe that there are two pillars to support sustainable growth. The first one is the tenet that customers are always right. This means knowing the customers well and delivering products and services deemed satisfactory to their needs. The second one is that appropriate regulation is never wrong. This means we need a sound regulatory framework for maintaining public trust and confidence whilst facilitating growth and continuous development of the industry.

### ***Competitive and innovative market***

18. Hong Kong has long been a market facilitating continuous business growth and development with vibrant activities on both the demand and supply

sides.

19. It has long been one of the most active and open insurance centres in the world. Not only have we been able to attract a great number of insurers to operate their business here, we are also proud of our ability to innovate and devise products that can suit a wide spectrum of needs in the market.

20. There are indeed ample opportunities lying ahead of us. Firstly, the aging population means an expanded market catering for retirement needs. In recent years, insurers in some Asian markets have begun to explore alternative underwriting approaches for the silver market.

21. Korea, for example, scrapped its age-65 issue limit for critical illness products in 2012 and launched its Silver Cancer critical illness product. The product features simplified underwriting that enables applicants who also have diabetes and/or hypertension to be accepted without requiring additional medical underwriting or loadings. This could be done because cancer risk has significantly lower correlation with diabetes or hypertension, so high loadings are not needed.

22. The Census and Statistics Department conducted a Thematic Household Survey in 2012 on “Retirement Planning and the Financial Situation in Old Age”. Among the future generations, 50.9% had savings and investment while only 17.1% had purchased insurance to cover possible medical and healthcare expenses for various chronic illnesses in old age. The corresponding percentages for the current generation were even lower at 39.1% and 5.5% respectively. These

statistics suggest that as the retirement protection system matures and with a change of mindset, there is scope for improvement in the retirement protection for both current and future generations.

23. I believe that Hong Kong does have a favourable environment to encourage further development of insurance business in this respect. Hong Kong has a flourishing life insurance market. In 2014, there were more than 11 million life insurance policies in force and the total insurance cover was worth more than \$4,700 billion, with the overall insurance density<sup>3</sup> at more than \$40,000 and an insurance penetration rate<sup>4</sup> of 14.2%, which ranked first and second respectively in Asia.

24. All in all, as the population ages, the silver market will continue to rise in importance, and the senior cohort can offer substantial opportunities for insurers if there is a supply of comprehensible and suitable retirement planning products.

25. Secondly, the shift of the world's economic gravity towards Asia and the Mainland will put Hong Kong under the spotlight of the world's financial arena. A leading reinsurer has projected that Asia will account for 40% of the global insurance market by 2020 with five of the top 10 primary growth markets in Asia Pacific. With more intense commercial and financial activities conducted in the Asia Pacific region, I foresee that our role as an international financial centre would be more prominent.

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<sup>3</sup> Insurance density refers to the insurance premium per capita.

<sup>4</sup> Insurance penetration rate refers to insurance premiums as a percentage to the Gross Domestic Product.



26. There are also vast opportunities brought possible by projects under the Belt and Road Initiative. Hong Kong boasts a mature insurance market with rich experience and knowledge of insuring major infrastructure development, as well as talented professionals and well-developed laws. Furthermore, as more and more Mainland enterprises seek to “go global” under the Belt and Road Initiative, Mainland enterprises will find it advantageous to establish captive insurance companies in Hong Kong, make insurance arrangements and enhance risk management for their overseas businesses here.

27. Thirdly, we have all the necessary ingredients to develop and embrace Fintech. On this note, I am glad to see that some insurers in Hong Kong have already made some exemplary moves, for example, some life insurers have made use of wearable devices and mobile apps to launch health and lifestyle management programmes that encourage healthier lifestyles. There are also insurers who have formulated comprehensive digital strategies and invested in research laboratory for the application of Fintech in insurance business.

28. Further opportunities are where more innovative concepts could be adopted across different business lines and along the value chain. For example, claims management could be improved through better predicative analytics that helps connect data to effective action by drawing reliable conclusions about current conditions and future events. For back-office processes, big-data technology allows underwriters to more conveniently access customers’ conditions and risk patterns as well as enables the product development departments to know their customers better and reach out to new customers. As

for insurance distribution, we see more direct sales channels such as mobile apps available for consumers to take out simple and standardised insurance products. We don't know how this development may impact the role of insurance intermediaries. But we need to get prepared for changes that may come earlier than we expect. In any case, the Authority will be prepared to collaborate with the Government and the industry to facilitate development of Fintech in Hong Kong.

### *Sound regulation*

29. A vibrant market is underlined by growing demand and supply. Financial transactions are underpinned by trust and confidence. Like every other industry, or perhaps even more so, the insurance industry is critically dependent on consumers' trust because insurance is simply what provides consumers relief when their Plan A fails. That brings me neatly to the second pillar of sustainable growth.

30. As I mentioned earlier, in the wake of the 2008 financial crisis, regulators and lawmakers around the world have enacted a growing number of local and global regulations with which financial institutions need to comply. In the early days, financial institutions seemed to view these regulations as a mere compliance issue. Now, I am happy to see that conduct and professional integrity are very firmly on the agenda of executive management and Hong Kong Federation of Insurers has been working on a framework for treating customers fairly.

31. Apart from the traditional prudential regulation to ensure insurers' obligations to consumers are met, regulations are needed to eliminate any unfair

and deceptive policies and practices. A sound regulatory system also promotes true competition by ensuring consumers' access to information about the quality and comparative cost of different insurance policies.

32. As a regulator, the Authority's key objective is to facilitate the development of the industry without compromising consumers' protection and tilting a level playing field. I understand that recent regulatory initiatives of the Office of the Commissioner of Insurance have created a lot of workload for insurers to redesign ILAS products and update benefit illustrations of life policies. I am sure insurers' efforts to treat customers fairly will pay off.

33. Let's be honest. ILAS are complicated and the fee charging structure is bewildering. There have been mis-selling causing dissatisfaction, frustration and even anger among ILAS buyers, bringing disrepute to insurers and intermediaries. And the benefit illustration is an important piece of information for a customer to make an informed buying decision. Providing an up-to-date benefit illustration is a basic, and not extra, requirement. Luckily, the industry has been very co-operative in these two exercises.

## **Conclusion**

34. Ladies and Gentlemen, I might have said too much on this very first opportunity to share some of my observations with the industry. And I certainly not wish to cause indigestion to you after such a good meal. To conclude, let me say that insurance company executives might often cite regulation as a major risk in responding to surveys on business risks. I must admit that regulatory

measures more often than not will result in higher compliance cost. That is why a responsible regulator has to be careful when formulating regulatory measures. And effective communication between the regulator and the industry is of paramount importance. The Insurance Companies (Amendment) Ordinance stipulates that the Independent Insurance Authority must consult the industry before introducing a new regulatory measure. And the Government will soon announce the appointment to the two statutory Industry Advisory Committees. They are the important advisors to the Authority. I look forward to working closely with them and to the constructive exchanges between the Authority and the industry in updating our regulatory framework so as to enable the industry to capture opportunities in the rapidly changing business environment.

35. Let me assure you once again, Ladies and Gentlemen, “Successful regulation is never coercion, it is effective collaboration.”

36. Thank you.