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Rising to the challenge

There was plenty of opinion, debate and discussion at this year's Turkish market roundtable event

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Turkish Market Roundtable Report

Readers of last year's *Turkish Market Roundtable Report* may spot some familiar themes this time around, such as continuing price competition and persistent foreign interest in entering this highly attractive market.

However, it would be a mistake to assume from this that it is business as usual in Turkey. It is clear from the comments and evidence provided by the excellent line-up of speakers around the table this year that the Turkish market is at an infection point.

While it is true that the market continues to be challenged by soft pricing, high competition and low public awareness of insurance, there are a number of positive forces at work.

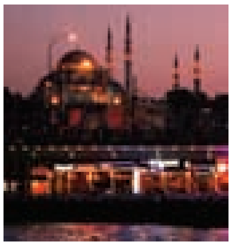
The Turkish economy has bounced back, but low interest rates remain, making it more important than ever to improve underwriting. There are also plenty of new opportunities for insurers to pursue, in part thanks to the addition of compulsory medical malpractice insurance in 2010, and the promise of more additions to come.

As the dual effects of low interest rates and soft pricing take hold, there is also the very real prospect of mergers, acquisitions or withdrawals from the Turkish insurance market, which could considerably ease the pressure on the remaining players.

The market is also bracing for the implementation of Solvency II. Evidence so far suggests that the market will hold up well under the more stringent capital rules, but implementation will be a challenge. While the burden will be greatest for smaller firms, the new regime is sure to mean big changes for (re) insurers of all sizes.

Turkey remains a market that is yet to fulfil its full potential, either for foreign entrants or local firms. But the changes afoot should bring about opportunities for all.

Ben Dyson
Assistant editor
Global Reinsurance



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Onwards and upwards

As Turkey marks out its recovery, things are looking good for the insurance sector. The *Global Reinsurance* Turkish Market Roundtable explored the factors contributing to this progress – from compulsory insurance to Solvency II, says Cahit Nomer

The Turkish economy has recovered as from the second half of 2010, and this positive development has been reflected in the Turkish insurance industry.

In 2010, the Turkish market made great strides compared with the previous year, and showed a 13.5% increase in premium production – a growth in real terms. We expect this trend to continue in 2011 and the following year, in the absence of another crisis.

That being said, price-focused competition is still a big concern for the market, as it has been for the past three to four years. This affects insurance companies' premium income, which in turn results in a negative impact on their profitability.

The influx of foreign capital has begun again in the aftermath of the economic recovery. One insurance company, Fiba Sigorta, was sold to Japanese insurance group Sompo in June 2010, and another, Aksigorta, merged with the UK's Ageas in February this year.

The market is continuing to develop and grow. More compulsory insurance products have recently been introduced to the market. These products are extremely helpful in increasing the market's premium production. The number of compulsory liability products is set to increase as Turkish law comes more into line with EU regulations.

Knowing our worth

The economic development of the country is boosting insurance penetration. Bancassurance is playing an ever greater role in the market's overall premium production as banks get more involved in people's lives by providing credit. The levels of credit banks are providing to allow people to buy homes and cars has increased dramatically compared with previous years. And recent natural disasters are significantly contributing to public awareness of the need for insurance.

> Following on from the most recent wave of liberalisation five years ago, the Turkish market continues to adapt and evolve

Following on from the most recent wave of liberalisation five years ago, the Turkish market continues to adapt and evolve. The preparation work for the European Commission's forthcoming Solvency II capital regime continues. Solvency II is likely to come into effect in Turkey later than the EU, where it is scheduled to arrive at the beginning of 2013.

But when it does arrive, it will strengthen the financial structure of companies, improve market transparency and protect customers' interests.

We continue to support the *Global Reinsurance* Turkish Market Roundtable because we understand how useful it is in allowing the international insurance market to get a more accurate picture of our industry.

We were pleased with the results of last year's event – we are certain that the 2011 roundtable will be even more effective. GR

Cahit Nomer is executive vice-chairman of Milli Re

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Outside influence

The influx of foreign investment in Turkey is a blessing as well as a curse, writes Ben Dyson. Changes and careful consideration will be required for both local and foreign firms to make the most of this attractive market

It is easy to classify Turkey's insurance market as emerging. Its insurance penetration figures would certainly support this analysis. Insurance premiums per capita in Turkey in 2009 were $105, according to figures from Swiss Re's *Sigma* publication – the second lowest in Europe after Ukraine. Total premiums were 1.3% of GDP in 2009, with 1.1% coming from non-life and 0.2% from life. By comparison, the average for Europe is 7.6% of GDP.

However, such a categorisation belies the market's sophistication. Turkey has a well-developed non-life insurance market in both personal and commercial lines, and the country appears determined to keep its capital adequacy regime in line with continental European standards (see box).

This combination of emerging market opportunities with mature market sophistication has proven a strong draw for large international insurers. These companies face limited growth prospects in their saturated home markets, and so the potential offered by Turkey is alluring.

This potential is only made more attractive by the fact that Turkey lacks the barriers to entry and restrictions on foreign ownership present in other markets that fall into the emerging market category.

The rush to get into the Turkish insurance market has slowed considerably since its peak in 2006 and 2007. Nevertheless, large international groups are still keen to gain a foothold, and are willing to pay extra to do so.

In February this year, Belgian-Dutch insurance group Ageas (formerly Fortis) bought 31% of Turkey's fourth-biggest non-life insurer Aksigorta for $220m. The price valued Aksigorta at a 53% premium to its closing price on 17 February.

There could be more soon. Ahmet Genç, general director of insurance at the Turkish Treasury, says that there are between one and three new entrants in the pipeline.

Foreign-owned companies now control more than 70% of Turkey's non-life market. For example, the biggest non-life insurer in the country by both gross written premium and market share as at 30 June 2010 was French group AXA, according to a report by actuarial consultancy Towers Watson. Seven of the top 10 companies (now including Aksigorta) are foreign-controlled, with big names such as Allianz, Groupama, Ergo, Eureko and Mapfre among the biggest non-life writers.

A mixed reception

Some argue that the influx of foreign investment has improved the market's sophistication. However, there is also evidence that Turkey's popularity with the outside world is a curse as well as a blessing. Turkish insurers initially welcomed the newcomers with open arms, assuming they would bring pricing discipline and improved underwriting techniques to the market. However, many market participants report that competition has intensified since their entry, as the new owners try to maintain or grow their market share.

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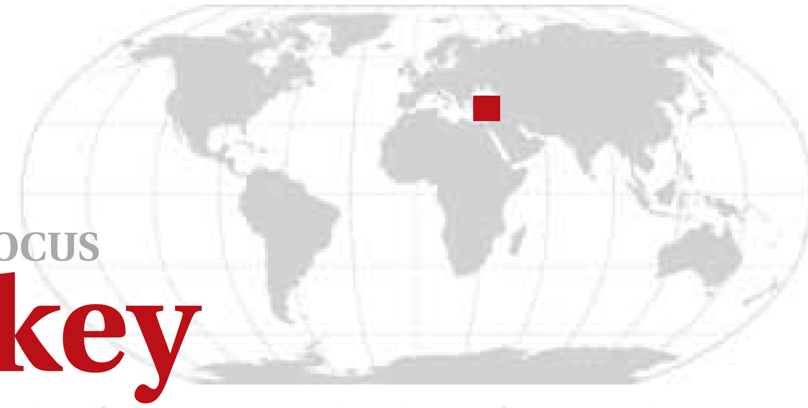

COUNTRY FOCUS

Turkey

Turkey has a well-developed non-life insurance market, and a combination of emerging market opportunities with mature market sophistication has proven a strong draw for large international insurers. Challenges remain for (re)insurance players both local and foreign, but the market has plenty of room for growth.

Turkey:
Population: 74,815,703 (2009)
GDP (PPP) per capita: $12,300 (2010 estimate)
Main players include: Allianz, AXA, Anadolu, Milli Re, Groupama, Aksigorta, Günes Sigorta, Eureko Sigorta, Ergo Sigorta, Mapfre

Insurance penetration

EU	27%
OECD	8%
*Emerging markets**	2.7%
Turkey	1.2%

**Turkey's emerging market peers in Latin America, eastern Europe, Middle East*

As a result, there continues to be much concern and commentary about underpricing in Turkey's non-life market. Although there are pockets of profitability, and some lines such as health have shown improvement, rates are generally still soft.

Foreign entrants are not the only ones putting pressure on insurance premiums. Insurance remains out of reach for many people, and so the Turkish government is keen for rates to fall further.

In addition to the cost issue, the Turkish insurance industry appears to be struggling to win over the hearts and minds of the public. Despite the threat of earthquakes in the country, policy count at the Turkish Catastrophe Insurance Pool dropped by five percentage points in 2010.

In commercial lines, the opposite problem exists. Coverage is widely held to be available for more mainstream risks, but Genç at the Turkish Treasury reports that several groups have complained about a difficulty in obtaining insurance, including owners of small kiosks known as bufes and real estate firms.

Challenges ahead

While the insurance penetration figures clearly show that there is plenty of room for Turkey to grow, some report that the market is not necessarily heading in the right direction. Çetin Alanya, general manager at Dubai Group Sigorta, points out that while both premiums and GDP grew in 2010, premiums as a percentage of GDP fell by between 0.1 and 0.2 of a percentage point.

The Turkish market is facing considerable challenges, but there are plenty of reasons to be optimistic about the market's future. Turkey's economy was hit hard by the financial crisis of 2008 and 2009, and, as with other insurance markets around the globe, a sharp drop in interest rates has severely diminished investment returns. As they can no longer rely on investments to prop up earnings, insurers will have to focus more on making an underwriting profit. Companies are hiring more actuaries and underwriters in a bid to boost technical profits.

There are also some signs that the competition from international players could abate soon. The firms that entered in 2006 and 2007 have now been in the market for between three and five years. While parent firms may tolerate thin profit margins or even losses for an initial period in return for maintaining or boosting market share, they may soon start asking for more robust returns. If their Turkish investments cannot deliver this, they could begin to rethink their strategies.

Milli Re director and general manager Hulki Yalçin believes the market has reached a turning point. "In terms of international investors, we are reaching another level where they make their final decision, because with this level of profitability it is not sustainable." **GR**

> The Turkish market is facing considerable challenges, but there are plenty of reasons to be optimistic about the market's future

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Keeping up with Solvency II

While not yet part of the EU, Turkey seems determined that its capital adequacy regime at least keeps pace with Europe. The country has started conducting Solvency II's fifth quantitative impact study (also known as QIS5), which insurers within the EU completed last year. The study is due to be completed by the middle of 2011.

The results of the previous Solvency II study, QIS4, contained encouraging news about the solvency levels of Turkey's insurance industry.

After Turkey evaluated 10 sample companies under the QIS4 framework, it was found that most firms fell between Solvency II's minimum capital requirements (the minimum capital a company can hold before regulatory intervention) and the solvency capital requirements (the amount of capital needed to provide at least 99.95% certainty that a company can meet its obligations over the next 12 months).

Ahmet Genç, general director of insurance at the Turkish Treasury, points out that Turkey's current capital adequacy regime is more stringent than Solvency I, with capital requirements roughly double what Solvency I requires.

Under Turkey's capital requirements, 10 companies have capital below requirements, while under Solvency I, only one or two companies are deemed undercapitalised. "That is not effective. That is why the EU has been working on Solvency II for more than 10 years," he says.

While implementing a capital regime in line with Solvency II will undoubtedly benefit Turkey's insurers, it will not be easy for some. "For smaller companies, QIS5 is not so easy to calculate and adopt," he says.

He adds: "Another problem is that our existing capital requirements are already tough, but Solvency II will require Turkish companies to hold even more capital."


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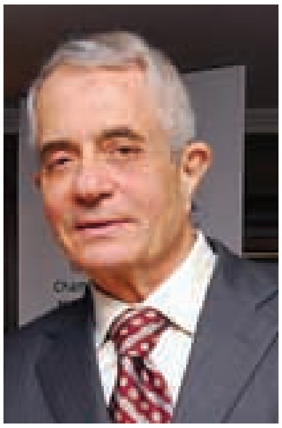
The faces around the table

They came, they discussed, they debated. Meet the industry figures who participated in our second annual Turkish market roundtable



Cahit Nomer (moderator)
Executive vice-chairman, Milli Re

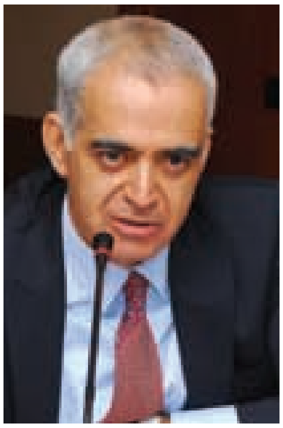
Muzaffer Aktaş
Managing director, Turkey, Africa and the Middle East, Willis Re

Hulki Yalçin
Director and general manager, Milli Re

Mustafa Su
Chief executive, Anadolu Sigorta

Kerim Tarman
Project manager, Catlin

Ahmet Genç
General director, insurance, Turkish Treasury



Ertan Firat
General manager and board member, Aviva Sigorta

Çetin Alanya
General manager, Dubai Group Sigorta

Jürgen Brucker
Client manager, Munich Re

Turkish delights

With only 25% of properties in Turkey covered, its insurance market shows plenty of promise. In this roundtable debate, held on 28 April in Istanbul, a panel of experts from across the region discussed how to overcome issues such as pricing, profitability, capacity and a public lack of understanding about insurance

'I often ask people if they smoke and tell them they can insure their house with the same outlay'

Muzaffer Aktaş, Willis Re

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Managing director, Turkey, Africa and the Middle East, Willis Re
Çetin Alanya
General manager, Dubai Group Sigorta
Ertan Firat
General manager and board member, Aviva Sigorta
Ahmet Genç
General director, insurance, Turkish Treasury
Cahit Nomer (moderator)
Executive vice-chairman, Milli Re
Mustafa Su
Chief executive, Anadolu Sigorta

Many observers have commented that Turkey is a market with great potential. Several large international insurance companies seem to agree, as the level of foreign participation in the sector now exceeds 70%. Sitting alongside traditional players are several well-known global brands such as Allianz, Eureko, Groupama, Generali and, more recently, Ageas (formerly Fortis).

However, this potential has yet to be fully realised and there is much debate about what could spur further growth of the market. While opportunities undoubtedly exist, there are a number of barriers, including public lack of insurance awareness on the personal lines side and a potential lack of capacity on the commercial side for more specialist risks.

Equally, especially on the commercial side, retentions are low and a large amount of premium ultimately flows to the international reinsurance market.

At *Global Reinsurance*'s 2011 Turkish Market Roundtable, experts discussed what could spur growth.

Muzaffer Aktaş: Despite the losses in Japan, Turkish property rates should be decreased, not increased. Only 23%-25% of properties in Turkey are insured. There is a golden opportunity for insurance companies to use the event in Japan and say to all Turkish people, 'you are not insured and if such an event happens in Turkey, you will be in a terrible situation'.

Production is very important. If Turkey properly uses its untapped potential, there will be no need to worry about whether rates are low or high. The limited number of properties insured are causing us a problem – we are not making the law of large numbers work for us.

Ertan Firat: Are we saying that if you decrease the price, the total volume will increase?

Muzaffer Aktaş: It will have an enormous effect. If you tell the agencies they are not properly exploring untapped potential, they will say people can't afford to buy insurance. In countries like Turkey cost is important, so it is necessary to reduce and explain the costs. We are not explaining adequately that the cost is not too high and that people can afford it. I often ask people if they smoke. When they say yes, I tell them they can insure their house and buy a low-sums-insured life policy with the same outlay. We are failing to educate ourselves and the people.

Ertan Firat: I think the issue is more than just price elasticity.

Muzaffer Aktaş: For a certain section of the population it is price, but I agree it is not only price. You also need to educate people that they need insurance.

‘Everybody in Turkey knows it is an earthquake country. Why are they not buying?’

Çetin Alanya, Dubai Group Sigorta

Cahit Nomer: To my mind, prices are very much on the low side and the issue is a lack of insurance awareness from the public.

Çetin Alanya: The Turkish market is growing, but not enough. It is an emerging country and the economy has one of the highest growth rates. But insurance as a percentage of GDP is getting smaller instead of larger.

I agree that the growth area is personal lines insurance, but have a look at the figures: there are between 11 and 12 million motor third-party liability policies, but 3.5 million motor own damage policies. Also, inflation was 6.5% and fire premiums grew in Turkey by 5.2% in 2010 – meaning there was a decrease in real terms last year in fire and allied perils insurance.

The number of policies in the Turkish Catastrophe Insurance Pool (TCIP) declined by five percentage points. Everybody in Turkey knows it is an earthquake country. Why are these people not buying or renewing their existing policies in TCIP? This has nothing to do with advertisements – Turkish people know an earthquake is expected.

Ahmet Genç: For about 30 years we have been saying that there is big potential in Turkey, but where is this potential? The growth issue has two parts: one is individual insurance and the second is industrial and commercial risks. For individual insurance I agree with all the arguments, but for the second part I do not. For industrial and commercial risks, there is demand, but not enough supply. First the industry needs to solve this supply problem.

At the Treasury we are trying to do our best to increase insurance penetration. For example, in 2010 we started to implement a new insurance – medical malpractice – as compulsory.

Almost TRY100m (£39m) of premium came into the market. After two years of financial crisis, we had a real increase in premium production in 2010. But in terms of technical profitability we are no better than the crisis years.

This is for two reasons: competition, and the fact that the government wants prices to go down. That leads us to the economies of scale issue, and also to the mergers and acquisitions issue.

Mustafa Su: Statistics clearly indicate that although we don’t know when the potential will explode, there is still a lot of potential, be it premium production per capita or if you define it as a percentage of GDP.

In the future, middle-market lines are likely to grow, especially personal lines and the insurance of small-to-medium-sized companies – kobis in Turkish. As far as I know, there are more than 700,000 kobis that are still uninsured.

So, apart from personal lines, other growth areas seem to be small-to-medium-sized companies, all types of liability products and the aviation sector, if insurers are successful in developing technically correct prices.

On that front, all companies are now required by law to employ actuaries. My company started with one and there is now one chief actuary in a department of five people, plus other actuaries in our technical departments. All companies should follow this example.

On the subject of supply and demand for industrial risks, I don’t think there is such a big problem. The larger companies in Turkey are insured – there is no problem with them. The problem is the smaller companies and we are more than willing to insure them. We have the capacity as a sector.

One problem is that, because Turkey was formed from an empire, people and businesses deem the state as the father of the nation and so expect everything from the state. The insured sometimes does not understand the difference between himself and the uninsured.

Even if the statistics show that there is great potential, we have problems addressing the feelings of individual people and this needs efforts from the companies and our association [the Association of the Insurance and Reinsurance Companies of Turkey].

Cahit Nomer: As far as I know, while coverage for some unusual risks is required by some insureds, all conventional covers are available in the local market.

Ertan Firat: When we are talking about growth, we also have to talk about the retained amount in the market. It is also an issue. When you look at the property market, most of the premiums are not retained by companies – they go to the reinsurers, though not in personal lines.

One risky element of the commercial and industrial side, which I think the Treasury should be aware of and come up with disciplines and regulations, is that I see an increasing trend of fronting, where the premiums are not retained in the market and are going out via brokers. We have to face up to this issue.

When I look at the whole commercial and industrial line of business I think the market is quite healthy, providing supply to meet demands. There may be some niche areas, but the niche areas may be very specific. The premium generation for that line of business may not be high, because of the nature of that type of business.

And the market is mostly dependent on the reinsurers on that side, because when you look at the commercial and property side I think the retention is about 20% or 25%, maybe a maximum of 30%.

I would add that it is not easy to create capacity for something specific. How we shape the scope of insurance is another issue between the regulators and the market. If you design coverage that is not in the range of the reinsurance coverage acceptance, it may be a risk.

Cahit Nomer: Ahmet, why did you say that there was a lack of supply in commercial lines?

Ahmet Genç: I have simply listed what people have come and told me, particularly over the past 10 years. For example, the Izmir chamber of industry and also the Agean region chamber of industry want credit insurance, because they are selling products to retailers and they are taking the money in 12-month, 15-month and 16-month instalments.

We are also talking to the association of Turkish bufes [small kiosks selling newspapers and tobacco]. We have hundreds of thousands of bufes around Turkey. The association says they are not able to find insurance, because insurers say they are not protected well enough.

Another group is real-estate experts, who are not finding liability insurance. Also, transportation to Iraq and even subways.

'The industry is creating problems of profitability – it has nothing to do with the regulator'

Çetin Alanya, Dubai Group Sigorta

Çetin Alanya: I think there is more than enough supply for conventional risks. Ahmet Genç mentioned credit insurance. This is a niche area and is done in Europe by specific credit insurance companies. We have got these sorts of companies now in Turkey, like Coface and Euler Hermes.

It is expected for them to do this business because in order to effect credit insurance you have to have a very good, knowledgeable network of people who provide you with statistical or financial information on the buyer side.

Also, in order for the insurance company to pay, there must be a court liquidation decision or bankruptcy decision. This takes a long time.

Regarding the kiosks, we are insuring these but they are highly open to burglary risks as they only sell things like cigarettes and newspapers, and the amount of claims you pay is 100 or 200 times the premium you ask for. They are unprotected.

Real-estate liability is something that should be covered. Some companies cover Iraq transportation and some don't. The loss history in Iraq is very bad, but some companies are providing some coverage.

With regards to growth, I read in the newspaper that Turkey has the third-worst income distribution after Chile and Mexico.

When this income distribution gets better – and it is getting better according to our per-capita income – and the young population enter the economy and amass some wealth to insure, Turkish insurance has a bright future for growth.

Our other big problem is profitability. This can be dealt with. We, the insurance industry, are creating this problem and it has nothing to do with the regulator. We know how to create unprofitability. We also know how to create profitability.

Mustafa Su: Some good news: we have introduced our own credit insurance product for petroleum distribution businesses.

With regards to kiosks, some are well organised, but many lack the simplest measure of fire or burglary prevention. As the quality of these institutions rise, the Turkish insurance industry will be with them. GR

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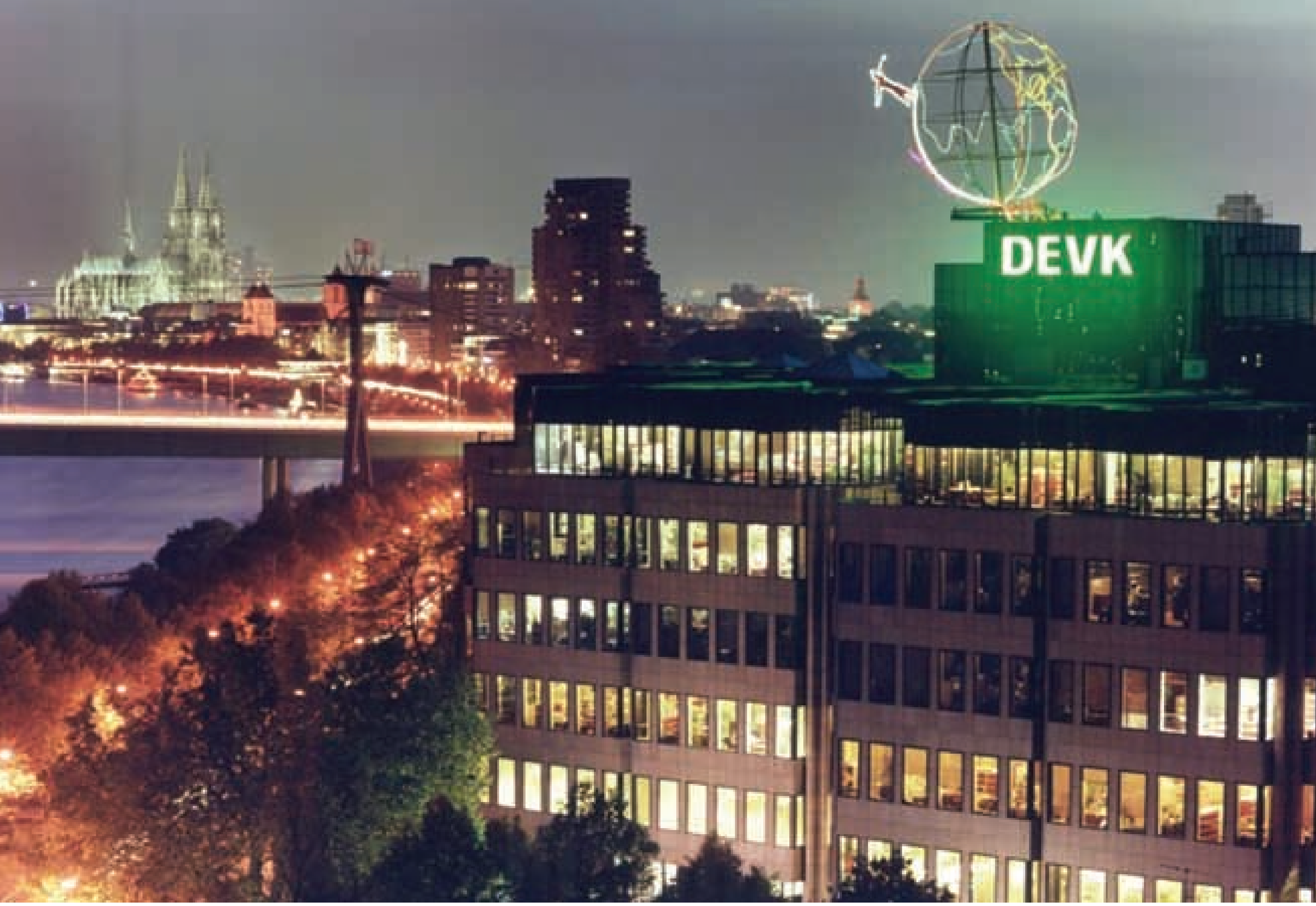

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A cut above the rest

Participants in the roundtable discussion were concerned about how insurance companies could enhance their profit margins in the context of inflation, low interest rates and intense competition

‘In 2007, we were taking 20% interest rates into account – the good old days. Now they are 8%’

Çetin Alanya, Dubai Group Sigorta

Jürgen Brucker
Client manager, Munich Re
Kerim Tarman
Project manager, Catlin
Hulki Yalçin
Director and general manager, Milli Re

One of the main barriers to the Turkish insurance market reaching its full potential is profitability. Competition is intense, driven in part by the large levels of foreign participation.

However, as in other insurance markets around the globe, low interest rates are depressing investment returns, placing a greater emphasis on the need to turn an underwriting profit.

The participants in the 2011 *Global Reinsurance* Turkish Market Roundtable discussed the current levels of profitability in the Turkish insurance market and how they can be improved.

Hulki Yalçin: Inflation could be a problem both worldwide and for the Turkish economy. Right now we are experiencing a low inflation rate, but we will probably see an increase in the figures in the second half of the year.

We should be very cautious as it seems that although we have overcome some of the problems of 2009 and 2008, there could be further problems that affect us. We had some good results in 2010, but because of the global issues, 2011 could be a problematic year for Turkey.

Çetin Alanya: The interest rates of investments went down enormously. In 2007, when we were preparing the feasibility study of Dubai Group Sigorta, we were taking 20% interest rates into account – the good old days. Now they are at about 8% and so the financial income of the market dropped from 2009 to 2010. It was 3% of premiums in 2009 and in 2010 it went down to 0.6%. This has had a big impact on profitability.

Cahit Nomer: This is affecting profitability, but is it affecting the underwriting of the companies? If there is no financial return, you have to get money from the technical account. Do you have any hope for this happening?

Çetin Alanya: I am hopeful. In motor personal accident we have seen an improvement in results from 2009 to 2010. It is a very positive development. Our problem is motor third-party liability, where there are losses of TRY585m (£226m). We should do something about it, hand-in-hand with the regulator.

Mustafa Su: I see improvements in some areas – for example, I haven’t seen kamikaze attacks on rates in the health business in recent months. Historically, we were used to offers [of premium] that were lower than the previous year’s claims payments in health, so there is a very clear improvement.

In motor, as Mr Alanya pointed out, we are seeing improvements, although we still recorded a loss in 2010. However, some companies reported profits. We have a problem with third-party motor liability, but we should keep in mind that the loss recorded in 2010 is the result of two previous years’ premium production. If you look at the average premium charged by the companies now, even if we cannot claim that the loss period will be over in the coming two or three years, it should develop positively.

Ertan Firat: I think we have to look at the macro drivers behind all this. The Turkish insurance market is in a transformation phase. We have seen the number of foreign companies increase over the past five years, and now 70% of the market is controlled by foreigners. The first issue for them is gaining market share, but now we all know that, on an international scale, the global players are concentrating on operational capital generation. It is an important issue for them and I think it will also affect the local market.

What I also mean by transformation is tariff abolition in motor third-party liability and also the reporting system. The market is learning from the reporting system. We can now digest information from the motor bureau and use it to identify fraudsters, for example, and price accordingly. When I look to the future, I see firms concentrating more on issues such as pricing, data mining and rate-making. I am optimistic that the market will recover, but we will have to see that all this happens because of the transformation.

Cahit Nomer: Do we want 100% freedom in setting third-party liability prices?

Mustafa Su: The question is, what would happen if it was 100% free? Philosophically of course I want it, but realistically I am worried about what would happen if it was totally free.

Ertan Firat: Before doing that, the transformation of the distribution network must be tackled, because there is a lot of competition on the network side, and a question over its quality. For example, cross-selling activities account for no more than 1.4% of business. The market should invest in the distribution network. If tariffs are abolished before that, it could create problems.

Ahmet Genç: It is not a problem to free motor third-party liability tariffs totally, but we are not interfering with the upper side of the rates – we are simply imposing minimum price levels.

Muzaffer Aktaş: If a crisis affects everybody, it is a blessing for the insurance industry because it should be taken as an opportunity to raise prices. In such a situation nobody can blame you for raising prices – everybody is in the same boat and is going to benefit. Because we are denying ourselves financial income as a result of this crisis, we need to raise our technical income.

‘A crisis that affects everybody is a blessing. It should be taken as an opportunity to raise prices’

Muzaffer Aktaş, Willis Re

Jürgen Brucker: We have seen the Turkish economy rebound in 2010 and 2011. This will have positive effects in the long term, but what does the industry have to do right now? Overall, efficiency in terms of administration, claims handling, underwriting, marketing, and sales and distribution has to be improved with a view to perhaps reducing both management costs and distribution costs. Distribution costs in Turkey are quite high compared with other countries.

If a company can address and improve on these issues, it will have more room to offer competitive rates if it is deemed wise to expand its customer base. Insurance penetration is still quite low in Turkey, mainly because people cannot afford insurance cover. The insurance industry has to offer adequate terms and conditions to the market, but can only do so in a low-interest-rate environment if they create synergies and improve efficiency.

Cahit Nomer: So before you increase rates you must reduce management expenses and acquisition costs?

Çetin Alanya: It depends on the size of the company. It is the size that determines how big a percentage the costs are of the total.

You have standing costs that you have to pay, and until you reach a certain size they are a high percentage of your revenue. When you exceed this size, the relative cost comes down and you are able to adjust your rates. The companies with this advantage of lower costs are charging lower rates and are making profits.

Mustafa Su: Maybe improving underwriting will increase our costs in terms of payroll. We have to employ more actuaries, more risk engineers, more able underwriters, and we have to increase the inside pressure for the correct pricing.

That should be an inside conflict between the marketing people, the risk engineers and the actuaries. That is, I think, the salvation from today’s problems.

Kerim Tarman: Let me make one point on retentions related to generating more underwriting profitability. From my point of view, a lot of insurance companies active in Turkey tend to reinsure a huge part of their portfolio. This leads to a minimised risk exposure, while on the other hand the possible return per policy is affected.

Players who want to improve their underwriting profitability through higher retentions would, of course, need to be very careful with their pricing and risk acceptance strategy. Otherwise the expected profits could be wiped out very quickly. GR


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Our new friends

With more than 70% of the Turkish insurance market under foreign control, the panel discusses how companies can deal with the effects of global reinsurance rates and increased competition

> 'In terms of international investors, we are reaching a level of profitability that is not sustainable'
>
> **Hulki Yalçin,** Milli Re

In some respects, the Turkish insurance market keeps itself to itself. Its local insurers do not write a great deal of business outside their home country, for example. However, that does not mean that Turkey is immune from outside influence.

More than 70% of its insurance market is now controlled by foreign-owned entities, which means it is affected by the strategies and thinking of the large international insurance groups. Furthermore, a large proportion of Turkey's commercial insurance is ceded to international reinsurers. In theory, the reinsurance premiums paid by Turkish insurers could be affected by the string of natural catastrophes that have hit the market over the past 12 months – even though none of the losses have emanated from Turkey.

And while Turkey has not yet joined the EU, the European Commission's forthcoming Solvency II capital adequacy regime is having a big influence on the market.

The participants of the 2011 *Global Reinsurance* Turkish Market Roundtable discussed the positive and negative aspects of the various external influences.

Reinsurance rates

Cahit Nomer: What would be the effect, if any, of the Japan loss on the reinsurance costs of Turkish companies?

Muzaffer Aktaş: The reinsurance community is large. Contributions to losses from major events [in the form of increased premium] will come from all parts of the world. Where losses occurred, it will be a major contribution. For others, the contribution may be tiny.

If there were no contributions from the rest of the world, the country that suffered the major loss – in this case Japan – would not be able to find a solution. We had a similar case on 11 September 2001. It was a $40bn loss and it wasn't only the Americans who paid the price – the rest of the world contributed, although some only a tiny amount.

In this case I think there will be a tiny increase from this part of the world.

Jürgen Brucker: We have seen an extreme event in Japan. Following such extreme events, we tend to experience a global hardening of terms and conditions. We therefore expect price increases, especially in global lines such as natural catastrophe or industrial business, but also in other loss-affected regions from previous events, for example Australia and New Zealand. There might be some side effects in other countries, too.

I think some changes might be expected in the Turkish market, as it depends very much on international as well as local reinsurance support; to what extent remains to be seen.

However, this has to be seen in the context of supply and demand. One impact on supply and demand is the exchange rate. The weakening Turkish lira against the euro means the capacity

‘I welcome foreign investment. But I think our expectations were optimistic and naïve’

Mustafa Su, Anadolu Sigorta

required by the regulator to cover a one-in-200 or one-in-250 year event is being reduced. The capacity that may be needed in euro terms in six or seven months, at the time of the renewals, might be lower, despite the increased exposure in Turkish lira.

I would add that we have recently observed the issue of new catastrophe models (also for Turkey), particularly from one company that is widely used in the Turkish market. I think it is fair to say at this stage that we will experience a change in the exposure probable maximum loss driven by the change of this model.

Ertan Firat: Reinsurers’ first instinct appears to be to increase prices. We experienced this issue on 1 April. I think the Turkish market should be ready for this.

Cahit Nomer: What are the implications of the unrest in Libya and other Middle East and North African (MENA) countries on local reinsurance markets?

Kerim Tarman: We have a very big construction industry here in Turkey. Turkish contractors are among the most successful in the world, and are playing a big role, particularly in this geographic region.

When Turkish contractors take on projects in foreign countries, they often approach their local Turkish insurer or broker for placement. As a result, Turkish insurers do have a fairly high exposure in the MENA states.

It will be very interesting to see how the industry will react to current political developments in this region, in terms of claims handling and how coverage and exclusions for riots, strikes, civil commotions and terror will be interpreted under the policies they have issued.

At the end, the target should be for the insurance industry to be seen as reacting swiftly and professionally for all parties involved.

Foreign insurers

Cahit Nomer: Foreign-capitalised companies control more than 70% of the Turkish market. To what extent have they had a positive influence?

Çetin Alanya: International companies are coming to Turkey because they see growth potential. They are not coming to make profits in the initial stage of roughly three to five years. They come to grow because they come from saturated markets with very low growth potential – 1% or 2%. When they come here, they can grow by between 8% and 10%. For one large international company, Turkish premiums made up 5% of their total. That is an important part of a big company, however, in terms of 2009 profits Turkey only accounted for 0.5% of that company.

Jürgen Brucker: We are of the opinion that the influx of international companies spurred the further development of the Turkish market, especially when you look at improvements to the IT infrastructure and other features, and also in connection with certain products which had their origin in the UK or other countries.

It also increased competition and put a lot of pressure on local companies. However, one could say this also spurred further positive developments in local Turkish insurance companies.

Hulki Yalçin: Maybe in a couple of years some of the entrants will start to question themselves and ask whether they are doing the right thing because of the lack of profit. At that point there may be a reduction in numbers, maybe though mergers or maybe through withdrawals.

You cannot survive in a market where you are continually making technical losses. Turkey is a very promising market in other senses and also geographically a very important location. But, personally, right now I believe in terms of international investors we are reaching another level, because with this level of profitability it is not sustainable.

Cahit Nomer: Are there any newcomers in the pipeline?

Ahmet Genç: Not as many as in 2006 or 2007. Between one and three.

Mustafa Su: As a local insurer and a Turkish citizen, I am more than welcoming of foreign investment in Turkey. But I think the expectations were in a sense naïve because many of our colleagues were expecting more disciplined price premium levels.

However, the international companies buying shares of medium-sized companies have tried to maintain the market share and those buying smaller companies have tried to increase theirs. The way to do this is price competition. It is a vicious circle, and after all those years we are still speaking about price levels that are not in harmony with the technical realities.

Muzaffer Aktaş: I share Mustafa Su’s view that foreign investors are most welcome. But I also share everybody’s disappointment about international companies’ way of functioning in Turkey. They had expertise and knowledge, and they knew this country was missing out in personal lines. We were expecting them to come in and educate insurance companies and tell them, ‘this is how you should operate. Let’s do it together’. GR

Milli Re

Milli Re was established in 1929 to run the reinsurance monopoly in order to prevent foreign currency outflow, and has successfully achieved this main purpose. In addition, Milli Re has provided considerable support to the development of skills in the Turkish market, to training and educational activities, as well as providing a permanent revenue stream to the Treasury.

After the abolition of the compulsory cession, Milli Re has been acting as a free market reinsurer, and has climbed up to the main position in the market by making the best use of its status as the single local reinsurer. As at 2011 renewals, Milli Re has maintained its position by keeping its 25% share in the reinsurance market and leading the majority of the proportional reinsurance programmes which are currently being employed by most of the insurance companies in the Turkish market.

The continuing intense competition among the insurance companies remains the major cause of adverse effects on the technical results. On the other hand, the Turkish insurance market has produced nearly TRY14bn ($8.8bn) in total in 2010-11. This represents 13.5% increase as compared to the previous year due to economic recovery from the second half of 2010 and some recently introduced compulsory liability insurance policies. This positive trend is expected to carry on in 2011 and the following years.

Foreign capital inflow, which halted during the economic crisis in 2009, revived in 2010, with the acquisition of two locally capitalised companies in the market. This trend will naturally increase the foreign share in total paid-up capital which currently accounts for 50%, and foreign increase in control of premium which currently accounts for 60%.

This gradual increase of foreign share in the insurance market has not affected Milli Re's share in the local reinsurance market. Milli Re is leader in the majority of proportional treaties and participates in nearly all the cat programmes in Turkish companies: not only in Turkish standalone cat programmes but also some global cat programmes of foreign capitalised companies. There is no concern about Milli Re's strong position in the future.

Milli Re continues to hold 25% of the local reinsurance market and 20% of its total premium income is generated from overseas. From this point of view, while Milli Re is known as a local reinsurance company, its portfolio consists of risks from all over the world.

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The Turkish market has suffered as a result of fierce competition and lower interest rates. This was reflected in the results published by Turkish companies in 2010. On the other hand, Turkey has managed to weather the storm of the global financial crisis and emerge in relatively good shape.

On the insurance front, the premium volume has grown by 11.9% from $8.4m in 2009 to $9.4m in 2010. Life, health and pension insurance are the branches which are most likely to grow going forward. There is also a huge potential for personal lines. Currently, the premium per capita and insurance penetration as a percentage of GDP remain very low at $128 and 1.28%, respectively. This, coupled with a young population who possess aspirations and the ability to adapt, presents a sizeable opportunity for growth.

The use of catastrophe and financial modelling is well established within the Turkish insurance market, with RMS being the most popular model used. Turkish companies are legally required to buy up to 1-in-250-year event cover. In addition, adherence to existing tariffs for earthquake, strike riots and civil commotion (SRCC) and terrorism is required under pro rata treaties. The dynamic Insurance Directorate keeps insurance legislation on a par with EU countries and Turkey is keen to implement Solvency II in 2012.

Willis Re prides itself on being the largest reinsurance broker in Turkey, with over half the market share. It offers global resources and local delivery.

For more than 100 years, Willis Re has proudly served its clients, helping them obtain better-value solutions and make better reinsurance decisions. As one of the world's premier global reinsurance brokers, with 40 locations worldwide, Willis Re provides local service with the full backing of an integrated global reinsurance broker.

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Anadolu Sigorta

Established in 1925, Anadolu Sigorta today retains its market position as the most prominant locally capitalised insurance company in Turkey. In its 86 years of history, the company has lived through many phases of the evolving Turkish insurance market, always keeping its pivotal position.

Aspiring since its foundation to provide a world-class service to the local market, the company has a sound financial position, an extensive sales network and has heavily invested in technology and human resources. As a result, Anadolu is the first name that comes to the mind when one thinks of insurance companies in this part of the world. Our brand name is one of our most valuable assets.

We consider ourselves as working in a very competitive market that is also very demanding. Throughout the years we proved to not only be able to live in such an environment but also do so profitably while increasing our already sizeable market share. While there are many technical aspects of insurance, we believe, the essence is to be 'closer to the customer' than our competitors. Our organisation and machinery are all tuned around this simple philosophy.

We have a good reason to do so: Although many in the industry would define the Turkish insurance market simply as one that is characterised by price competition, there is much more to say about it. As the Turkish economy grows rapidly, our customers have increasingly more complex demands that need innovative solutions. We can say this not only for corporate risks but also on personal lines. A company that is responsive to the customer demands, that can serve their customers promptly will have the ingredients to succeed.

Today Anadolu Sigorta has 11 branch offices and approximately 3,500 agencies all throughout Turkey and Northern Cyprus. This extensive sales network is key in our aspiration to be closer to our customers. In addition, Anadolu Sigorta has an online sales channel.

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Catlin Group

Catlin Group Ltd. is an international specialist insurer and reinsurer, writing more than 30 classes of business. Catlin's overriding aim is to help realise the ambitions of our clients through the development of imaginative and effective risk management solutions.

Catlin operates six underwriting hubs, allowing the group to provide insurance and reinsurance underwriting expertise on a local basis worldwide: London/UK (which includes Catlin's operations at Lloyd's of London, where the Group owns and operates the largest syndicate), Europe, Bermuda, the US, Asia-Pacific and Canada. The Group wrote a total of $4.1bn in gross premiums in 2010.

The geographic spread provided by the hubs allows Catlin to write a highly diversified portfolio of insurance and reinsurance, both by country of origin and by class of business.

Catlin Europe

Catlin Europe, Catlin's European underwriting hub, underwrites both insurance and reinsurance classes of business. The hub is present in Austria, Belgium, France, Germany, Italy, Norway, Spain and Switzerland.

Insurance

Catlin's European offices underwrite commercial and industrial insurance business as well as facultative reinsurance in the following product lines: Aquaculture, Aviation, Construction and Engineering, Directors' and Officers' Liability, Financial Institutions, Energy, Equine, Film / Event, Fine Art / Specie, Liability, Livestock, Marine, Personal Accident, and Political Risks / Terrorism.

For insurance clients, Catlin Europe's ambition is to provide excellent risk management solutions and superior service through a professional broker network. Business is underwritten on behalf of the Catlin Syndicate at Lloyd's (Syndicate 2003) and Catlin UK (Catlin Insurance Company (UK) Ltd.) through owned coverholder arrangements, managed within the context of Catlin's group-wide underwriting and claims procedures and controls.

Reinsurance

Catlin Europe's reinsurance operations are led by Catlin Re Switzerland, headquartered in Zurich.

Property, Casualty and Specialty classes are underwritten with a focus on clients based in the Continental and Southern European market as well as the Nordic region. Catlin Re Switzerland offers proportional as well as non-proportional catastrophe, risk and aggregate covers.

Trade Credit, Surety Bond and Political Risk Reinsurance are underwritten by Catlin Re Switzerland on a global basis with the centre of competence being Zurich.

European reinsurance business is also underwritten by the Catlin Syndicate at Lloyd's (Syndicate 2003) and Catlin UK (Catlin Insurance Company (UK) Ltd.).

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Words of wisdom

‘I share everybody’s disappointment about international companies’ way of functioning in Turkey’

Muzaffer Aktaş, Willis Re

‘I see an increasing trend where premiums are not retained in the market and are going out via brokers’

Ertan Firat, Aviva Sigorta

‘You cannot survive in a market where you are continually making technical losses’

Hulki Yalçin, Milli Re

‘People deem the state as the father of the nation and so expect everything from it’

Mustafa Su, Anadolu Sigorta

‘Premium production increased in 2010, but in terms of technical profitability we are no better off’

Ahmet Genç, Turkish Treasury

‘Players who want to improve their underwriting profitability through higher retentions need to be very careful’

Kerim Tarman, Catlin

‘The Turkish market depends on international as well as local reinsurance support’

Jürgen Brucker, Munich Re

‘Insurance as a percentage of GDP is getting smaller instead of larger’

Çetin Alanya, Dubai Group Sigorta

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