FINANCIAL STABILITY AND ITS DETERMINANT OF ISLAMIC INSURANCE COMPANY, CASE STUDY INDONESIA VIS-A-VIS MALAYSIA



UNDERGRADUATE THESIS

SUBMITTED TO FACULTY OF ISLAMIC ECONOMICS AND BUSINESS OF ISLAMIC STATE UNIVERSITY OF SUNAN KALIJAGA YOGYAKARTA IN PARTIAL FULFILLMENT OF THE REQUIREMENTS FOR THE STRATA ONE DEGREE

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2022

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UNDERGRADUATE THESIS' APPROVAL

Subject: Undergraduate Thesis by Alfi Febriany

То

The Honorable Dean of Islamic Economics and Business of Islamic State University Sunan Kalijaga In Yogyakarta

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Assalamualaikum Wr. Wb.

After going through proofreading, examining, giving direction and correcting, also making necessary improvements, thus I, as a Supervisor, reckon that undergraduate thesis by following student:

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Thesis' title :"Financial Stability and Its Determinant of Islamic Insurance Company, Case Study Indonesia Vis-a-vis Malaysia"

has deserved to be submitted to the Faculty of Islamic Economics and Business, Islamic Finance and Management Department, Islamic State University of Sunan Kalijaga Yogyakarta, as partial fulfillment of the requirements for the degree of bachelor of economy.

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UNA

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DECLARATION OF ORIGINALITY

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Certify that this thesis under the title **"Financial Stability and Its Determinant** of Islamic Insurance Company, Study Case Indonesia Vis-a-vis Malaysia" to the best my knowledge, my thesis does not upon anyone's copyright nor the work of other people which has been accepted for the any other degree or diploma in any university, except where due reference is made in the text of thesis. I hereby conclude my declaration with utmost sincerity.

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APPROVAL OF THESIS PUBLICATION FOR ACADEMIC PURPOSES

As an academic of State Islamic University of Sunan Kalijaga Yogyakarta,I, unsersigned below:NameStudent NumberStudent Number: 16830029DepartmentFaculty: Islamic Finance and ManagementFaculty: Islamic Economics and BusinessType of Research: Undergraduate Thesis

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Alfi Febriany NIM. 16830029

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PAGE OF MOTTO

AS MUCH AS IT SEEMS DIFFICULT AT THE TIME, THERE IS ALWAYS PARADISE IN THE DISTANCE-B.I

YOU WILL HAVE A BAD TIMES BUT IT WILL ALWAYS WAKE YOU UP-K.J.H.



PAGE OF DEDICATIONS

I dedicate this thesis to all families who lose their loved ones because of Covid–19 and to all class 2020–2021 who are still pursuing their dream until now. We are here together.



LATIN ARABIC TRANSLITERATION

The transliteration of Arabic words in this research refers to the regulations of Ministry of Religion and the Ministry of Education and Cultural Republic of Indonesia, number 158/1987 and 0543b/U/1987.

A. Single Consonant

Arabic	Name	Latin Letters	Name
words			
1	Alif	Not Symbolized	Not Symbolized
ŀ	Ba'	В	Be
ប	Ta'	T	Te
ث	Sa'	ś	Es
			(with the point above)
હ	Jim	J	Je
7	Ha'	h	На
	In		(with the point below)
SIAIE I	Kha'	C UN Kh EKSI	Ka and ha
SUNA	Dal	ALDJAC	De
YOC	DZal	KAżRT	xet (with the point above)
J	Ra'	R	Er
j	Zai	Z	Zet
س	Sin	S	Es
ش	Syin	Sy	Es and ye

ص	Sad	Ş	Es
			(with the point below)
			De
ض	Dad	ģ	(with the point below)
			Te
ط	Ta'	ţ	(with the point below)
			Zet
ظ	Za'	Ż.	(with the point below)
3	''Ain		Converted comma
			above
Ė	Gain	Gh	Ge and ha
ف	Fa'	F	Ef
(å	Oaf	0	Ki
ك	Kaf	К	Ка
J	Lam	L	El
4	Min	М	Em
SJATE	S Nun	C UNIN/ERSIT	En
SIN	XXI		
JUIN	Wawu		We
Y O C	Ha'	K AHR T	На
Ş	Hamzah	6	Apostref
ي	Ya'	Y	Ye

B. Double Consonants for Shaddah Written in Multiple

متعدّدة	Written	Muta'addidah
عدَة	Written	ʻiddah

C. Ta'Marbuttah

All *ta 'marbuttah* are written with h, both in a single word or in the middle of a combination of words (words that are followed by the article "al").

حكمة	Written	Hikmah
2 عنة	Written	ʻillah
كرمةالآولياء	Written	Karamah al auliya'

D. Short Vowels and their application

ó	Fatha	Written	А
STATE	Kasra	Written	Ι
Stón	Dhammah	Written	A ^U
فعل O	Fatha	Written	Fa'ala
ذکر	Kasra	Written	Zukira
يڏھب	Dhammah	Written	Yazhabu

E. Long Vowels

1. fatha + alif	Written	А
جاهليّة	Written	Jahiliyyah
2. fatha + ya' saakin	Written	А
تنسى	Written	Tansa
3. kasra + ya' saakin	Written	Ι
کريم	Written	Karim
4. dhammah + wawu saakin	Written	U
فروض	Written	Furud

F. Complex Vowel

1.	fatha + ya' saakin	Written	Ai
	بينكم	Written	Bainakum
2.	fatha + wawu saakin	Written	Au
	STATE ISL/	Written	Q <mark>aul</mark>
	SUNAN	I KALIJA	GA

G. Consecutive Short Vowels in One Word Separated with Apostroph

		II. 7 W.
اانتم	Written	a'antum
أعدّت	Written	u'iddat
لننشكرتم	Written	la'in syakartum

H. Said Alif+Lam

1. If followed by the *qamariyyah* letter, it is written using the initial letter "*al*"

القرآن	Written	Al-Quran
القياس	Written	Al-Qiyas

2. If the *Syamsiyyah* letter is followed, it is written according to the first letter

of the Syamsiyyah

الستماء	Written	As-sama'
الشَّمس	Written	Asy-syams

3. Writing Words in Sentences

Written according to the writer

الفروض ذوي	Written	Zawi al-f <mark>urud</mark>
الستنة أهل	Written	Ahl as-su <mark>nnah</mark>
STATE ISLA	MIC UNIVE	RSITY
SUNAN	KALIJ	AGA
YOGY	AKAR	ΤΑ

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GYAKA

Yogyakarta, December 22nd 2021 The Author

Alfi****Febr

NIM. 16830029

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ABSTRACK

This study examines the determinant factors of the financial stability of Islamic life insurance in Indonesia and Malaysia. The analysis covers Islamic life insurance companies or Takaful that operated in Indonesia and Malaysia from 2014 to 2019. The Z-score measures financial stability as the dependent variable. In contrast, the independent variables will be divided into insurance-specific factors (internal factor) and the country's economic scale (external factor). This research employs company-specific ratio analysis, such as return on equity (ROE), investment income ratio, reinsurance ratio, premium growth, and underwriting ratio as internal factors. The GDP growth, interest rate, and market share are the external factors to employ the country's economic scale. This study uses dummy regression to examine the difference between Malaysia and Indonesia insurance stability. Then, panel regression is used to understand the factors influencing Islamic insurance stability. This finding shows no difference in financial stability on Islamic life insurance in Indonesia and Malaysia. The findings reveal that the stability of Indonesia (significant at 0.1) and Malaysia (significant at 0.05) insurance companies is positively affected by return on equity (ROE). The reinsurance ratio plays an essential factor that negatively affects the stability of Islamic life insurance in Indonesia (significant at 0.05). Investment income has a positive effect on financial stability in Indonesia at a significant level of 0.1. The underwriting ratio has a significant negative impact at a 10% level in Indonesia Islamic life insurance stability. The interest rate also positively affects Indonesia Islamic life insurance stability at the 1% level.

Keywords :Islamic life insurance companies, financial stability, insurance specific factors, macroeconomics, Indonesia and Malaysia.

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ABSTRAK

Penelitian ini bertujuan untuk menganilisa faktor yang mempengaruhi stabilitas keuangan asuransi syariah di Indonesia dan Malaysia. Penelitian ini menganilisa perusahaan asuransi jiwa syariah atau Takaful yang beroperasi di Indonesia dan Malaysia pada periode 2014 sampai 2019. Stabilitas keuangan (Z-score) digunakan sebagai variabel dependen, sedangkan variabel independen akan dibagi menjadi dua kelompok yaitu faktor spesifik perusahaan asuransi (faktor internal) dan makroekonomi (faktor eksternal). Penelitian ini menggunakan analisis rasio return on equity (ROE), rasio pendapatan investasi, rasio reasuransi, pertumbuhan premi, dan rasio underwriting sebagai faktor internal. GDP, suku bunga dan market share sebagai faktor eksternal. Penelitian ini menggunakan regresi dummy untuk meganalisis perbedaan stabilitas keuangan pada kedua negara, Indonesia dan Malaysia. Selanjutnya, regresi panel digunakan untuk mengetahui faktorfaktor yang mempengaruhi stabilitas keuangan asuransi syariah. Hasil penelitian menunjukan tidak ada perbedaan stabilitas keuangan perusahaan asuransi syariah di Indonesia dan Malaysia. Hasil penelitian menunjukkan bahwa stabilitas perusahaan asuransi Indonesia (signifikan pada level 0.1) dan Malaysia (signifikan pada level 0.05) dipengaruhi secara positif oleh return on equity (ROE). Rasio reasuransi merupakan faktor penting yang berpengaruh negatif pada perusahaan asuransi jiwa syariah di Indonesia (signifikansi 0.05). Rasio pendapatan investasi memiliki pengaruh terhadap stabilitas keuangan di Indonesia secara positif signifikan pada level 0.1. Rasio *underwriting* menunjukan pengaruh negatif signifikan pada level 10% pada stabilitas asuransi jiwa syariah di Indonesia. Suku bunga juga berpengaruh positif terhadap stabilitas asuransi jiwa syariah Indonesia pada level signifikansi 1%.

Kata kunci : perusahaan asuransi jiwa syariah, stabilitas keuangan, faktor spesifik asuransi, makroekonomi, Indonesia dan Malaysia.

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CHAPTER I

INTRODUCTION

A. The Background of Study

Businesses and individuals use insurance to reduce the risk that may occur. Insurance is used as a form of risk management to protect against losses. Insurance as financial intermediation enhances a country economically. Today, several countries operate two types of insurance, which are conventional and Islamic insurance (*Takaful*). Islamic insurance is one of the Islamic financial instruments. Islamic insurance, or *Takaful*, has different terms than conventional insurance in the concept and contract employed (Ali et al., 2015). There are several contract types of *Takaful*, such as *Wakalah*, *Mudarabah*, and *Wakalah-Mudharabah* (hybrid contract). Then, the funds are managed under the chosen arrangement.

Thus, in Takaful, the policyholders act as muwakkil or mudharib regarding the chosen agreement. The Wakalah model, an agent-principal agreement, has a mechanism where the *Takaful* operator is the agent to manage policyholder' funds (capital principal). Hence, the Takaful operator earned a fee for the service rendered. In the Mudharabah contract, the policyholders, known as mudarib, are joint investors. The Takaful operator is the manager who manages the funds from policyholders. Then, policyholders and Takaful operators share the investment pool's profit and losses. A hybrid contract is the modified combination of Wakalah and Mudharabah (Rahman et al., 2011). This model allows the *Takaful* operator to have both a *wakalah* fee and profit-sharing from the investment activity.

Islamic insurance uses a concept where several people share a mutual risk through contributions (an amount of fund from policyholders) to bear financial losses. Meanwhile, conventional insurance uses a transfer risk model. This model in conventional insurance requires the company to bear all the risks that occur since the funds are recognized as the company's revenue. Islamic financial institutions need to follow the regulations and the *sharia* concept to maintain their business activities.

Islamic finance has been developing significantly. However, many studies focus more on banking and almost neglect another vital sector, Islamic insurance. Based on the IFDI Report in 2020, it can be seen that *Takaful* only reached 2% of assets compared to the other IF instruments.



Chart 1.1 Sectoral Composition of Islamic Finance Assets

Source: IFDI Report, 2020.

Chart 1.1 above shows that Islamic banking has the most extensive assets with 69%, followed by *Sukuk* with 19%, Islamic funds with 5%, other Islamic funds with 5%, and *Takaful* has the minor assets with 2%. Even though the *Takaful* asset penetration is still lower than the others, the Islamic insurance market has reached several regions, such as Southeast Asia (ASEAN), Gulf Cooperation Council (GCC) countries, Africa, and others.

Chart 1.2 *Takaful* Compound Annual Growth Rate by Regions (in 2017)



Source: IFSB Report, 2019.

Based on Chart 1.2, in 2017, Africa has reached the highest growth, with 19%, followed by GCC countries which reached 18%, other counties at 7%, and Southeast Asia at -4%. Several countries are trying to promote Islamic financial institutions to the current conventional industry, including Southeast Asia. Among ASEAN countries, Indonesia and Malaysia are the pioneers in Islamic finance. Indonesia's first Islamic insurance was established in 1992. In Malaysia, *Takaful* was introduced in 1984, while in Brunei Darussalam in

1993. Indonesia and Malaysia are the leaders in Islamic finance with a high number of customers, assets, and growth, especially in Southeast Asia.

Indonesia and Malaysia are neighboring nations that are actively pursuing economic cooperation. Both countries agreed on financial cooperation to strengthen bilateral relations. Indonesia and Malaysia also continue to cooperate in developing Islamic finance. Those regional agreements facilitate the movement of IF. Based on the IFSI Stability Report in 2019, Indonesian Islamic insurance is worth USD 972 million, and Malaysian Islamic insurance is worth USD 2.77 billion. These differences reflect the different growth between the two countries.



Chart 1.3 Takaful Growth in South-East Asia

Over the period 2012 to 2015, Indonesia's Islamic insurance tends to increase per year. Meanwhile, Malaysia's Islamic insurance tends to decrease per year from 2012 to 2015, and Brunei's Islamic insurance over the period 2012 to 2015 remains at 5%.

On the other hand, previous research by Abduh and Omar (2012) revealed that conventional insurance in Malaysia is more efficient than the *Takaful* industry in both ratio analysis and data envelopment analysis. Even though Indonesia's *Takaful* growth is still lower than Malaysia's, a study by Ghaisani (2018) found that the *Takaful* industry in Indonesia is more efficient than conventional. In Brunei, a significant majority prefers *Takaful* over conventional insurance (Bashir et al., 2011).

Default probability has attracted a great deal of attention since life insurance has been reported to have a long list of failures in the 1980s, including in Europe, Japan, and the U.S. (Caporale et al., 2017). Indonesia has also reported some defaults by insurance companies. Latest, the following defaulted insurance carriers in Indonesia, such as PT Asuransi Jiwasraya Persero, PT Asuransi Jiwa Bakrie Life, and Asuransi Jiwa Bumiputera 1912. Malaysia also reported the insolvency case of Mercantile Insurance Berhad in 1993. The financial crisis during 2007-2008 proved that major insurers could be the source of financial fragility and systemic risk (Baluch et al., 2011). It means the insurance failure may endanger the financial industries. Insurance is one of the intermediaries and a strong driver of economic development since it plays an essential role as the primary risk management tool for companies and individuals.

A default can happen because of uncertainty and risk that comes unexpectedly. A company requires the initiative to manage its risk. Islamic insurance companies are susceptible to financial problems that can cause bankruptcy because insurance is a service that engages in risk management. Companies need to understand their financial condition early to anticipate and manage unexpected risks. An Islamic insurance company can minimize the risk by using financial analysis techniques given by regulators and boards.

Risk mitigation is essential for insurance companies because it can occur at any time. This early mitigation is vital for the financial health of the company. IFSB has guided the compilation and dissemination of production and structural Islamic financial indicators. There are several indicators of the *Takaful* industry, such as capital adequacy, the quality of assets, retakaful and actuarial, management soundness, profitability, and liquidity.

Insurance and banking are the intermediary institutions. Unlike banks, insurance companies do not receive deposits, so they are less exposed to the risk of sudden liquidity that may lead to bank runs (Caporale, 2017). Meanwhile, insurance companies receive premiums or contributions from policyholders to bear the risk together. Insurance should manage the funds effectively to indemnify the financial loss of the policyholders. The financial stability of insurance can be a sign that insurance has the ability to provide good service and management.

Thus, it is essential to investigate the stability of insurance companies. This research extends the theory to research that focuses on insurance companies with various variables that drive the soundness of insurance. The Zscore, a financial stability measure, is used to investigate the financial stability of Islamic life insurance companies in Indonesia and Malaysia. The Z-score is an accounting-based measure of the distance to default (Pasisouras & Gaganis, 2013). At first, Boyd and Graham (1986) conducted research using the Z-score to assess banking risk. The banking sector has widely used the Z-score for estimating bank risk, and several studies reveal that this measure may be a valuable tool for the insurance sector as well.

The Z-score is applicable when dealing with unlisted and listed entities. Since Islamic insurance companies in Indonesia and Malaysia are mostly unlisted, the Z-score is the most suitable tool to measure insurance companies' soundness. This method does not require market-based risk measures like the Merton model. Unlike in the banking sector, the research on insurers' financial stability is not extensive. However, several studies have employed an accounting-based measure of the Z-score formula to estimate insurance stability, such as Shim (2011), Pasiouras and Gaganis (2013), Cummins et al. (2017), Kramaric et al. (2019), and Misas (2020).

Research by Kramaric (2019) on financial soundness using Z-score found that insurers' size positively affected the soundness of Croatian insurers. Reinsurance is statistically significant and positive for financial stability in Hungary and Poland. Chen and Wong (2004) research found that premium growth does not affect financial health. Life insurers' financial health is significantly affected by the size, change in asset mix, investment performance, and product mix.

A study by Kim et al. (1995) found that insolvency is positively and significantly affected by the premium's rapid growth. This research also found

a significant and negative effect of investment performance on insolvency, while the underwriting result variable is positive and significant. Reinsurance also statistically has a significant and positive impact on insurer insolvency.

Shim (2017) research on financial stability in U.S. property-liability insurance revealed a negative relationship between underwriting and reinsurance on an insurer's financial stability. The result revealed that interest rates have a positive impact on stability. This study also discovered that mutual, product, and geographical factors positively affected the insurance stability. The research also indicates that higher premium growth without a corresponding policyholder surplus may jeopardize insurance stability.

Research by Cummins et al. (2017) indicated that the soundness of the EU life insurance markets is affected by the competition. However, the soundnessenhancing effect of the competition is more significant for weak insurers than for healthy ones. Research by Caporale et al. (2017) revealed several conditions connected to the insolvency risk of insurance firms, such as credit quality, counterparty risk through reinsurance, and the direct default risk when firms' liabilities are higher than assets.

This study examines two main research questions. First, this study analyzes the differences in financial stability (Z-score) between Indonesia and Malaysia. Second, investigating the determinant effect of insurance-specific factors and economic variables on financial stability. The fundamental objective is to assess whether the economic variables alongside a company's financial conditions can investigate the insurance company's stability. Accounting information plays a crucial role in identifying vulnerabilities, thus offering predictability (Mubarak, 2012). It means that financial ratios remain the critical vulnerability indicators in any company. Financial ratios are the basis for answering some essential questions regarding the health of companies.

On the other hand, risk exposure depends on the company's internal factors and general economic condition. According to Keasey and Watson (1987), an adequate model could not be based solely on financial ratios. The study implies that economic variables are also essential in predicting corporate failure. The insurance failure may accelerate the entire financial industry, harming the real sector and likely hastening the default.

Because of the importance of insurance stability, analyzing the condition of insurance is essential since insurance often has a close link to banks and other financial institutions. Life or health insurance characteristics differ significantly in operations, investment activities, vulnerabilities, and duration of liabilities from general insurance (Brocket et al., 1994). Life insurance contributes to the safeguarding of a stable household. Life insurance acts as a financial intermediary, while general insurers are risk-takers (Chen & Wong, 2004).

This study aimed to analyze the determinants of financial stability for Indonesia and Malaysia *Takaful* life companies rather than general companies. The differences between general and life *Takaful* make it inappropriate to mix them. Thus, it is interesting to study the financial stability of Islamic insurance (*Takaful*) in Indonesia and Malaysia and the factors that may associate with the stability.

The macroeconomics are external factors employed to determine Takaful stability in Indonesia and Malaysia. The company-specific ratio analysis includes internal factors, such as return on equity (ROE), investment income ratio, reinsurance ratio, gross premium growth, and underwriting ratio. The financial stability (Z-score) is the dependent variable. In contrast, the independent variable will be divided into specific insurance factors (internal factors) and the country's economic scale (external factors). Hence, this study aims to investigate the financial stability of Islamic Insurance or Takaful in Indonesia and Malaysia from 2014 to 2019 under the title "Financial Stability and Its Determinant of Islamic Insurance Company, Case Study Indonesia Vis-a-Vis Malaysia."

B. Research Questions

Based on the background above, the formulation of the issues raised in this research are: ATE ISLAMIC UNIVERSITY

- Does any difference between the financial stability of Islamic life Insurance companies in Indonesia and Malaysia?
- 2. Does the return on equity (ROE) significantly affect financial stability?
- 3. Does the investment income ratio significantly affect financial stability?
- 4. Does the reinsurance ratio significantly affect financial stability?
- 5. Does growth in the gross premium significantly affect financial stability?
- 6. Does the underwriting ratio significantly affect financial stability?

- 7. Does Gross Domestic Product (GDP) growth significantly affect financial stability?
- 8. Does interest rate significantly affect financial stability?
- 9. Does market share significantly affect financial stability?

C. Research Objectives

Based on the formulation of the problem that the author has presented, the objectives of this study are:

- 1. To find out whether Indonesian Islamic Insurance financial stability is diverse with Malaysia *Takaful* companies.
- 2. To analyze the impact of the return on equity (ROE) on the financial stability of Islamic life insurance.
- 3. To analyze the impact of the investment income ratio on the financial stability of Islamic life insurance.
- To analyze the impact of the reinsurance ratio on the financial stability of Islamic life insurance.
- 5. To analyze the impact of growth in the gross premium on the financial stability of Islamic life insurance.
- To analyze the impact of the underwriting ratio on the financial stability of Islamic life insurance.
- To analyze the impact of GDP growth on the financial stability of Islamic life insurance.
- To analyze the impact of interest rate on the financial stability of Islamic life insurance.

 To analyze the impact of market share on the financial stability of Islamic life insurance.

D. Research Contributions

The research is expected to provide benefits to related parties in the form of:

- For the theoretical side: This research expects to increase scientific knowledge regarding the financial stability of Islamic Insurance in South East Asia, especially the primary country of *Takaful* penetration, Indonesia and Malaysia. As for the output, related parties such as companies and government agencies, in particular, can consider an insurance product's decision-making, company regulation, and others.
- 2. For the practical side:
 - a. For academics, this research is expected to explain the performance and factors determining the financial stability of Islamic Insurance in Indonesia and Malaysia. Therefore, it is expected to make a positive contribution to the previous researchers. FRSTY
 - b. For practitioners, this research is expected to reference parties, especially those dealing directly with Islamic Insurance companies.
 - c. For further research, this research can be used as a reference related to this topic.

E. Research Structure

This research consists of five chapters, and each chapter includes different topics as follows:

Chapter I, introduction contains the background of the problem of the study, objectives, benefits of research, and thesis structure. The background of this study presents the importance of the financial stability of Islamic Insurance in Indonesia and Malaysia.

Chapter II, in this chapter literature review contains the theoretical framework, literature review from the previous study and hypothesis of the study. Previous research helps determine research limitations and builds the research's base from several resources. The theoretical framework in this study supports the study and gives the theoretical ground for each variable.

Chapter III research methodology contains the research methods, data collection and resources, operational definition of variables, and data analysis techniques as an analytical instrument used to conduct the research.

Chapter IV research and discussion, chapter four discusses the result of data analysis that has been done using analysis tools and the research findings. The findings of the study are explained under discussion.

Chapter V conclusion and recommendation, this chapter contains the conclusions, limitations, and suggestions. The conclusion consists of a summary of the findings and analysis. The suggestions in this study include research implications, limitations, and suggestions for the upcoming study.

CHAPTER V

CONCLUSIONS AND SUGGESTIONS

A. Conclusions

This study shows that *Takaful* companies face changes in their stability due to changes in the insurance-specific factors and macroeconomic changes. Regulators, policymakers, and standard-setting are challenged to improve policies and procedures. Regulatory framework and *sharia* regulations need to ensure safe and stable insurance for the benefit and protection of *Takaful* members.

This study examines the insurer-specific internal variables and country's economic scale on the financial stability of Islamic life insurance in Indonesia and Malaysia. This finding shows no difference between financial stability on Islamic life insurance in Indonesia and Malaysia. Empirical findings answer the key determinants in ensuring a stable *Takaful* company. Firstly, return on equity (ROE) in both countries has a positive and significant impact on insurers' financial stability in Malaysia at the level 0.05 and Indonesia at the significant level of 10%, suggesting that the higher return are expected to be financially more stable.

Second, as Indonesia shows, those insurance companies that employ more reinsurance are exposed to counterparty risk or reinsurance insolvency. The finding on the reinsurance ratio reveals that reinsurance negatively influences financial stability at a significant level of 5%. The higher reinsurance shows a decrease in insurance stability. Third, the investment income positively affects the financial stability of Indonesia Islamic life insurance at the level of 10% (0.1), suggesting that the good management of investment activity contributed to the stability of Islamic life insurance. Fourth, the underwriting ratio measure by incurred claims to contribution shows negative effect and significantly at 0.1 level to insurance stability in Indonesia. Fifth, the findings specifically reveal that interest rate positively affects the financial stability in Indonesia *Takaful* at the level significant of 1%.

By recognizing the *Takaful* specific factors together with the nation's economic conditions might affect insurance stability, this study finds that reinsurance coverage and higher underwriting ratio (claims divided by contributions) might be a danger to the insurance company's financial stability. This finding also shows that the *Takaful* industry is positively affected by return on equity, investment income and interest rates. These findings could be used as an early warning to improve regulation based on country-specific features for insurance sector stability.

B. Research Limitations AMIC UNIVERSITY

Besides empirical findings from this study, the authors are mindful of its limitations that should be discussed in future research. This study only focuses on the insurance stability before the pandemic era. Limited variables and proxy variables used to measure financial stability. This study employs cross country data, Indonesia and Malaysia without employ the product diversification, *Takaful* board and regulation between two countries. Therefore, the difference in stability between the two countries was not found in this study.

C. Suggestions

The stability or soundness of an institution is a complex variable, and other measurements to examine the soundness of *Takaful* companies should be addressed in the forward study. Other aspects might need to be evaluated when examining its determinants, such as its capital requirements regulation, *sharia* regulation and countries specific regulation toward the *Takaful* industry. It is also valuable to explore stability determinants for life and non-life insurance. Furthermore, it might be essential to segregate the type of *Takaful* that is already full-fledged and *sharia* unit. Adding countries data, other insurance specific factors, and period (before and during pandemic) to the sample with another analysis and soundness approach might be helpful for following study to measure Islamic life insurance stability. Since, it is essential to understand insurance's risks at a particular period.

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