



REFLECTIONS ON LONG TERM QARD AL HASSAN IN TAKAFUL / RE-TAKAFUL

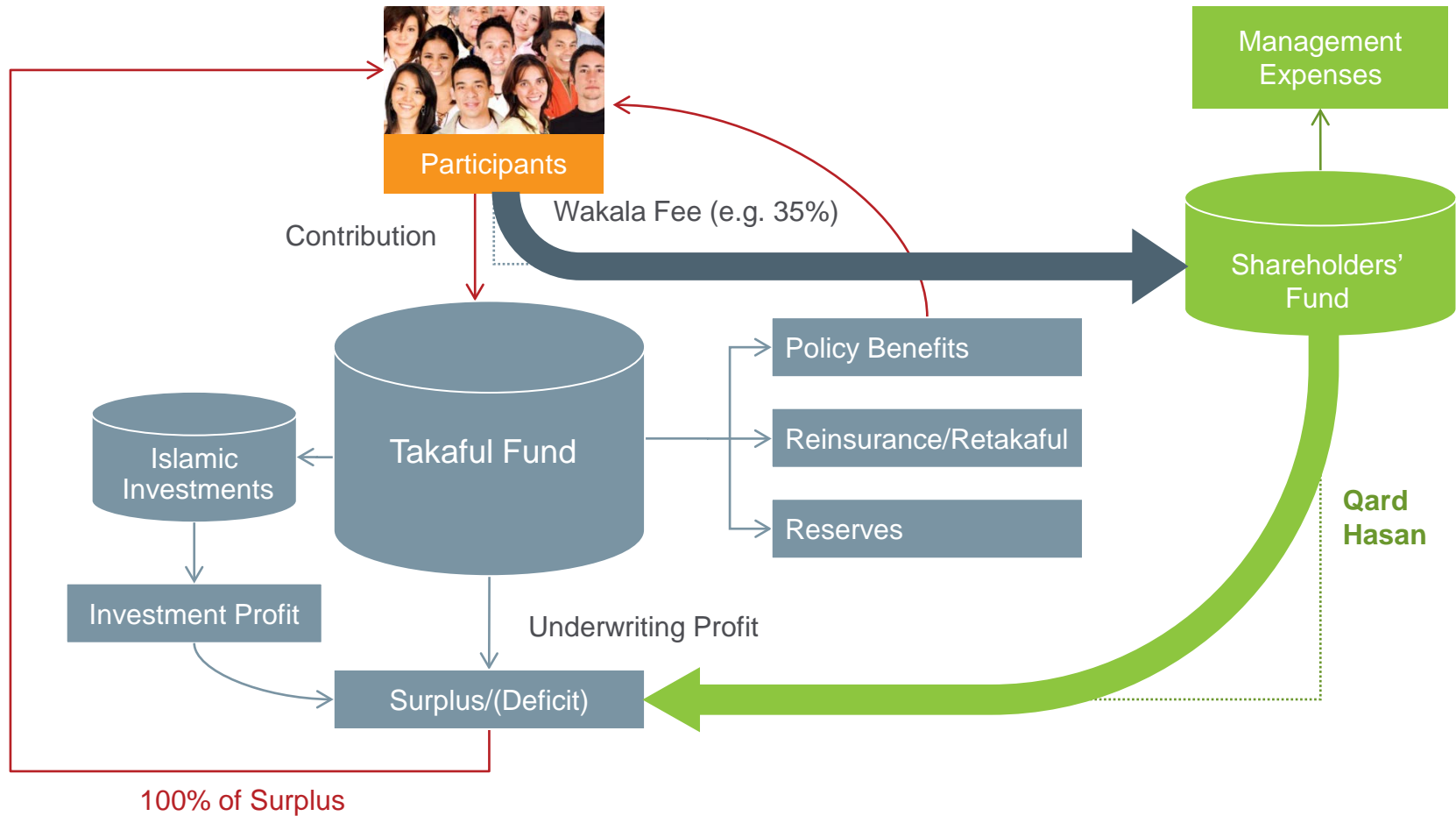
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Problems with Qard Hasan

- Breach of the risk sharing principle?
- Voluntary nature versus solvency effect
- Divergence of legal and economic nature (accounting)
- Cost of Capital

If Qard Hasan becomes more than marginal



Qard on frequency business which is not being repaid by future surpluses
(persistent qard)

Qard as element of pooling mechanism (solidarity qard)

Qard due to high severity/low frequency losses (volatility qard)

1. Reason for emerging of persistent Qard

What wakala fee/reserve would you suggest?

Conventional 2007	
Net Risk Premium	3.481.652,89
Claim Incurred	2.381.784,49
Technical Profit/loss	1.099.868,40
Loss Ratio	
RI	68%
Insurer	68%
Conventional 2008	
Net Risk Premium	1.504.789,39
Claim Incurred	1.179.877,65
Technical Profit/loss	324.911,74
Loss Ratio	
RI	78%
Insurer	78%
Conventional 2009	
Net Risk Premium	2.858.073,58
Claim Incurred	2.817.717,07
Technical Profit/loss	40.356,51
Loss Ratio	
RI	99%
Insurer	99%

1. Reason for emerging of persistent Qard



What wakala fee/reserve would you suggest?

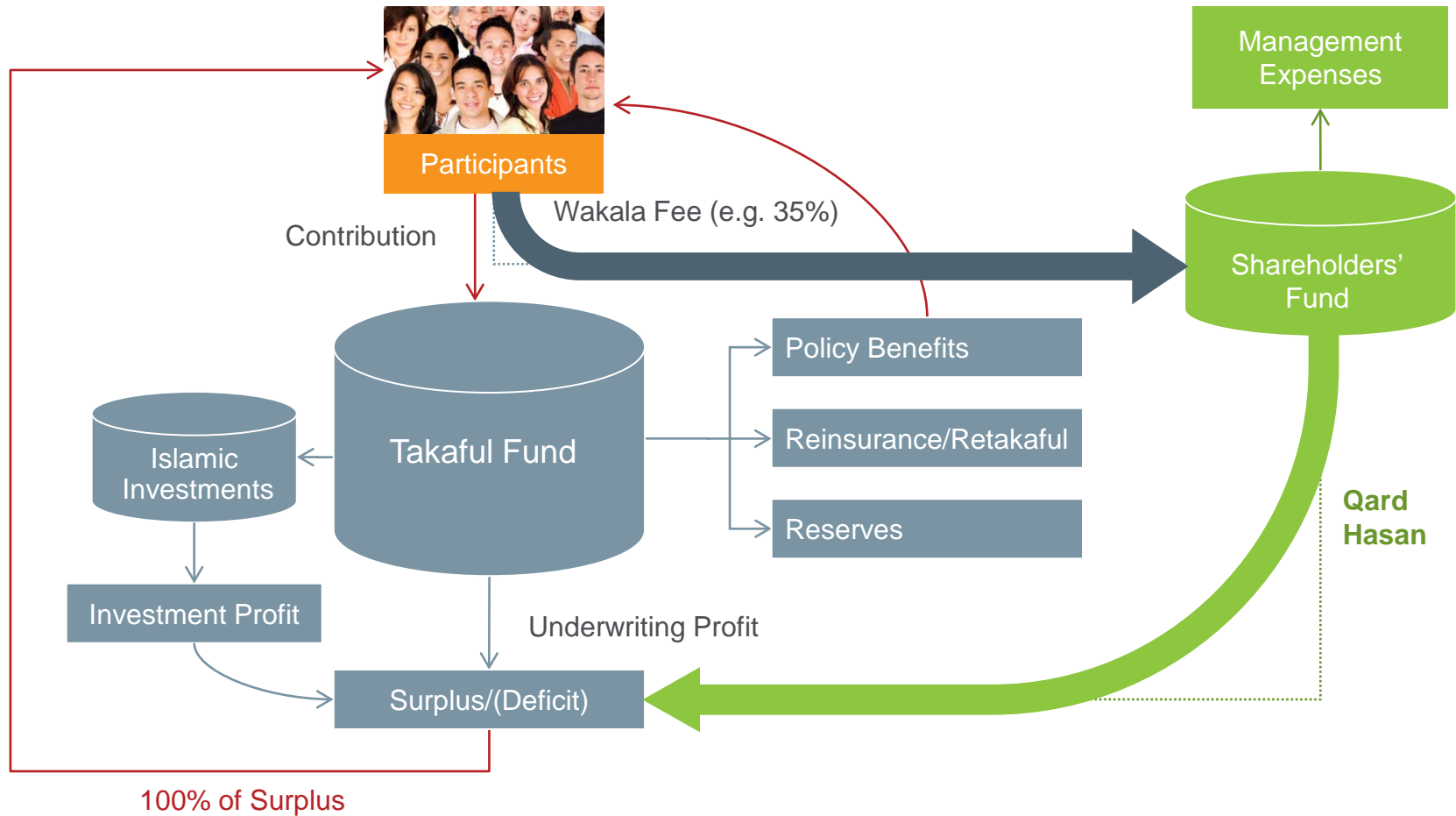
Average LR/CR: 81%

Minimum LR/CR: 68%

Required margin for retakaful operator: about 20%

Rationale of persistent qard: it is “produced” in order to avoid payment of surplus, which can in average not be sustained.

Reversing the effect on the wakala fee



2. “Solidarity Qard”

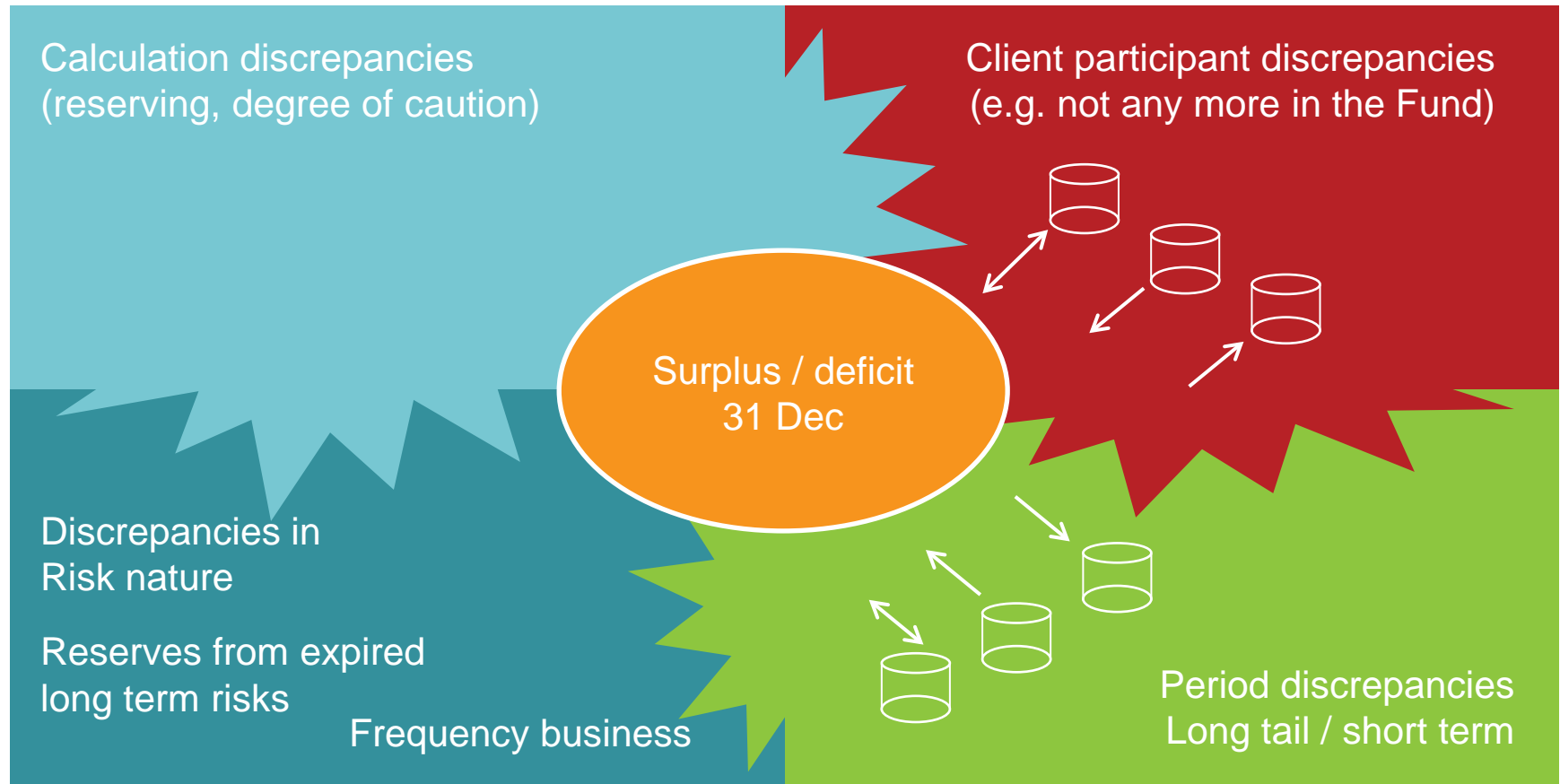
Requirement of scholars:

No surplus paid out to good risks as long as the overall fund is in deficit (i.e. Qard outstanding).

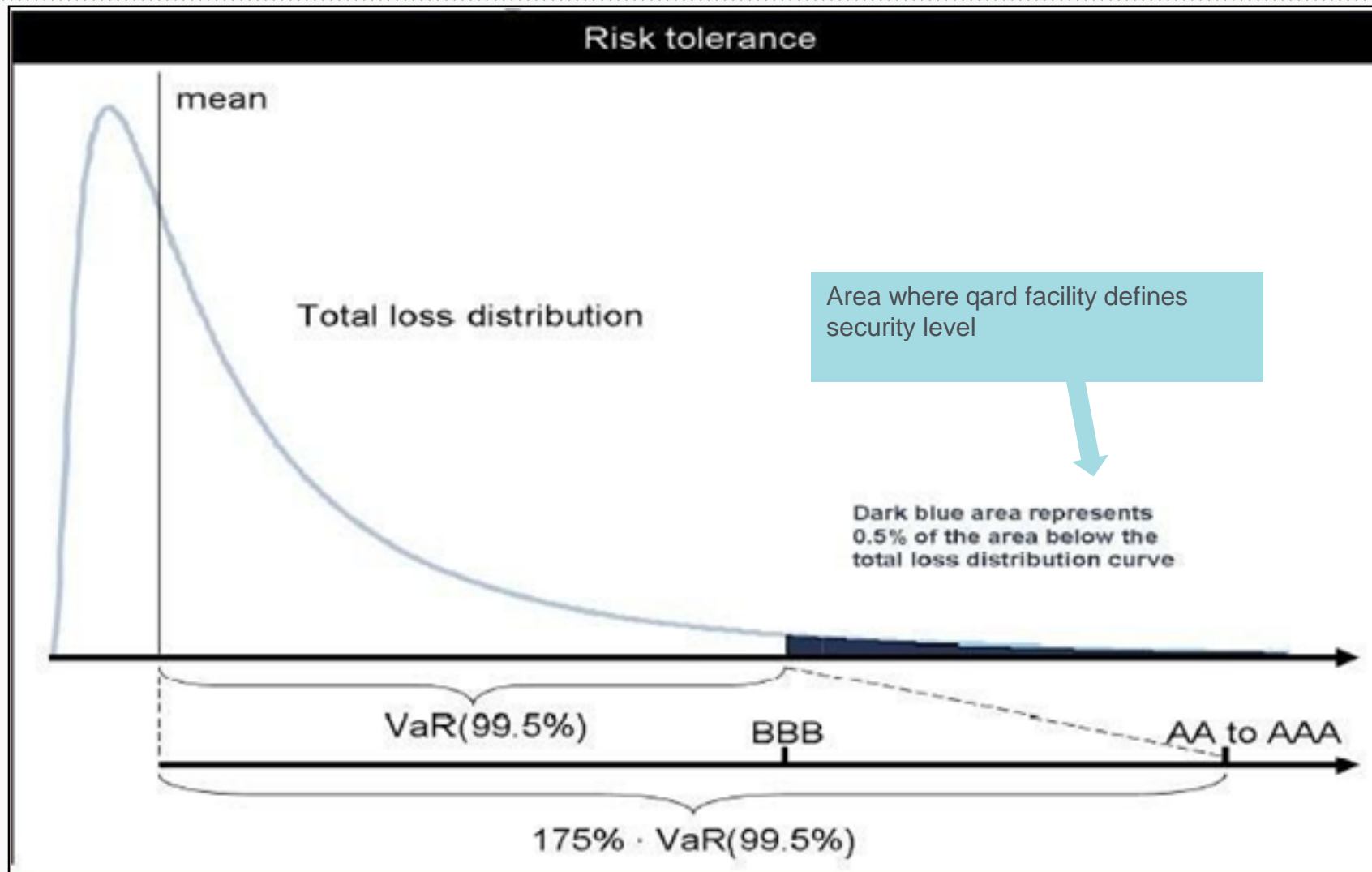
Qard: sum of contribution and investment income since inception exceeds outgo (losses, commission, wakala fee)

This seems simple, but does not pay tribute to the very different sources, reasons and periods from which deficits and surpluses can arise.

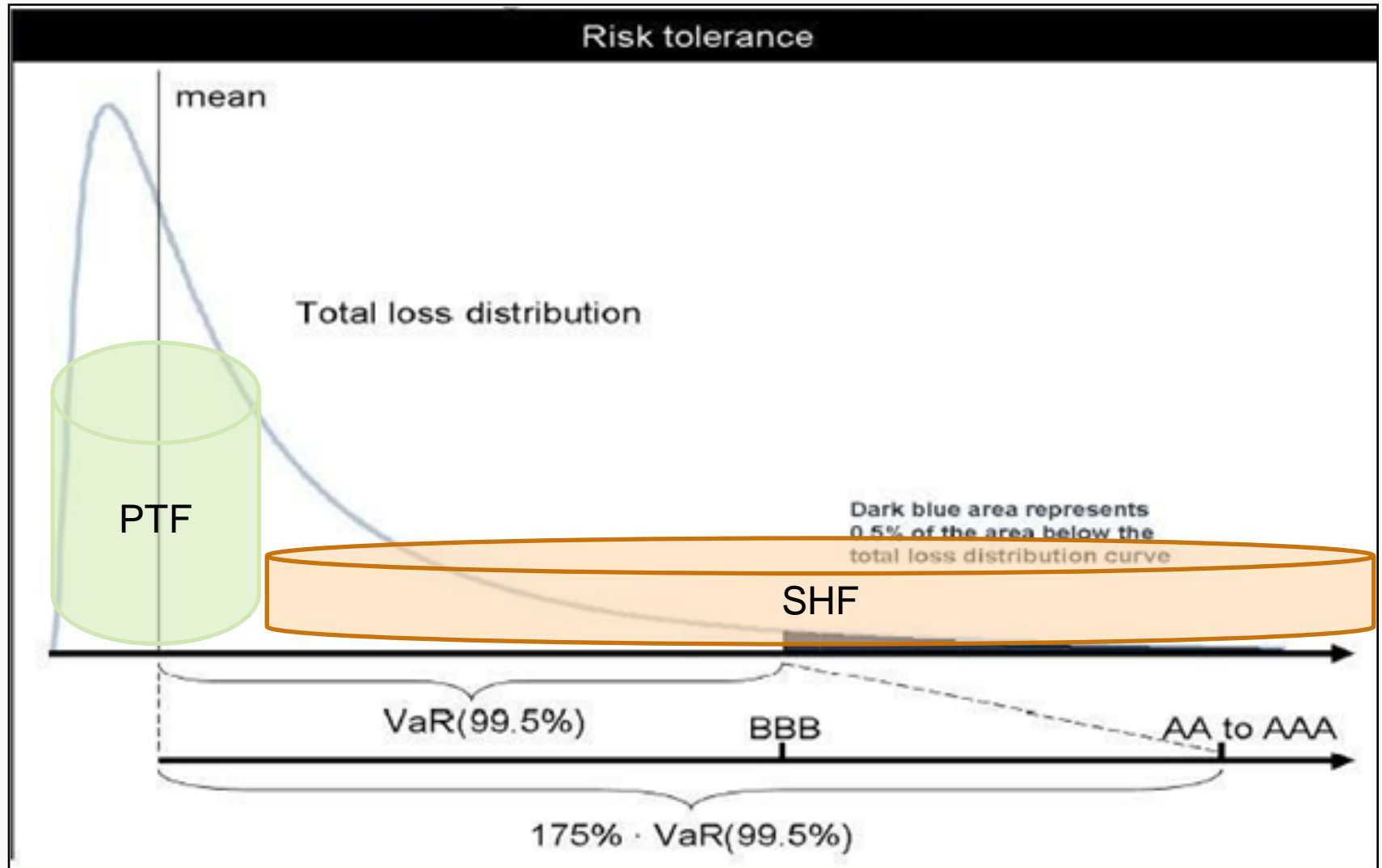
2. “Solidarity Qard”: Tangible Calculation is not risk adequate

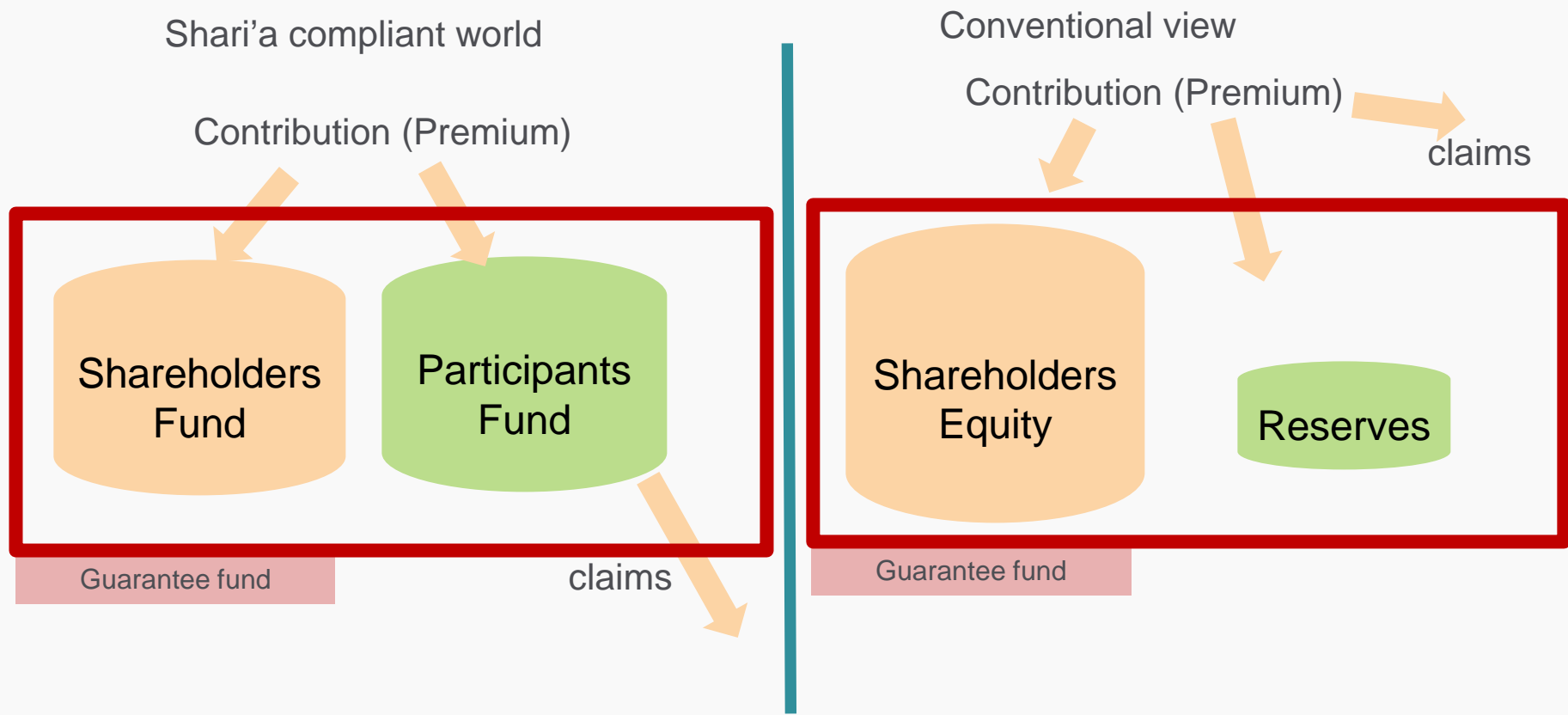


3. Qard due to high severity/low frequency losses (Volatility Qard)



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The items 0. to 8. are distributed differently over the two funds, their sum stays the same

Shari'a compliant world

Conventional view

Shareholders Fund

- 0. Seed capital
- 1. Wakala fee

PTF

- 2. catastrophe reserve
- 3. equalisation reserve
- 4. provision for onerous contracts/anticipated losses
- 5. unearned premium reserve
- 6. case reserve
- 7. IBNR
- 8. contingent commission reserve

Shareholders Equity

- 2. catastrophe reserve
- 3. equalisation reserve

Reserves Items 4. to 8.

Guarantee fund

Guarantee fund

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1. Qard ul Hasan is a legal construct the technical repercussions of which need to be in the focus of scholar discussions.
 2. Its legal features often need to be stretched to fit the economic reality. And that should be a reason for concern.
 3. The advantage of it: it is a sensitive indicator for deviations of reality from the ideal .
 4. Providing capacity and security is a working capital-based business. I.e. financially some sort of mudharaba or musharaka.
 5. Qard hasan concept is crucial and should be elaborated on an industry. It definitely does not seem apt at least for segments where the risk transfer element prevails. So, its abolition/replacement in these cases should be considered.



THANK YOU VERY MUCH
FOR YOUR ATTENTION

Ludwig Stiftl