

# CHAPTER I

## INTRODUCTION

### 1.1 Background

MNC stands for Multi-National Corporation is an enterprise which operates in two or more (hosts) countries thus managed from the home country. We can see the MNC's contribution towards the state, such as for economic growth, they increase state's GDP (Gross Domestic Product) and GNP (Gross National Product) through their company's branches as their FDI (Foreign Direct Investment). Beside of that, MNCs also provide job to people. Nevertheless, we cannot underestimate their roles towards our state. They are like an invisible empire. Indonesia is an archipelago which has the most significant population number in the world after China, India, and the United States become the target market for Multi-National Enterprises, especially life insurance industry.

In Indonesia, the potential life insurance market is quite significant in demand but low in the penetration rate. We can see that penetration for life insurance is shallow when correlated to GDP (5.17 per cent in 2018), only around 1-1.5 per cent, and it is lower than Brazil, Colombia, Malaysia, and India. Although the number of life insurance penetration rate lower, Indonesia presents a more considerable seepage, with a briskly growing insurance market. Other than that, population density also determines the life insurance development market, noted that in 2017, most of life insurance companies made annual surplus more than 10 per cent (Stabilitas, 2019).

A lot of foreign life insurance companies are sprinkled in Indonesia, and they lead Indonesia's insurance market when compared to life insurance companies emanating from the state. Otoritas Jasa Keuangan (Financial Service Authority) recognised that there are 50 life insurance companies, both from the private sector and also from the government. Foreign-based life insurance that people know such as *Panin Dai-Chi Life*, *AIA Financial*, *Allianz*, *CIMB Sun Life*, *Generali Indonesia*, *Prudential Life Assurance*, *Hanwha Life Insurance*, *Great Eastern*, *Commonwealth*, *Manulife*, *Reliance*, and *Sequis Life* (Prakoso I, 1989). From 50 life insurance, ten companies dominated the market itself in 2017 in the category of the most significant asset;

there were: *Prudential Life Assurance, Asuransi Jiwasraya, Manulife Indonesia, AIA Financial, Allianz Life Indonesia, Axa Mandiri Financial Service, and followed by Indolife Pensionsama, Simas Jiwa, Sequis Life, and BNI Life Assurance* (KONTAN.CO.ID, 2018).

Sharia economy system already in Indonesia already existed since the colonial era. The history of the Islamic economic movement has been going on since 1911, namely since the establishment of the Islamic Trade Syarikat organisation (Syarikat Dagang Islam) which was led by businesspersons and Muslim figures at that time (Mashdurohatun, 2011). We jumped into 1998 when there was a monetary crisis. At the same time, there was the phase of enlightenment by the depiction of law number 10, the innards of which gave the course to the conventional bank to transform themselves into Sharia or made a branch (division) for Sharia. In this aspect, banks and the sharia-based financial system began to establish in the year of the 2000s. The next is the enlivening phase. In this stage, the sharia-based financial service system and the banks reviewed their performance, and they found out that Sharia economy system can be socialised and succeed if they implemented in a structured way and sustainable. In 2001, there was an emergence of MES (Islamic Economic Society) (Pegadaian, 2017).

Regarding the opportunity of Sharia market in Indonesia, we can use the example such as Malaysia. Malaysia is a federation country in which the majority 60% is Muslim, and the total population is around 37 million. In 2018, Malaysia's GDP per capita was USD 11,079,266 (CEIC Data, 2018). Malaysia's policy is to make at least 75% of Malaysian got insured until 2020. Confirmed that Islamic Insurance is rising rapidly if compared to conventional. It can be seen that Takaful grew to 7.5% for family, while for general Takaful increased to 5.9%. These percentages are higher than insurance growth in conventional and each of them only 5.2% and 4.1%. The main background of the solid performance of Takaful in Malaysia is the increasing people's power purchasing and the government's struggle to increase the Sharia industry penetration and also Sharia industry is still emerging because there are still many conveniences from the market. Central Bank in Malaysia called Bank Negara Malaysia ordered the insurance industry to provide affordable insurance for people. This policy is already synchronised with the government's target to increase insurance customers from 56% to 75% until 2020. In July, there will be a regulation about a separation between family takaful and general takaful and they have their license (Budiartie, 2018).

Indonesia, as well as Malaysia, also has Muslim like the majority. If we compare to Malaysia, indeed, we still left behind to Malaysia, even Malaysia become Sharia role model in Southeast Asia. There are several factors why the insurance customer in Indonesia is low. Also, this will be a challenge for every life insurance corporations:

1. An economic slowdown that will decrease insurance market demand and also conditions of the capital market. With that factor, people tend to buy primary needs as their prioritise instead of insurance;
2. There is an open competition to face ASEAN Economic Society where Indonesia is included;
3. In terms of the capital of the insurance industry, every insurance company must have at least 100 billion rupiahs. In other words, following POJK Nomor 72/POJK.05/2016 printed out that an insurance company must have RBC (Risk-Based Capital) minimum requirement is 120% (OJK, 2016);
4. Lack of human resources who understand about Sharia insurance;
5. There are still conventional insurance products;
6. The low awareness people about the importance of insurance due to lack of education and there are some group who still anti-insurance despite there is Sharia insurance;
7. Distribution of insurance product and accessibility among society and the existence of insurance office relatively low;
8. There is still an insurance product that lower middle class and lower class can afford it due to insurance is expensive, and innovation shortage (Ramadhani, 2015).

Although this is an objection for every insurance company, it is precisely this kind of opportunity that Sharia market is still wide open. Also, Indonesia's Government accommodates through dual economy system policy which consists of conventional and Sharia. This policy existed since President Susilo Bambang Yudhoyono put the Islamic Economy as one of the national plans with the initiation of the GRES (Islamic Economy Movement). The next president supported the establishment of KNKS (National Islamic Financial Committee) and was established by the Decree of Presidential No.91/2016 and immediately led by President and Vice. We can know this plan as Masterplan Ekonomi Syariah Indonesia, which started in May 2019, and there are four components:

1. Firming Halal Importance Chain

- This primary strategy is to enhance the whole halal chain for all cluster, which measured and arranged in the GIEI (Global Islamic Economy Indicator), as well as looked-for such as social security or renewable energy
2. Invigorating Islamic Finance Division
    - Islamic financial sector can be a key to the halal industry or halal value chain. This plan is also targeting to raise the volume of financial businesses and Islamic banking
  3. Strengthening MSMEs (Micro Small Medium Enterprises)
    - The individual of the MSMEs are small, yet if 60 million MSMEs are combined, they will become the most significant contributors in economic. There are two exciting part about MSME: they backed 50% of Indonesia's GDP, and they absorb 90% of the national labour force
  4. Improving Digital Economy
    - In developing the keenness from a global player, Indonesia, through state halal business needs to implement digitalisation in their manoeuvre and to improve their efficiency such as using Islamic digital imbursement access (Deloitte, 2019).

## **1.2 Research Question**

1. Regarding this thesis's concentration is Multi-National Corporation, how did Prudential Life Assurance Company as Multi-National Corporation to cope with the Dual Economy System Policy in Indonesia?

## **1.3 Theoretical Framework**

In this proposal, we are going to use Cohen's Concept which contains MNC and FDI as a theoretical framework

## 1. MNC (Multi-National Company) & FDI (Foreign Direct Investment)

Other names for this term are Multi-National Enterprise (MNE) and Transnational Corporation (TNC). Lewis and Moore stated that an MNC that involves in FDI (Foreign Direct Investment) and controls value. According to Jones, a Multi-National Enterprise delineated as a firm that operates in more than one country or at least two countries and monitors income-generating asset (UK Essays, n.d.).

An FDI (Foreign Direct Investment) is different from portfolio investment which investor solely acquires equities of foreign-based corporations. FDI is an expenditure made by an individual or a firm into the business earning located in another state. FDI also takes place when a financier creates overseas business operator or acquire the external business asset in a foreign corporation (Chen, 2019). MNC and FDI are two things that must be synchronised each other, why? Because FDI is pivotal for an emerging market and developing. Their state needs a vital component to build infrastructure and to increase incomes and jobs while the companies of the host country demand multinationals' expertise and capital to bolster their international sales. For MNCs itself, they need capital and profit not only from their market but also from the host's country market (Amadeo, 2019).

Companies find out why FDI to be glamorous. Countless executive companies notice abroad expansion as a crucial part of meeting unstoppable demand from stakeholders for growth, Increased profits and sales can come equitably from oversea subsidiaries because of the host country or other states always have more potential customer than the original state (Cohen, 2007). In other words, FDI is a core and tool of an MNC itself from a multinational company process (Afivah, 2019).

The FDI of MNCs plays an essential role in their (developing countries) entry into advanced technologies. MNCs are one of the leading technologically modern organisations, accounting for a critical sector of investment in research and development (R&D) worldwide. Another potential benefit of FDI is the accumulation of capital. FDI also affects the balance of payments by increasing the flow of capital, boosting production and increasing exports. It helps to create prospective trade surpluses and economic growth. Also, access to FDI by MNCs helps to

enhance the international network to increase the potential for trade (Mishra, Degtereva, & Paneru, 2017).

Regarding that concept, We can categorise *Prudential Life Assurance* company (corporation's name in Indonesia) as a Multi-National Corporations because basically, Prudential is a foreign-based life insurance company from Britain named *Prudential Life Corporation* (PLC), Prudential has a various name in other states or become localised such as *Jackson National Life Insurance* in the U.S due to there is the same company called *Prudential Inc.*, *Prudential BSN Takaful Berhad* from Malaysia, *Prudential Corporation Asia* is also same, but the headquarter is located at Hong Kong.

FDI is an essential component thus for an extractive corporation which operates a business where natural resources such as geographical condition, and raw materials are promising for commodities in agricultural. Thus, how if the companies are like service companies, especially life insurance? When foreign-based life insurance companies come to Indonesia, they usually take a partnership as the alternative of seeking FDI as an objective to find profits from overseas market and the most common way to seek benefit from abroad market is licensing. It can be seen that *Prudential Life Assurance* when the first time came to Indonesia in 1995, Prudential name was *PT Prudential Banc Bali Life Assurance* (PBBL) due to Prudential merged itself into *Bank Bali* and also the government's policy (Soeharto's reign) at that time was only government company were allowed to be established. If a foreign corporation wanted to establish, it must do a merger or joint venture (Prudential Indonesia, n.d.).

Beside Prudential cooperate with local companies to invest their money Prudential Life Assurance company also cooperate with member organisations of the *Prudential Life Corporation* called *Eastspring Investment*. Eastspring itself is an international manager investment in every cluster such as fixed income, equity, and multi-asset, and they invest their capital on five SEA (Southeast Asia) states, India, South Korea, Japan, China, and Taiwan. Eastspring Indonesia or called *PT Eastspring Investment Indonesia*, established in 2011 and got a license from OJK (Otoritas Jasa Keuangan) a year later (Eastspring Investment Indonesia, n.d.).

## 2. Adjustment/ Localisation Theory

Every Multi-National Corporation must be doing adjustment or localisation in order to get the customers and adjustment, or localisation is the most common way that the Multinational Enterprises use in the international business. Localisation or adjustment is a process of integrating a good or service from a specific local or market to comply with the requirements of another specific local or market (Translit, 2017). When localising, the company must take into account different cultural values. Let us take the example of MNC that operates in food such as *Kentucky Fried Chicken* (KFC). Mostly Indonesian love spicy food and also they eat together with their family. Nevertheless, the company adjusts with the Indonesian preferences and do localise such as make a bucket food into their package, even make a traditional food such as chicken *sambal matah*.

However, when a life insurance company such as Prudential, they see Indonesia as one of the most significant populations and Indonesia has potential customers and a lot of productive customers. They realise Indonesian 89% is Muslim so as Prudential prefers life insurance unit they put in Indonesia and the corporate establish Sharia unit and change colour for Sharia from red to green due to Indonesian see green as a holy colour. God loves green colour according to Islam's perspective, and they still have a conventional unit with red colour as their logo. That is their way to adjust and to localize with the host country.

#### **1.4 Hypotheses/ Arguments**

According to the research question and concepts that the author use, the author has a hypothesis that *Prudential Life Assurance Company* in Indonesia responds to the Dual Economy System Policy Indonesia by:

1. *Prudential Life Assurance* adjusted with Dual Economy System Policy in Indonesia due to the majority of Indonesian is Muslim by establishing Sharia unit.
2. *Prudential Life Assurance* also did several innovations as their adjustment or localisation, especially products due to at that time, there was no innovation among life insurance companies plus people used to choose a traditional product. Thus, Prudential itself was a pioneer for life insurance product as well as investment.

## **1.5 Analysis Scope**

In order to make the research more focused, the author will analyse to understand about this thesis. The scope of the analysis started from the year 2015 to 2018

## **1.6 Research Methods**

In this thesis, the author is going to use content analysis and statistical analysis. Content analysis means analysis use enshrined material, observed phenomena individual, and other supporting documents as legitimate material (Shelley, 1984). The author also use books, journals, documents, and also websites. At the same time, statistical analysis is an analysis which uses statistic or data as evidence.

## **1.7 Outline**

The author will divide into five chapters; there are:

### **Chapter I**

In this chapter, the author will explain the background of the subject research such as background, research question, theoretical framework, hypothesis, the scope of analysis, research methods, and system of writing

### **Chapter II**

Chapter two will explain more detail regarding how the establishment of the Prudential Life Insurance which started from Britain, and how they expanded their business until to Asia and finally come to Indonesia

### Chapter III

Chapter three will discuss the Dual Economy System in Indonesia

### Chapter IV

This chapter will consider how *Prudential Life Assurance* company respond towards the Dual Economy System Policy in Indonesia and its analysis by using Key Performance Indicator according to the *Financial Services Authority* (OJK)

### Chapter V

In the last chapter, the author will provide a conclusion and suggestion from the result of this research.