ARE SYSTEMIC RISKS INSURABLE OR NOT?

LERATO MATTHEWS

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- Systemic risk and insurance
- The role of insurance in building resilience
- The changing role of intermediaries in an evolving risk landscape

SYSTEMIC RISK AND INSURANCE

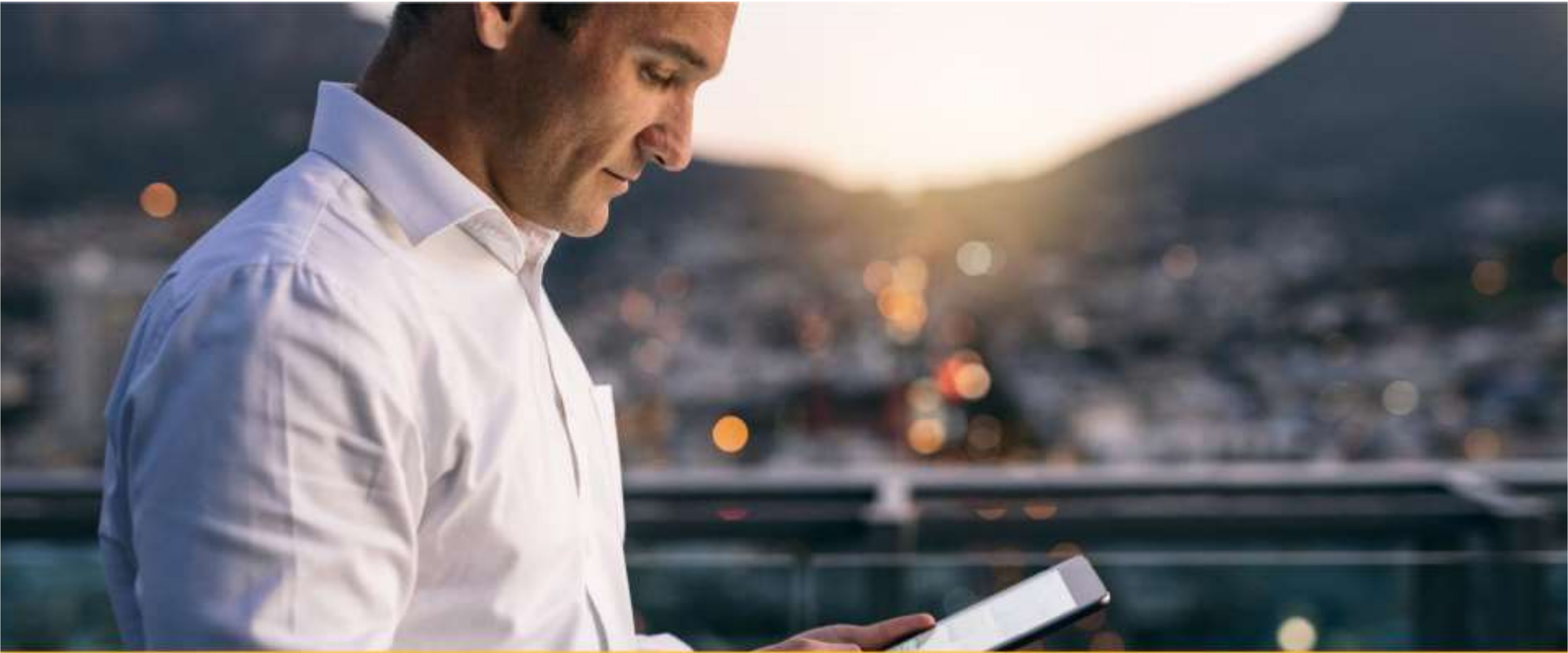
WHAT IS SYSTEMIC RISK?

Systemic risk refers to risks that typically play out as a chain reaction in a system resulting in widespread losses to individuals, businesses, industries, and even countries. Examples of systemic risks:

- pandemics
- climate change
- cyber risks
- political instability, etc.

Such risks are a threat to both resilience and access to capital because they are increasingly difficult or expensive to insure against.

SOUTH AFRICA’S CHALLENGES



RISK ENVIRONMENT HAS SHIFTED

		LOOKING FORWARD
MACRO-ECONOMIC	• Claims inflation • Affordability	• Double digit increases not sustainable • **Need for hyper tailored solutions**
GEOPOLITICAL	• Loadshedding • Road infrastructure • Municipalities	• Systemic risk • Public private partnerships • **Need for risk prevention**
REGULATORY	• FATF • Energy • POPIA	• Cost of compliance • Cyber • **Growing advice risk, importance of skills**
CLIMATE	• KZN floods • Rainfall	• Earnings volatility • Reinsurance capacity • **Traditional insurance too expensive**

CHALLENGES CREATING A FRAGILE ECONOMY

Uncertain global operating environment

- **Rising geopolitical tension**
  - Russia/Ukraine conflict causing supply chain disruptions globally
  - US/China tension
  - SA foreign policy
- **Slowing global economy**
  - Elevated inflation (consumer and repair/replacement cost for insurers)
  - High interest rates
  - Market volatility
  - Tight monetary policy

CHALLENGES CREATING A FRAGILE ECONOMY

The insurance sector is poised for growth, despite operational and structural challenges

- Continuation of structural market dynamics with rate hardening spilling into personal lines (higher reinsurance costs)
- Above average NatCAT insured losses
  - Property class continues to experience rate increases in CAT-hit areas; not yet at a sustainable level
- Inflationary pressures leading to increased premium collection challenges
- Corporate actions to address growth and profitability challenges
- Higher interest rates benefit investment returns; however, with pressure on disposable income

CHALLENGES CREATING A FRAGILE ECONOMY

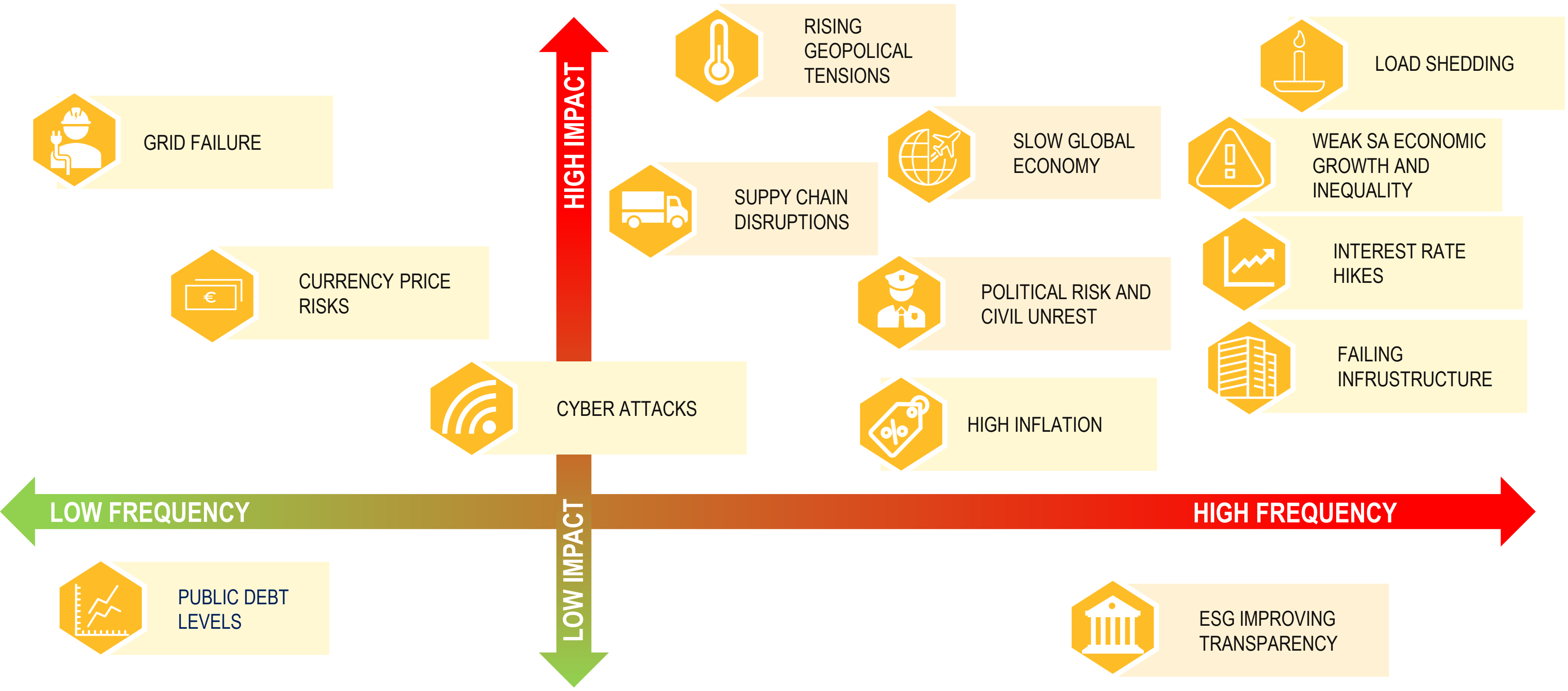
SA economy continues to be under pressure

- Weak SA economic growth
- Severe electricity constraints, which led to increased load shedding
- High consumer inflation, but may have peaked
- 350 bps rise in interest rates since June 2022
- Increasing strain on personal disposable income
- Old and frail infrastructure
- SA foreign policy under scrutiny
- Supply chain disruptions issues with Transnet domestically

CHALLENGES CREATING A FRAGILE ECONOMY

Climate change remains an ever-present risk

- **Frequent and severe climate-related events**
  - Earthquakes in Türkiye
  - Cyclone Freddy in Madagascar and Mozambique
  - Highest average temperature across Europe and the U.S in history
  - Wildfires in Canada and US-Hawaii
  - Rainfall leading to flooding - Eastern Cape, Mpumalanga, KZN, Western Cape
- **Increasing sustainability and climate-related disclosures (ISSB)**

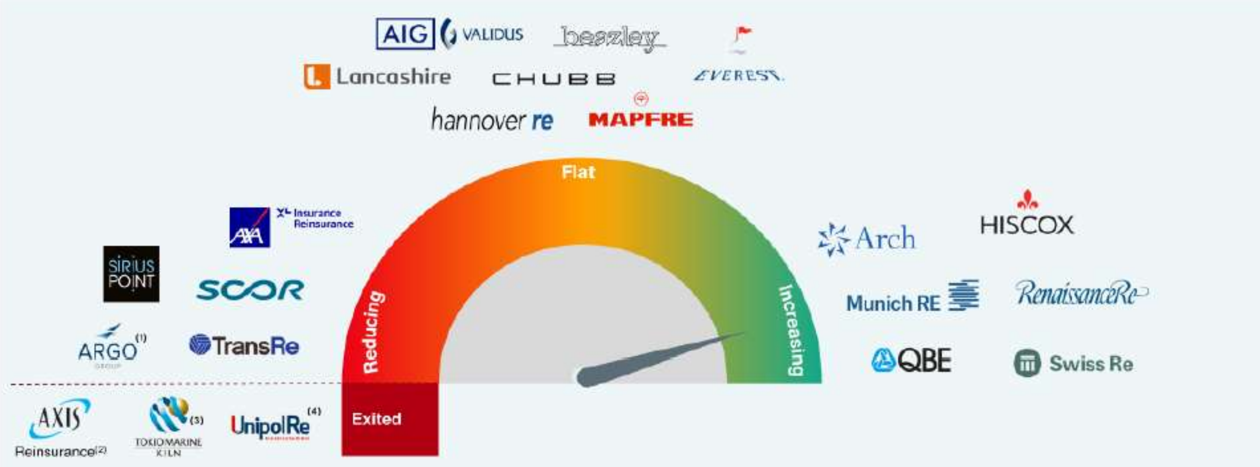


If a perfect storm were to arise, wherein these systemic trends were to occur simultaneously, it could potentially lead to a catastrophic event for many insurance companies and reinsurers.

RISK APPETITES ARE CHANGING

- Some reinsurers have exceeded tolerances for volatility, with many not covering their cost of capital
- The risk environment has become very challenging: climate change; inflation; geopolitics
- Weak results and uncertainty have undermined investor appetite for reinsurance risk and assets

- Split market for cat risk, some reinsurers are cutting back or pulling out entirely while some see the difficult risk environment as an opportunity to grow
- Buyers will need to show flexibility: strategies may need to change in order to secure required capacity
- Portfolio results, data quality, views of risk, positioning on inflation and market access are all critical
- On current trends, cat risk will be concentrated in fewer, larger hands going forward



REINSURANCE MARKET KEY OBSERVATIONS

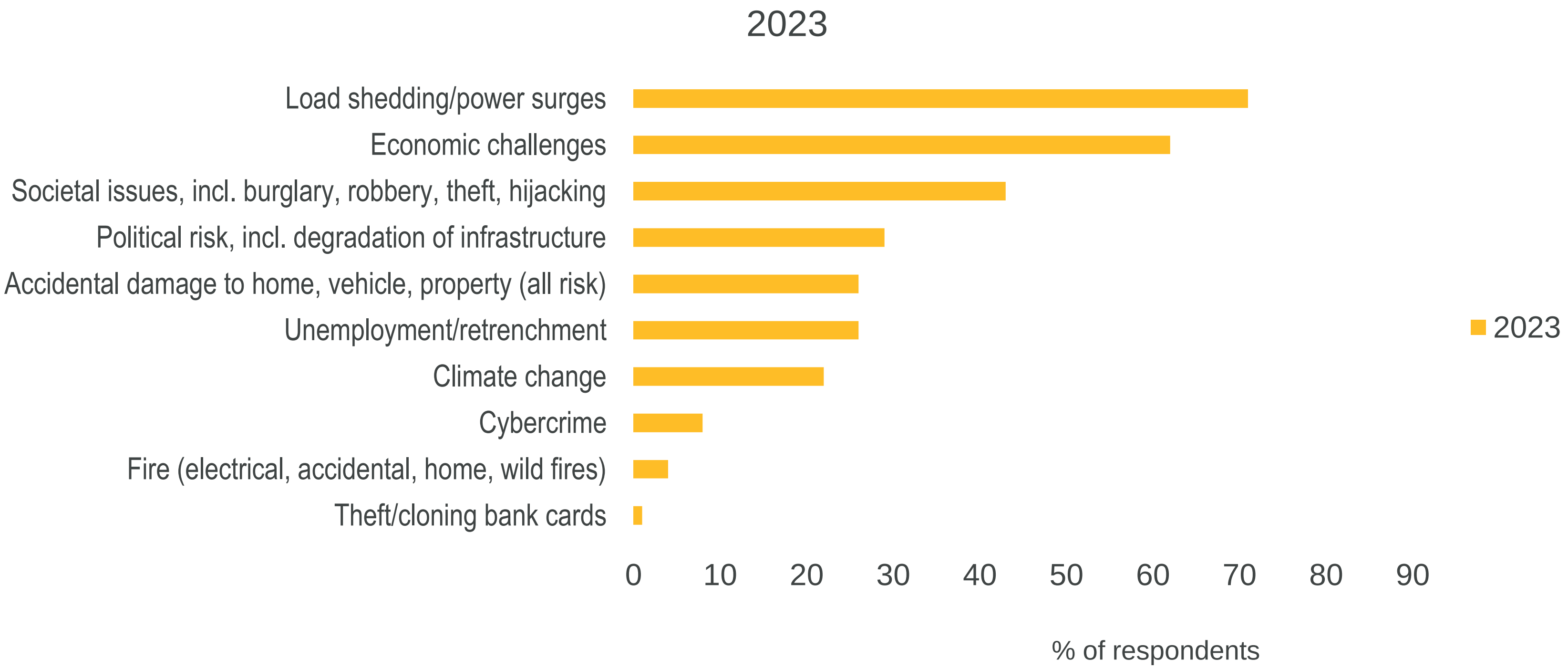
- Continued hardening market
- Impacting all lines of business
- Reduced deployment of capacity opens a gap for small reinsurers

Reduced Reinsurer Appetite	Global Uncertainties	Inflation	Sanctions	Wordings Scrutiny
Evident reduced reinsurer appetite for volatility noticeable in all forms of property reinsurance	Global economic and political uncertainties driving overall reduced net risk appetite of reinsurers	Presence of inflation now also impacting pricing of short tail lines	Ukraine war / Russian sanctions stimulating contract exclusion discussions	Cat programmes: Reinsurers seeking greater clarity of occurrence definitions

TOP EMERING RISKS IDENTIFIED BY INTERMEDIARIES

RESEARCH METHODOLOGY AND SAMPLE

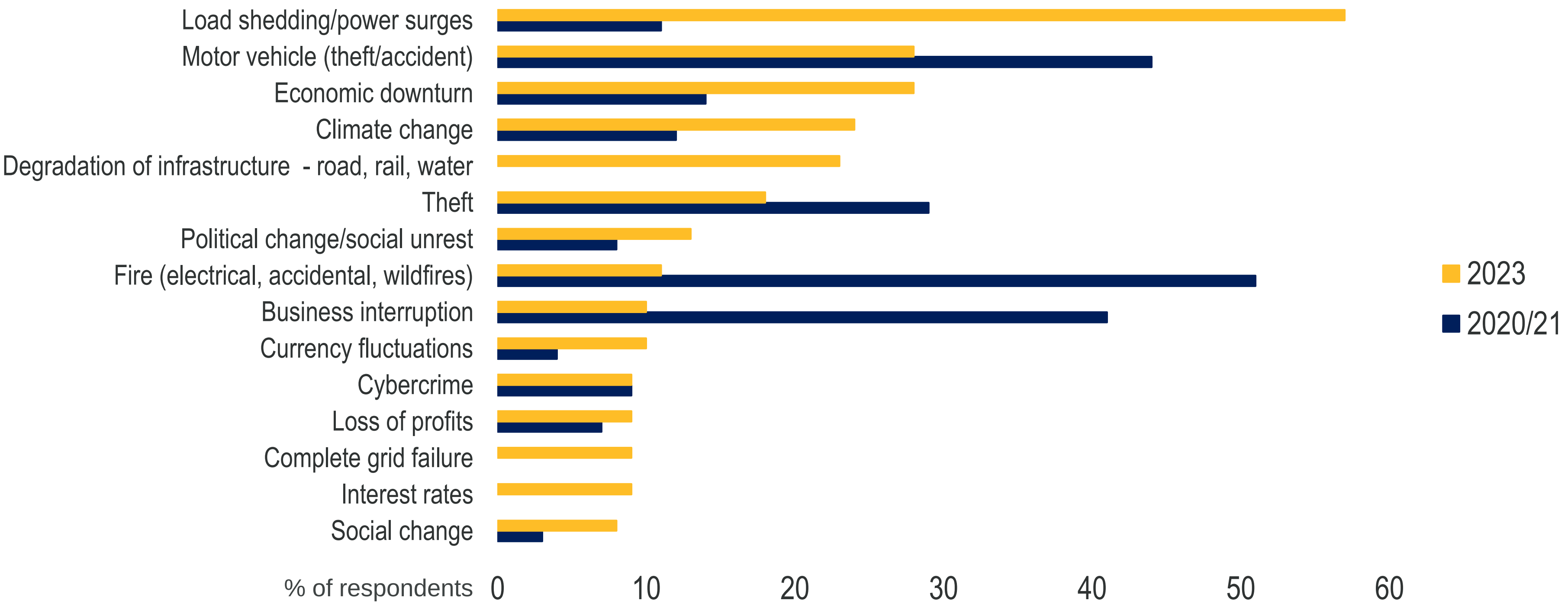
The "top 3 risks" to consumers are load shedding, economic challenges and societal issues according to personal lines intermediaries



Base: Personal lines intermediaries (n=77)

Q. Which of the following do you consider to be the THREE biggest risks that your personal lines clients face?

Commercial intermediaries identify a mix of 'traditional' and emerging risks as the "top 3 risks" facing businesses today, but emerging risks have become a growing threat in the past 2 years



Base: Commercial intermediaries 2023 (n=90); 2020/21 (n=90)

Only risks mentioned by 5+% of respondents in 2023 shown

Q. Which of the following do you consider to be the THREE biggest risks that your commercial/large corporate clients face?

THE ROLE OF THE INSURANCE INDUSTRY IN BUILDING RESILIENCE

RATIONALE FOR PARTNERSHIP

Governments have a leading, regulatory & coordination role in Disaster Risk Management & should engage stakeholders in design & implementation of policies, plans & standards (Sendai, 2015).

Collaboration between public, private sectors, civil society organizations & academia, scientific & research institutions is essential to building societal resilience.

Sendai Mid-term review (18 May 2023) noted that public and private investments to anticipate, plan for, & reduce disaster risks remain insufficient & do not match scale of existing & future risks.

More dedicated action needs to be focused on tackling underlying disaster risk drivers, such as consequences of poverty and inequality, climate change and variability, unplanned and rapid urbanization, etc.

Private sector can play a significant role in mobilizing resources to build resilience and reduce disaster risks.

P4RR THEORY OF CHANGE (TOC)

Santam

What we are doing	What we wish to achieve	What we wish to change	What we wish to change	What we aspire to
ACTIVITIES	**SHORT-TERM OUTCOMES**	**MEDIUM-TERM OUTCOMES**	**LONG-TERM OUTCOMES**	**IMPACT**

ACTIVITIES

- **Institutional Arrangements**
- **Risk Assessment**
- **Risk Reduction**
- **Response & Recovery**
- **Information Communication Technology (ICT) / Early Warning Systems**
- **Capacity Building**

SHORT-TERM OUTCOMES

- Fire prevention systems are in place
- Flood prevention systems are in place
- Drought prevention systems are in place
- Fire response systems are in place
- Improved water security
- Communities have early warning of impending disasters
- Disaster Management & fire services response and recovery plans are in place
- Climate change adaptation plans are in place
- Identified school risks are highlighted
- Improved disaster awareness in vulnerable communities
- Municipalities and stakeholders understand risks

MEDIUM-TERM OUTCOMES

- Improved fire safety
- Improved regulatory & institutional basis for fire code enforcement
- Improved disaster management & fire services response systems
- Enhanced disaster risk reduction measures
- Improved disaster management & fire services stakeholder coordination
- Improved understanding of climate risks

LONG-TERM OUTCOMES

- Optimal disaster management & fire services systems
- Reduced loss of life & injury
- Reduced damage to property

IMPACT

- Resilient communities
- Reduced climate risks
- **Santam has a reduced risk exposure**

Sphere of measurement

SANTAM'S PARTNERSHIP FOR RISK AND RESILIENCE – SUPPORTING SUSTAINABLE RISK MANAGEMENT PROGRAMMES

01 CAPACITY BUILDING

- GIS Capability
- Flood, Fire, Drought Data Exchange
- Disaster-ready Communication Toolkit
- Automated incident reporting (Data Collection APP)
- Firefighter & Disaster Management personnel Training
- PPE for Fire-fighters and Disaster Management Personnel
- Fire Services and Disaster Management Equipment

02 RISK ASSESSMENT

- Community-based Risk Assessment
- Disaster Management Plans
- Fire response plans
- **Climate Change adaptation (Green-Book**)
- Fire Services Capacity APP
- Conduct risk assessments in selected schools (LSEN)

03 RISK REDUCTION

- Alien Vegetation Clearing
- Fire-breaks
- Disaster simulation exercises
- Water security initiatives
- Drainage clearance

04 RESPONSE & RECOVERY

- Disaster relief material
- Provide training & capacity building to civil society partners to enhance response & relief coordination
- Building a coalition of agencies to enhance response & recovery

05 RISK AWARENESS & EDUCATION

- Education & Awareness Campaigns & Advocacy
- Community Research
- Community-level training
- Provision of training to partner Civil society organisations

06 EARLY WARNINGS

- Smoke Alarms
- Flood early warnings
- Early Warning initiatives with South African Weather Services (SAWS)

THE CHANGING ROLE OF INTERMEDIARIES IN AN EVOLVING RISK LANDSCAPE

TOUGHEST THREE-YEAR PERIOD IN MEMORY

- Contingent Business Interruption
- KZN riots and resultant SASRIA increases
- Extreme weather catastrophes
- Extensive policy screening actions
- Double digit renewal increases
- Compulsory tracking devices in high-risk vehicles
- Aggressive rating and excess response to power surge and grid failure
- Active de-risking to manage volatility exposure and access to reinsurance
- Tough approach to risk reduction requirements
- Limited negotiation mandates

A NEW RISK MODEL

1

Idea of repair replace to predict and prevent

2

Commoditised risk transfer to collaborative risk mitigation

3

Product sell to solution build

4

Client value only at claims stage to client value throughout the life cycle

5

Reducing cost of insurance over time

THE IMPORTANCE OF ADVICE

- Intermediaries have always been integral to the success of insurers. They are essential players in the insurance value chain, making material contributions across the advice, sales, marketing, and claims handling functions
- Intermediaries will become even more important as the insurance landscape evolves requiring them to provide more than just the cheapest insurance quote
- **Strengthen client relationships -** will give intermediaries an advantage to explore and thoroughly map out the risks that businesses and individuals face. As clients increasingly seek solutions built for them
- **The importance of risk management - a**s risk advisers, intermediaries could **bring more focus to the practice of risk prevention and mitigation as opposed to pure risk transference.**
- Ultimately, this would reduce the number of total claims

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