South Africa: Insurance Industry Update
September 2021

Introduction

The third quarter of 2021 was a rollercoaster ride of ups and downs. The rioting in parts of the country caused widespread damage and loss of life, and also raised public awareness of Sasria. Disappointingly slow COVID-19 vaccination rates resulted in vaccines being made available to all adults. Leading insurers announced mandatory vaccination plans for their staff, and some are considering vaccination status as an underwriting factor.

In this update, we bring to you a collation of regulatory updates, court rulings, operational risks and our view on COVID-19-related developments.

IN THIS UPDATE:

Riot insurance and premium increases

The public unrest that swept across KwaZulu-Natal and up to Gauteng in July this year, following the imprisonment of former president Jacob Zuma, was the most expensive riot globally in the past decade, lasting less than a week. Although settlements are still being finalised, it is currently estimated that the claims could fall between ZAR 20 billion and ZAR 25 billion, with a total economic impact estimated at around ZAR 50 billion.

The South African Special Risk Insurance Association (Sasria) was launched in 1974 to provide cover against risks associated with civil commotion, public disorder, strikes, riots and terrorism. A state-owned entity, Sasria was created in response to the risks associated with these activities at a time in South Africa's history that was turbulent. By providing this cover, traditional insurance markets could continue their growth with greater certainty, supported by international reinsurance companies. Sasria is the only insurer in South Africa that provides cover for political violence.

Sasria had been well capitalised prior to the July riots, with sufficient assets to meet its Solvency Capital Requirement (SCR) three times. However, in the wake of the riots, Sasria's cover ratio had fallen to below 100% of its SCR, and a preliminary capital injection request of ZAR 3.9 billion has been submitted to the government to cover shortfalls in payments and meet its capital requirements.

Unsurprisingly, Sasria's reinsurance cost has increased as a result of the unrest, which in turn has resulted in the insurer increasing its own premiums to meet the rising cost.

Ombud rules in favour of the insured in excess speed-related claim

The Ombudsman for Short-Term Insurance (OSTI) recently overruled a rejected claim for damages incurred by the insured when rear-ending a third-party vehicle while travelling at 173 km/h prior to collision.

It is commonly assumed that breaking the law will often automatically lead to a rejection of claim. Wording to this effect is fairly common in short-term insurance policies.

The insurer rejected the claim stating that the insured breached the "reasonable precautions" clause, which is another common term. The insurer stated that the insured had not exercised due care to limit the risk of damage by driving within the speed limit.

However, the OSTI ruled in favour of the insured, stating that "the policy condition does not preclude a successful claim for damage caused by the insured's negligence."

The OSTI has seen an uptick in rejected claims from speeding due to this policy condition in recent years, with 16% of these claims overruled in favour of the insured in 2020.

Insurers have noted this ruling and may consider reviewing their policy wording to strengthen their standing in instances of law breaking or policyholders not taking reasonable precautions. Moreover, recent and ongoing claims could be challenged given the latest ruling, further increasing administrative costs surrounding the processing of claims.

Proposed amendments to the policyholder protection rules for microinsurers

In July 2021, the Financial Sector Conduct Authority (FSCA) published proposed amendments to the Policyholder Protection Rules (PPRs), which would have important implications for microinsurers. In particular, the FSCA has proposed that:

- The current 12-month limit in contractual term should be removed from the product standards for microinsurers
- The definition of a funeral policy should be expanded to cover all policies that offer funeral cover, regardless of whether it constitutes the primary obligation or a rider benefit; regardless of the class of business under which it is written; and regardless of any other rider benefits that are attached to a funeral policy

Removing the 12-month limit on microinsurance contract terms will enable microinsurers to implement waiting periods of up to six months, provided that the contract term is at least 24 months. The PPRs limit waiting periods to the lesser of one quarter of the contract term, or six months. Therefore, under the current 12-month contract limit, microinsurers are only permitted to implement waiting periods of up to three months.

These changes have been proposed to level the playing field by ensuring that traditional insurers and microinsurers are subject to the same requirements. However, if long-term policies are permitted under microinsurance, this will have serious consequences for prudential supervision and the complexity of actuarial provisioning.

IFRS17 risk adjustment, capital allocation and transition

In a recent survey on capital allocation methodologies, two-thirds of respondents reported not having finalised their IFRS17 risk adjustment methodology decisions, let alone their capital allocation decisions.

For those following a cost of capital approach, the allocation of capital and diversification benefits can have a meaningful impact on which policies are loss-making and which require a contractual service margin. This remains a key decision for IFRS17 projects and can affect the transition impacts and ongoing earnings recognition.

While the preference for simple capital allocation methods is nearly universal, a small number of insurers have seen the advantage of gradient or Euler methods allocations of diversification benefits over the common but cruder proportional allocation methods. Gradient or Euler methods are simpler than many expect and, once set up initially, can provide easy, effective and rational allocations of capital across lines of business.

Several insurers have progressed well with their transition estimation. It should be no surprise that the impacts vary widely, as a direct function of prior accounting choices. Insurers with large discretionary margins or zeroisation under IFRS4, or those with significant profitable premium increases, are generally seeing a significant increase in net asset value (NAV). Insurers having made more aggressive accounting choices are seeing smaller increases or even decrease in NAV.

Draft public reporting for insurers

The Prudential Authority (PA) published in July the draft Prudential Standard on Public Disclosures for Insurers (PDI) and related guidance notice for public comment.

The draft PDI's objectives are "to set out the information that insurers are required to disclose to the public in order to promote market discipline and an understanding of the risks to which insurers are exposed to, as well as the manner in which those risks are managed."

The requirements include publishing audited qualitative and quantitative information on a website within the same timeframes as for current regulatory reporting.

There will be a cost to establishing the public reporting process as well as ongoing costs to perform the reporting, including the audit and independent review.

Listed insurers will likely have the least effort to establish the public disclosure reporting. They will be able to leverage existing internal and external reporting processes and automation.

Smaller, unlisted insurers will likely incur more work and costs to set up, and many of these costs are fixed and, therefore, will not scale down to their smaller size. This will place greater financial and resource burdens on smaller insurers.

We hope that the PA specifies a standard format for at least the basic quantitative information. Use of machine-readable format will make it easier for users to perform analyses on the information. At the very least, any quantitative extracts of the Quantitative Reporting Template (QRT) included in the public disclosures should be made available in XBRL or Microsoft Excel format, as is also required under Solvency II.

Finalising the PDI is long overdue to address the lack of public information which can inform stakeholders, promote market discipline and promote capital market efficiencies.

The draft PDI has set the bar high. We expect some further refinements following the public consultation process. Some likely areas of challenge and potential pushback along with areas of further consideration include:

- Balancing different stakeholder needs
- Clarity on audit and review requirements
- Further considerations on availability and format
- Concerns on proprietary and confidential information

- Balancing value with the additional work and cost
- Initial pressure on reporting teams
- Refinements to tailor to South African industry

There are going to be costs to establishing the required reporting and ongoing production. However, this should be an overall positive outcome for the industry provided the information meets the required objectives.

Credit life and income protection responding to COVID-19

Life insurers writing credit life and income protection have had a particularly volatile 18 months.

Level 5 lockdowns triggered an enormous spike in retrenchments, partly as marginal businesses quickly saw the writing on the wall and retrenched staff.

Some insurers considered these reported claims and, taking a view on future adverse retrenchment experience, decided to close certain lines of credit life and income protection products to new business.

We saw divergent practices among insurers, including on premium increases, claim repudiations through tight application of policy conditions, requiring total loss of income, and questions around how to treat Temporary Employer/Employee Relief Scheme (TERS) payments to offset loss of income.

Retrenchment experience turned out better than most had initially feared. After an initial spike, retrenchment rates have returned to more moderate levels. The outlook for the economy remains bleak, so risk of an extended period of adverse retrenchment experience remains, albeit not to the level experienced in the second half of 2020.

Mortality, on the other hand, has turned out worse than many expected when reporting at 30 June 2020. In August 2021, the Association for Savings and Investment South Africa (ASISA) announced that claims paid from 1 April 2020 to 31 March 2021 were 64% higher in the last 12 months compared to the prior period. Death claims on credit life are up only 26% year on year, although this likely includes the impact of lower policy volumes given the reduction in sales and short-term nature of most credit life policies.

Generally, insurers that kept their credit life and income protection products open to new business, with or without reinsurance, were better placed to continue business as usual when retrenchment experience turned out to be better than initially feared.

We cover these topics and others in an article to be published later in 2021.

How Milliman can help

If you would like to discuss any of the above, or anything else with us, then please contact us. Milliman can provide a range of services including:

- Insurance strategy on reopening closed lines of business, or expanding into new markets
- Dealing with regulatory change and approvals
- Product performance reviews and changes in light of COVID-19 lessons
- Solo and Group Head of Actuarial Function
- Independent review of actuarial and risk functions
- Own risk and solvency assessment (ORSA) and risk management maturity reviews
- Licence conversion and application assistance
- IFRS17 implementation and advice

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