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African Short-term Insurance Industry Trends.

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PRESENTATION SCOPE

- ✓Intro.
- ✓Common Concerns.
- ✓Overview of Current State of African Insurance Industry.
- ✓Trend Drivers/ Global Trends.
- ✓Conclusion & Recommendations.

INTRODUCTION

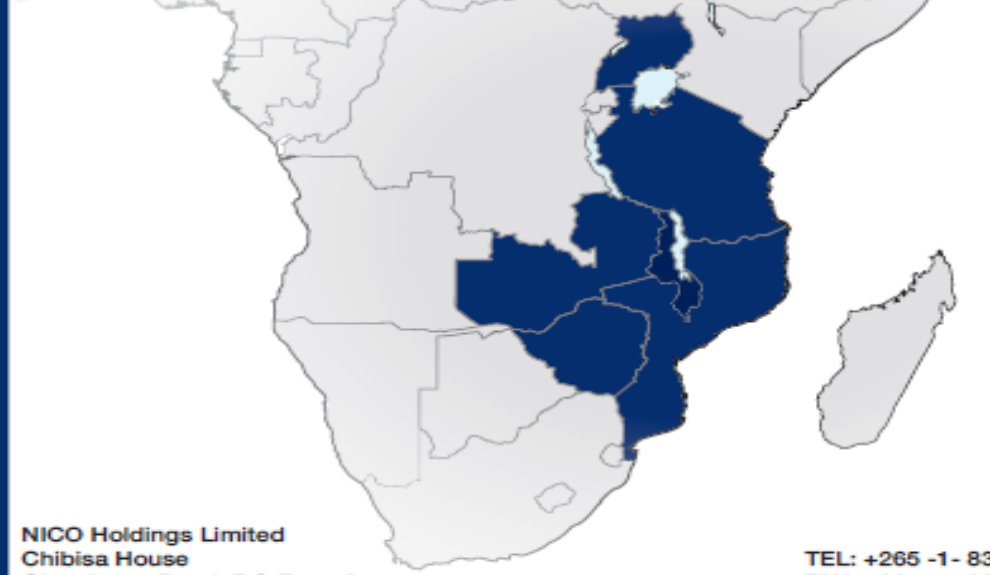
- This paper is presented on behalf of Felix Mlusu, MD - NICO Holdings Limited Malawi; we are honored to be invited to share our views on the subject with this gathering.
- My mandate is to look at trends in the Insurance Industry primarily from a short-term multi-national (Africa) insurer's view-point.
- The global rate of change continues apace; inevitability of rapid change in climate, in regulatory environments, in governance and in socio-economics will have considerable impact on the African Insurance and Reinsurance industry and the way we do business.
- In highlighting the trends, the presentation comments on inter alia observable trends in the African insurance/reinsurance industry and implications.
- A few Recommendations will conclude the presentation.
- Given the diversity of Africa's 54 states (with South Sudan) and their economies, societies and policy environments, the discussion, recommendations etc are broad and general.

- *Information used in the presentation has been gleaned from various research papers and publications [including PWC (2008-2012), KPMG (2011), RENAISSANCE CAPITAL (2011), Africa Progress Report 2011, SWISS RE (2012), McKinsey Global Institute (2010), Geneva Association (2010) and the latest strategy papers from NICO entities in six countries].*

NICO Holdings

General Insurance | Life and Pension Assurance
Asset Management | Information & Technology | Banking

Malawi, Zambia, Zimbabwe, Tanzania, Uganda, Mozambique



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COMMON KEY CONCERNS

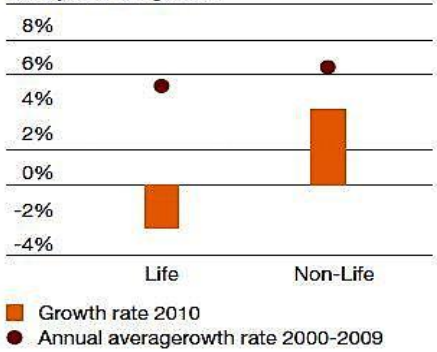
- Common interests in the value chain include:
  - Regulation/supervision Impact on business and business practice.
  - Market Growth.
  - Profile and quality of risks clients bring to the party.
  - Capacity availability to meet client needs.
  - Retention ratios.
  - Risk management by insurers & reinsurers.
  - Cover terms granted to our clients.
  - Quality of Client service.
  - Quality of claims settlement, primarily timeliness.

STATE OF THE AFRICAN INSURANCE MARKET.

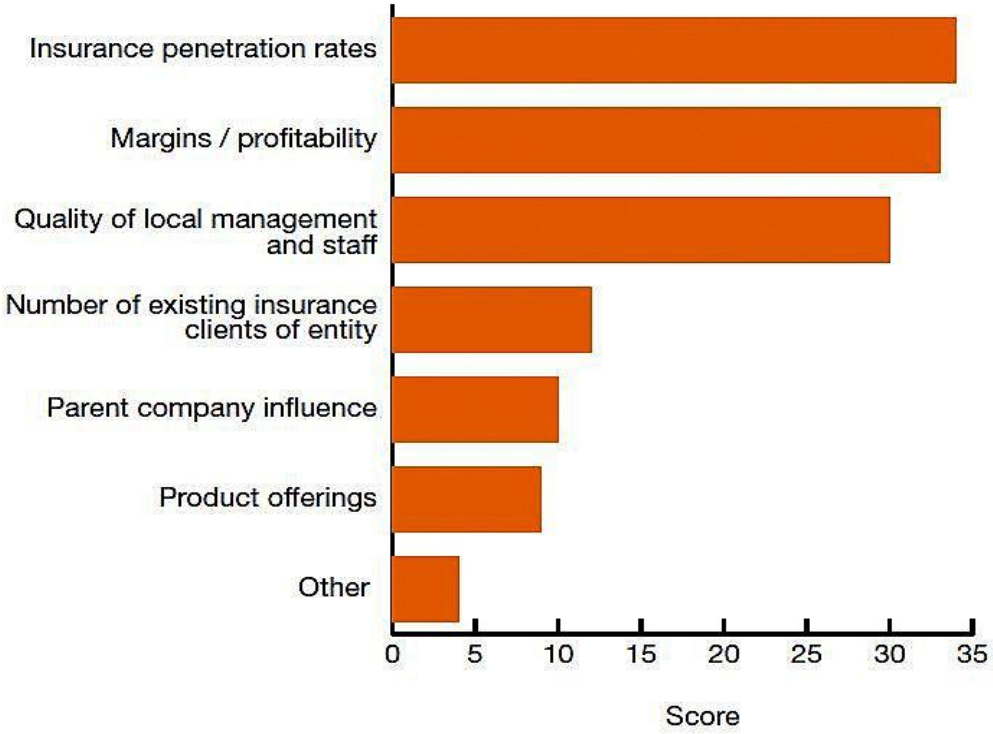
Premiums in 2010 in Africa

	USD bn	World market share
Life	47	1.9%
Non-Life	19	1.1%

Real premium growth



Source: Swiss Re



Gross Premiums Data stats published by Swiss Re indicate:

- **World <u>market share for Africa is just 1.1% for non-life premiums (1.9% life)</u>.**
- **South Africa is dominant in Africa accounting for 90% life and 50% non-life premium volumes.**
- **Premiums as a % of GDP in 2010 in RSA was 2.8% non-life (12.0% life); Nigeria 0.4% (0.1%); Kenya 1.9% (0.9%) ; Namibia 2.3% (5.0%).**

STATE OF THE AFRICAN INSURANCE MARKET. Cont….

	Ranked by premiums	
Life	**2011**	**2021**
United States	1	1
China	5	2
Japan	2	3
France	3	4
United Kingdom	4	5
India	8	6
Italy	6	7
Germay	7	8
Taiwan	10	9
South Korea	9	10
Canada	11	11
Brazil	17	12
South Africa	**13**	**13**
Australia	12	14
Luxenbourg	14	15
Belgium	19	16
Sweden	15	17
Spain	16	18
Switzerland	18	19
Hong Kong	21	20

	Ranked by premiums	
Non-life	**2011**	**2021**
United States	1	1
China	7	2
Germay	2	3
United Kingdom	3	4
Japan	4	5
Netherlands	6	6
France	5	7
South Korea	10	8
Italy	8	9
Canada	9	10
Spain	11	11
Brazil	13	12
Australia	12	13
Russia	14	14
India	18	15
Switzerland	15	16
Turkey	26	17
Belgium	16	18
South Africa	**19**	**19**
Mexico	23	20

Source: Swiss Re Economic Research & Consulting (2012)

STATE OF THE AFRICAN INSURANCE MARKET. Cont….

- Looking back at the last few years, we note that impressive progress, stagnation and discouraging regression continue to coexist on the continent.
- **Cross Border Barriers:** Work permits/Liability limits/Qualifications/Capital requirements/Legislation/Business languages/Culture differences. Foreign insurance covers. Inadequate info exchange?
- The challenging reality: I**nsurance penetration remains low**; **weak economies;** low per-capita income; disposable/discretionary income, low knowledge levels.
- **Regulatory environment challenges**.
- **Capital inadequacy** results in low retentions and high demand for re-insurance. The trend however is companies are increasing risk appetites.
- **Infrastructure bottlenecks:** holding GDP growth back e.g. Power remains the continent's largest infrastructure challenge. Infrastructure improvements added 1% to GDP growth rates over 1990-2005, (World Bank and Agence Française de Développement in 2010, *Africa's Infrastructure: A time for transformation*.)
- **Over-dependence on governments and corporate clients** and the under-development of the individual clients market .
- **Competition from foreign companies aka Globalization.**
- Companies are embracing **ICT in service delivery**

STATE OF THE AFRICAN INSURANCE MARKET. Cont….

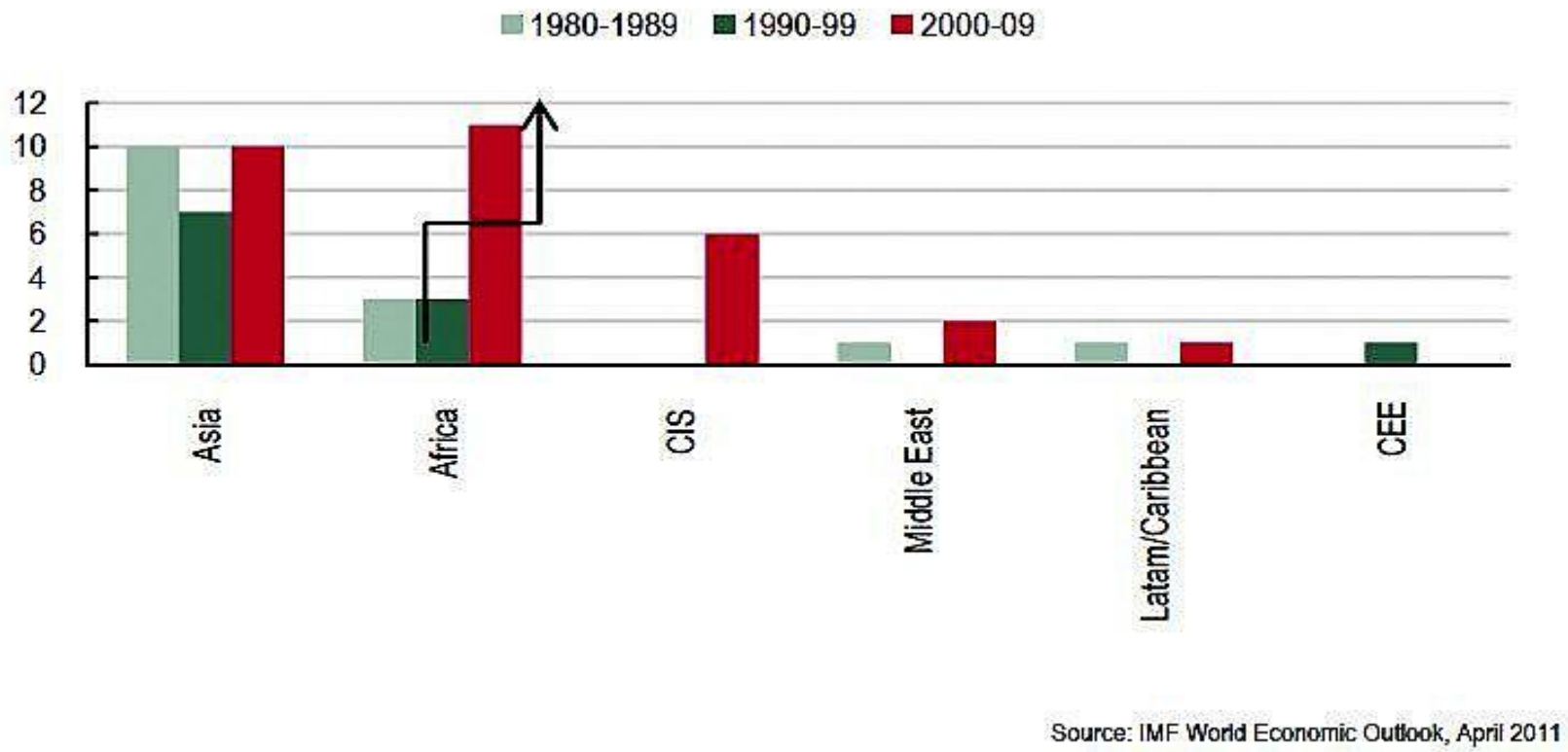
- Rising tide of **consumerism and** demand for sophisticated covers.
- Considerable uncertainty from the **Geo-political instability (**Middle East, North Africa, Somalia) and the unresolved Euro-zone crisis.
- **Basic insurance and reinsurance products** on offer.
- **Skills shortage:** The most pressing issue (list of 45 issues) was identified as the recruitment and training of competent staff (*PWC- South Africa*).
- **Insurance "Systemic Risk" management:** The three most threatening risks to earnings across African borders have been identified as credit risk, environmental risk and liquidity risk.
- Policyholders continue to be the greatest source of **fraud** for short-term insurers versus syndicates for long-term insurers.
- **Cross-industry co-operation limitations.** Communication shortfalls in the insurance value chain in the different levels.
- **Pension law changes are being enacted across Africa allowing for a culture of saving.**
- **Shareholder pressure- focus on short-term profitability** may be overshadowing the need for long-term planning.

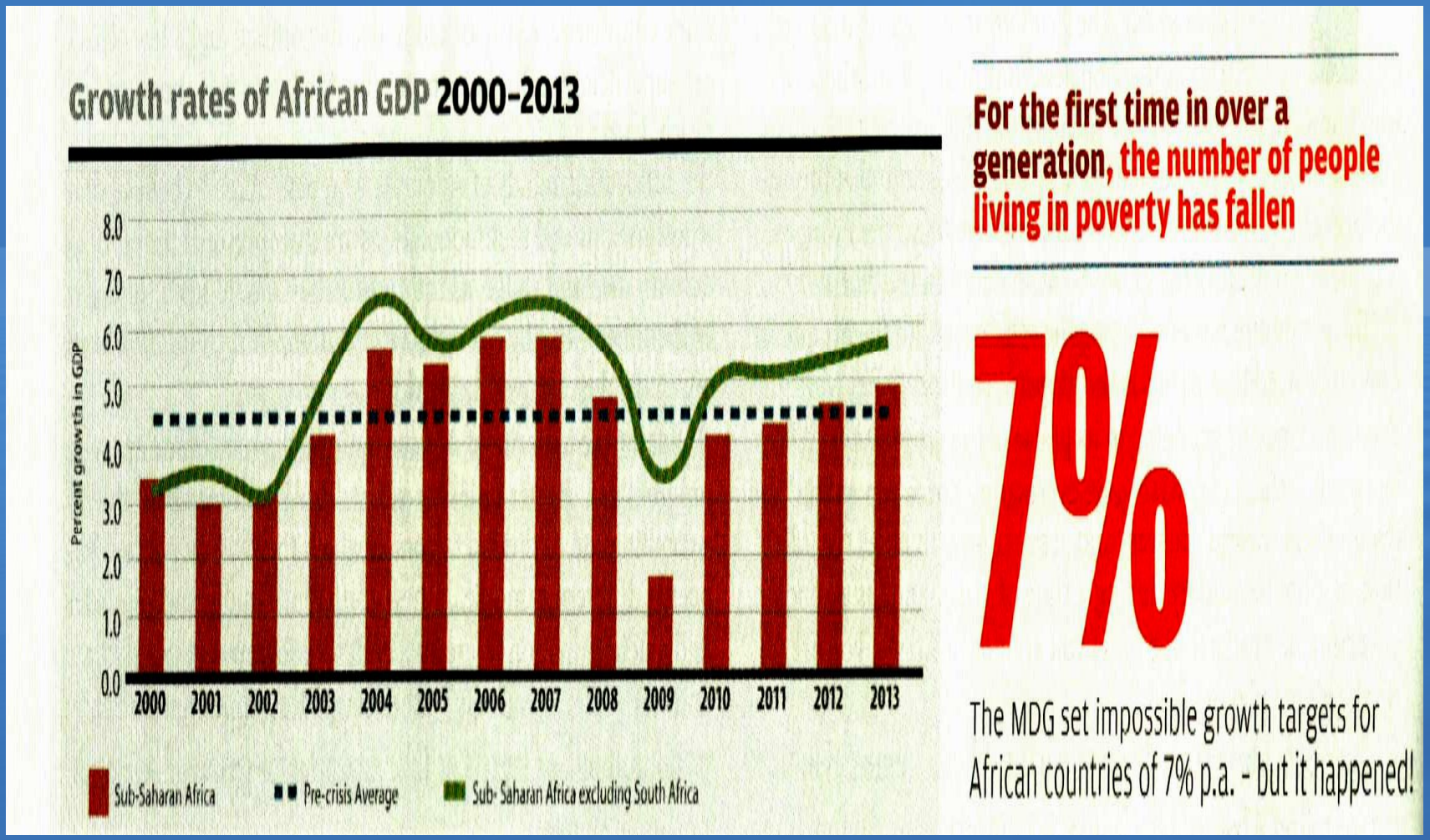
STATE OF THE AFRICAN INSURANCE MARKET. Cont….

- **Inadequate pricing**; Companies compete on price not on service. The net effect is rate cutting which is now widespread and leads to major instability of our markets.
- **Alternative Risk Transfer (ART) & Financial Reinsurances** are still not widely practiced but may have an increased level of activity with globalization and maturing economies .
- **Reinsurance demands are non-sophisticated generally.** International reinsurers provide basic covers, capacities and dictate pricing. African reinsurance pricing disproportionate experiences? (even when markets are considered soft).
- In the last few years most **markets have embraced insurer/re-insurer recapitalization**, necessitating Mergers and Acquisitions (e.g. Ghana, Nigeria, Gambia, Kenya to name a few) .
- African risks are good but **portfolios are largely unbalanced. (??)**
- **Unanswered questions??** Should **micro-insurance** be legislated**?** The **funeral** market…. does it need more oversight**?** Granted on the basic pooling of risks concept affecting global markets however should African markets continue to subsidize losses from other regions? Financial guarantees, do we have enough technical capacity and supervision? etc

Proving africa's direction: Theory and model…..

- **<u>Catch-up economic theory</u> suggests all countries will eventually make the leap from subsistence farming to developed nation status;**
- The fact that **11 booming African nations have already achieved at least 7%** annual growth is yesterday's story.
- **In the graph below:** Africa accelerates past Asia, with the highest number of countries that grew at 7% pa on average over 2000-2009.





Source: African Business June 2012/Africa Progress Report 2011.

The Rostow's Stages of Growth model postulates that economic growth occurs in five basic stages, of varying length:

Stage 1: Traditional society. Agriculture dominates; low per-capita GDP, due to a lack of technology. Hierarchical society.	Africa was agricultural and held back by very low education levels in 1960. Political leaders followed foreign models with little relevance for Africa
Stage 2: Take-off Preconditions (Occurs within 10-50 yrs.) Secular education, formation of entrepreneurial class; some capital mobilisation, with currency and banking, and modest manufacturing. Take-off To enter the second stage requires an effective banking system.	Primary schooling is now virtually universal; secondary schooling enrolment is up nearly tenfold since 1960. Botswana and Mauritius have secondary school enrolment levels better than China or India. Stock market investors in Ghana, Nigeria, Kenya and Rwanda have effective banking systems are in place. Anecdotal evidence that educated and internationally trained African professionals are to use their skills in the strong growth economies in the continent.
Stage 3: Take-off. (Maturity is reached after 50-100 yrs) Equivalent in effect to industrial revolution. When the rate of productive investment rises from 5% to 10% or more of national income, and one or more substantial manufacturing sectors demonstrates a high rate of growth. Sector-led growth becomes common. Economic processes, rather than tradition, predominate. One study suggests that achieving 25 years of 7% annual growth requires 25% investment/GDP ratios (Micheal Spence, Nobel Peace prize winner)	With the internet, services might replace manufacturing as the growth driver in Africa; Foreign financing might help boost investment; External debt/GDP ratios in 2010 very low in Sub Saharan Africa generally; As Chinese wages rise, Africa may win manufacturing market share too. Africa is now going through a population explosion as China begins to experience demographic shortages ; Mobile banking may also help pull rural etc savings into the formal economy; Domestically owned savings held abroad are high – and could return. High growth in Rwanda or Ethiopia may be linked to easier business regulation (Institutional developments). Loan to deposit ratios are healthy.
Stage 4: Drive to maturity. Investment rates of 10-20% Extend technology across the economy, and keep growth above population increase. New sectors take over from previous growth sectors. Poverty rates fall.	
Stage 5: Age of high mass-consumption. This enables countries to concentrate on their specific priorities, e.g. military/security issues, equality/welfare issues, luxuries for their elites.	

NOTE!! Aside from Mauritius, SA and Botswana, most African Countries are only now entering the third stage, and making the transition to Stage 4.

Emerging trends…..

Collage created from picture excerpts from PWC, Insurance, May 2012

Emerging trends…..

Africa today

$1.6 trillion
Africa's collective GDP in 2008, roughly equal to Brazil's or Russia's

$860 billion
Africa's combined consumer spending in 2008

316 million
the number of new mobile phone subscribers signed up in Africa since 2000

60% Africa's share of the world's total amount of uncultivated, arable land

52 the number of African cities with more than 1 million people each

20 the number of African companies with revenues of at least $3 billion

Africa tomorrow

$2.6 trillion
Africa's collective GDP in 2020

$1.4 trillion
Africa's consumer spending in 2020

1.1 billion
the number of Africans of working age in 2040

128 million
the number of African households with discretionary income in 2020

50% the portion of Africans living in cities by 2030

Mckinsey Global Institute: Lions on the move, The Progress and Potential of African Economies. 2010

INSURANCE TREND DRIVERS

We believe the items below will lead to primary insurer generic growth (market penetration; market development; product development; and diversification) the effect of which will be beneficial to the African reinsurance sector as a whole.

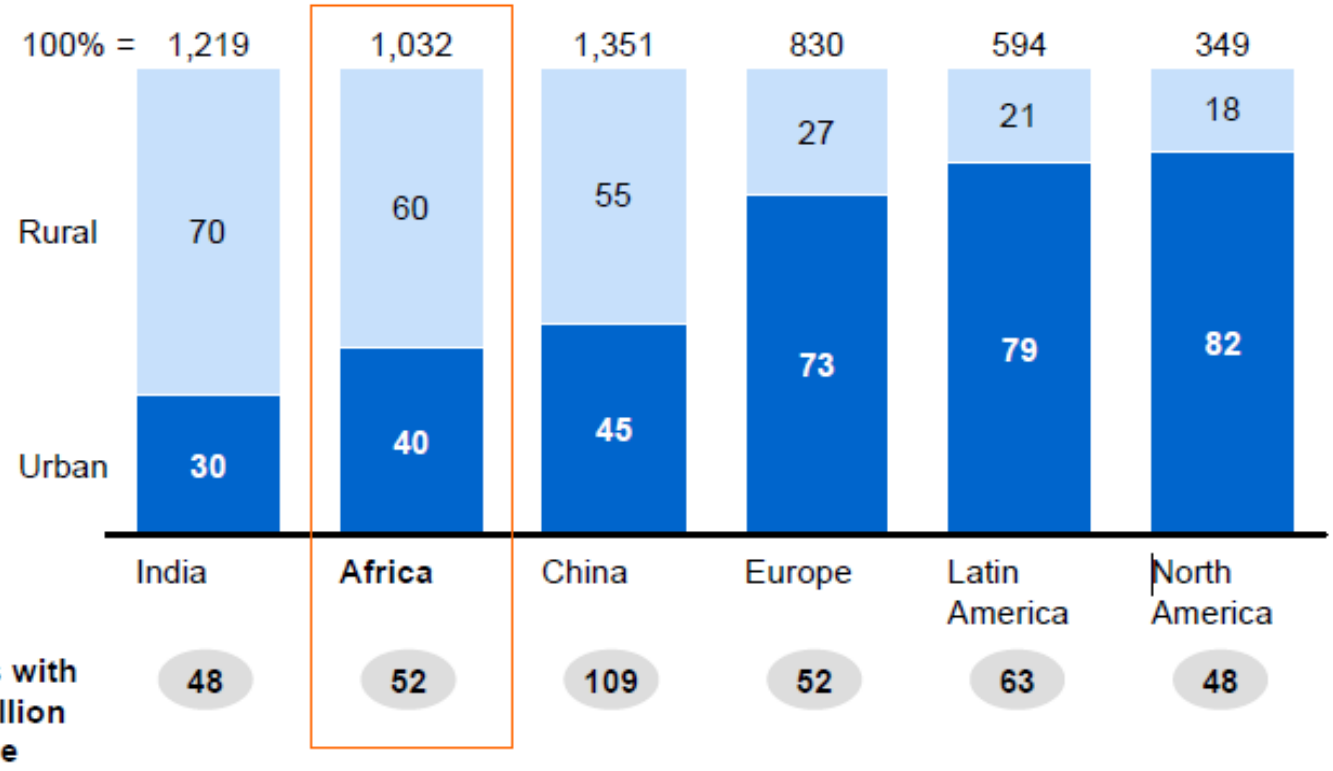
- **Motor insurance:** The proliferation of cars, the number of unlicensed drivers and the complexity and cost of car repairs will cause major changes in this sector.
- **Deepening regional integration** holds enormous potential for economic growth and social development across Africa, with spillover effects on the insurance industry.
- **First-time customers/ Urbanization:** Changing demographics has created new customers previously not seen in short and long-term markets; most of these not ascribing to the "old way" of doing business. More people in urban areas with higher levels of disposal income will also be good for producers. (Renaissance Capital, 2011).
- **Food production:** Africa will have to feed the world. Industrial-scale farming is likely to be a hallmark of African farming in the future.
- Africa will continue to **profit from rising global demand** for oil, natural gas, minerals, food, and arable land.
- **Convergence**: A blurring of the lines between insurance, investments, banking and medical protection.
- **E-business development**: The internet is gaining traction and increased distribution through this channel is anticipated.
- **Direct distribution**: "Several companies mentioned the trend to direct distribution" (PWC- 2012).

INSURANCE TREND DRIVERS,,,Cont

- **Consumer protection:** Greater attention will need to be devoted to consumer protection and its impact on insurance covers and service provision.
- **Mobile Telephony/Social changes,** e.g. changing customer behaviour, "fuelled by social networking, new customer expectations for speed and simplicity in an increasingly mobile internet environment and increasing risk awareness, are shifting the balance of power from intermediaries to customers." (PWC- 2012).
- **ICT and Technological advances**, "*driven by the exponential growth in smart-phones, tablets and mobile internet as well as sensors and other devices connected to the internet, present opportunities for better underwriting and proactive loss control for innovative insurers*." (PWC- 2012).
- **Change Drivers** that have and may significantly impact on current global insurance and reinsurance business cycle include; i)Terrorism/ Geo-Political instability, ii) Escalating CAT Losses from Natural Catastrophes all over the world in 2011. Insured Losses from natural disasters for 2011 half year US$67billion (2010 US$27billion) *source: Swiss re*
- "*The attraction of lower **insurance penetration rates** in most African countries, their relatively high GDP growth rates and prospects of higher margins all point to a new push for geographic expansion on the continent.*" (PWC- 2012)
- **Regulation/Risk management.** Own Risk and Solvency Assessment (ORSA) is the cornerstone of the EU's Solvency II Directive that the South african market is already embracing. Insurers will be required to make a self-assessment of the capital available to support their business risks. Regulators use this information to better understand the risks identified and judge the adequacy of capital available.

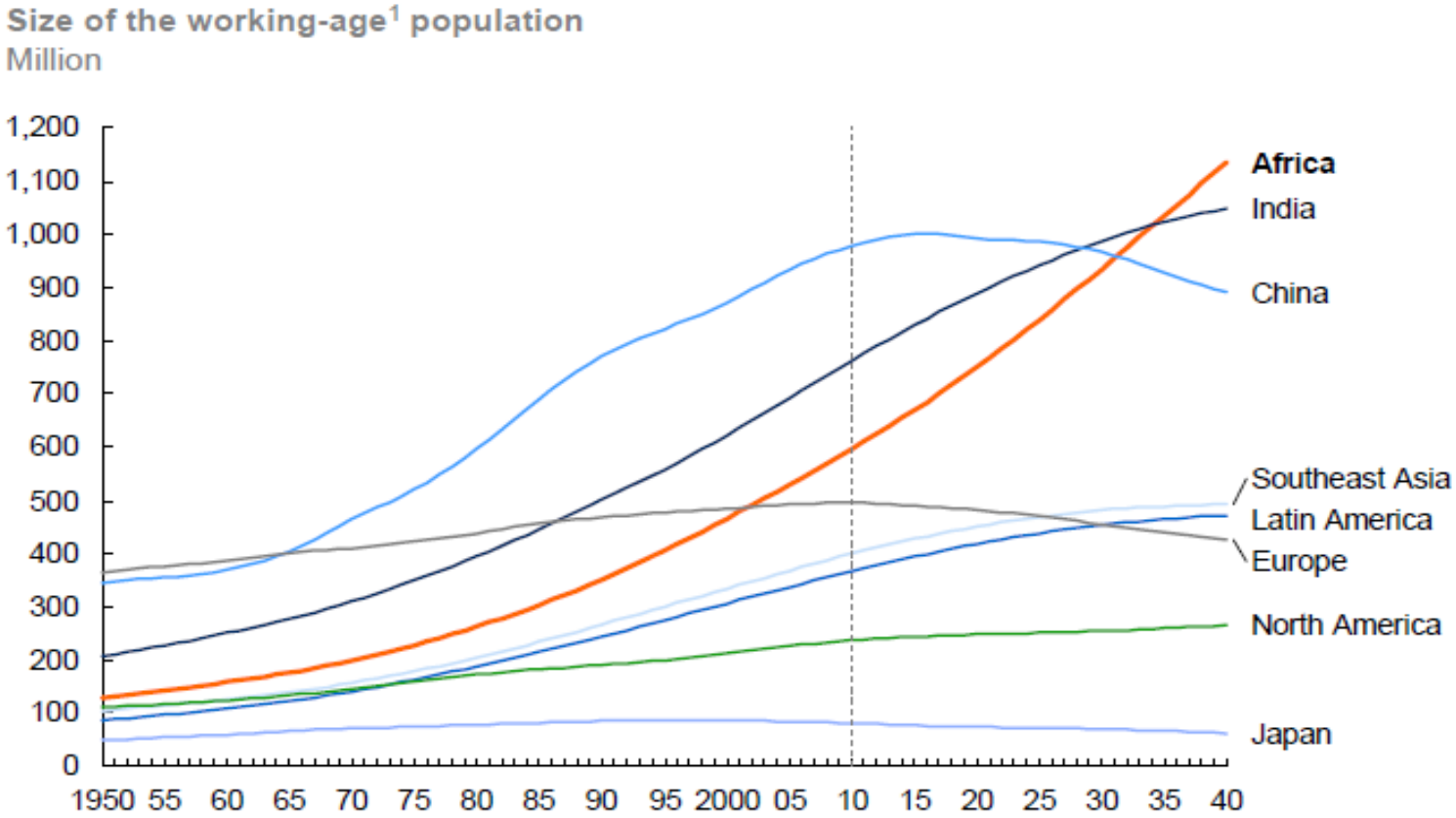
Africa is almost as urbanized as China and has as many cities of 1 million people as Europe

Share of rural vs. urban population by region, 2010
%, million



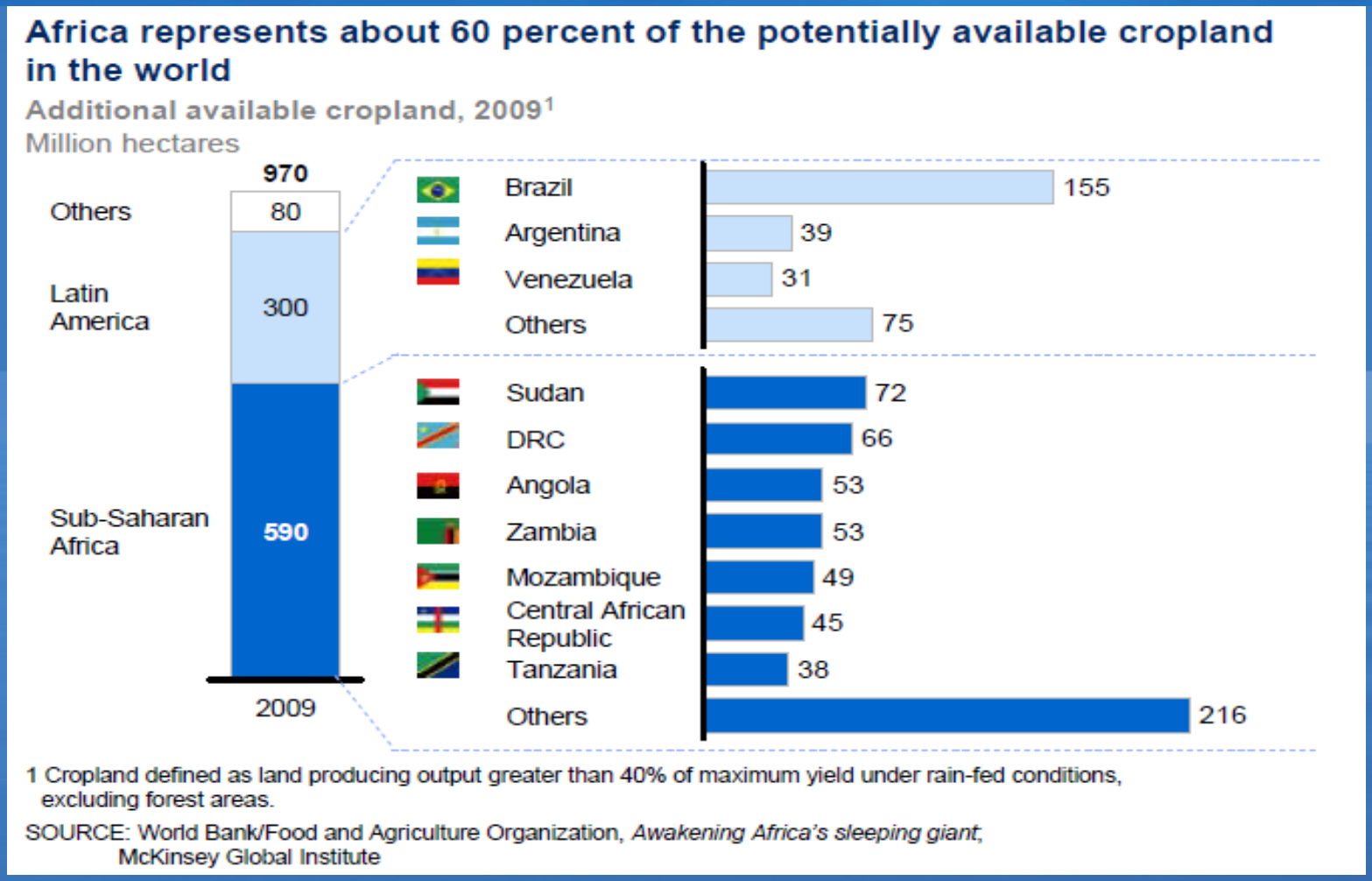
SOURCE: United Nations; McKinsey Global Institute

Africa's workforce will become the world's largest by 2040



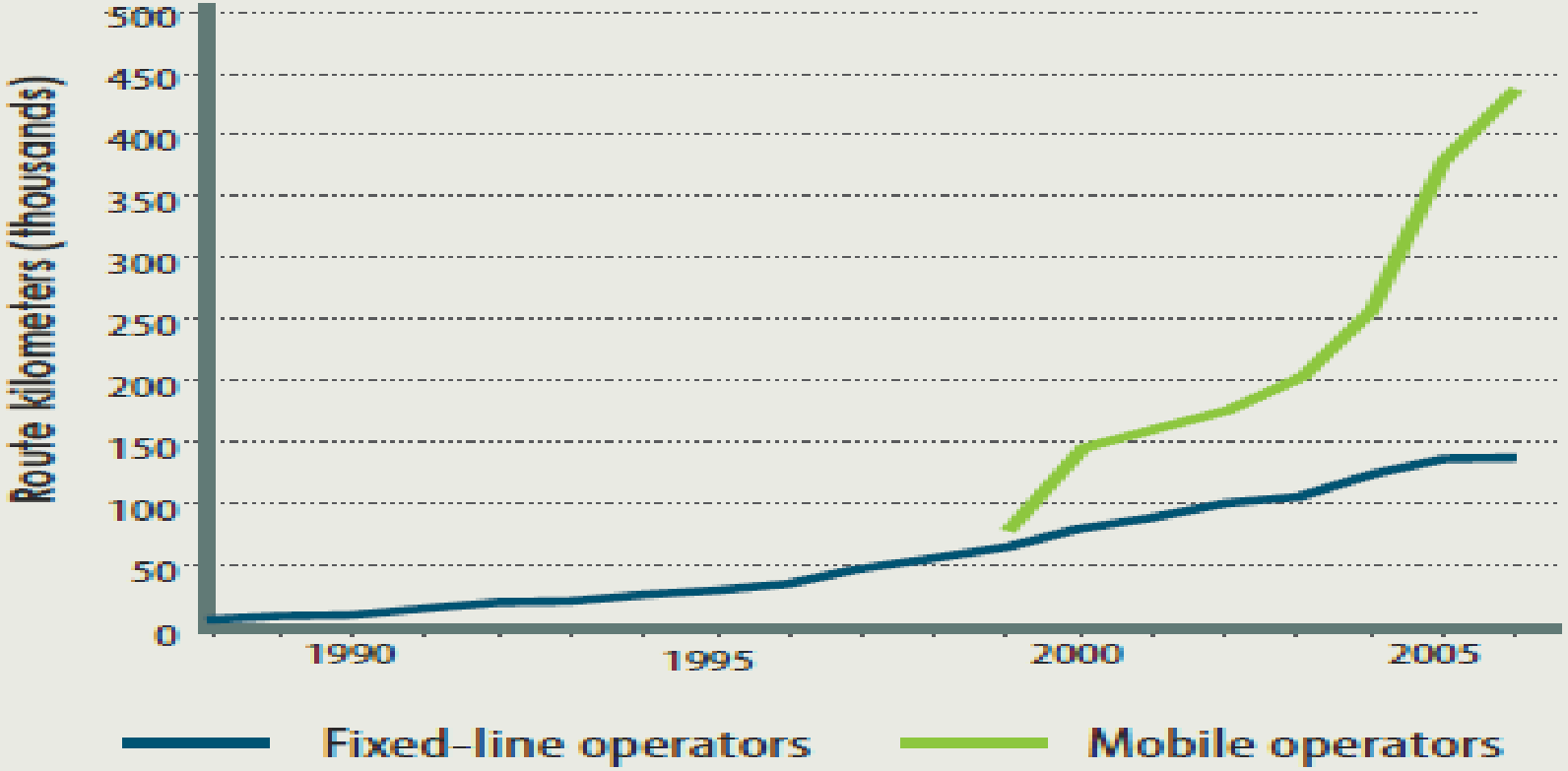
1 Population aged 15–64.

SOURCE: United Nations World Population Prospect; McKinsey Global Institute



Ceteris paribus *"If Africa could raise yields in key crop s to 80% of the world average, similar to the achievements of other countries that experienced a green revolution in Agriculture, the continent would increase the value of its agricultural production by US$ 235 billion over the next two decades"* Mckinsey Global Institute 2010.

THE GROWTH OF THE MOBILE NETWORK



Source: Williams (2010), Broadband for Africa: Backbone Networks in Sub-Saharan Africa, World Bank, USA.

CONCLUSION & RECOMMENDATIONS

- African Insurers as providers of insurance resources, innovation and expertise should consider:
  - Managing shareholder/ stakeholder expectations.
  - Lobbying governments for common regulation.
  - modifying business models to target the poor or integrate local communities and producers by aggregation into their value chains
  - Better Communication: practical and regular information sharing fora, perhaps embracing the e-solutions.
  - Instituting viable R & D set-ups that redefine insurance product offerings to be reflective of the needs of the African consumer.
  - Recapitalizing and retaining more to enable them play a primary role in providing capacity for the African continent.
  - Improving on fundamentals and get rated by appropriate rating agencies.
  - Cost reduction.

CONCLUSION & RECOMMENDATIONS

- Investing heavily in human capital development and better underwriting skills. , especially in the area of specialized risks e.g. Oil & Energy, Aviation etceteras .
- Devotion of ample attention consumer protection/consumerism and the increasing demand for sophisticated covers.
- Embracing technology to tame "big data" , harness opportunities and introduce modern products, Investing in customized reinsurance solutions and customer relationship management software.
- Creation of a common user service provider by African reinsurance companies in the area of R & D, specialized risks, risk management, etceteras.
- Improve on Risk Management, Corporate Governance and Fraud detection.
- Embarking on cost optimization to reduce cost of doing business and enable increased product access by publics. Avoid cash flow underwriting.

<u>International Reinsurers should consider:</u> Applying differential pricing models in Africa; giving due cognizance to aspects like differences in exposure and experience in pricing covers.

CONCLUSION & RECOMMENDATIONS

Regulatory Authorities may consider;

- Having a candid systemic risk study within their economies and trading regions.
- Partnerships with other regulators in areas like common cross border regulation. Creating accessible and regulators training capacity to create technical expertise to supervise emerging issues. Grow market analytical skills.
- Distinguishing between traditional insurance and micro-insurance (caters for the poor or those who are vulnerable to poverty). To increase penetration and ease product design.
- Creating an enabling environment on current product regulation, taxes etc.
- Enabling "bundled product" regulation that cuts across banking/insurance/investments/pensions/medical protection etceteras and prepare for revolutionary selling platforms like mobile companies.
- Encouraging insurance companies to explore other methods of Risk financing other than the traditional.
- **Generally:** Grow partnerships harnessing a broader range of actors, their energy, creativity and resources to fill the gaps.
- Establishing practical common working groups with clear TOR's. Establish a well supported Insurance Centre of Excellence to up professional standards.

END.

THANK YOU.

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