SANTAM

INSURANCE BAROMETER REPORT

2019

santam

CONTENTS

Introduction

The future of the insurance model

Quinten Matthew,
Executive Head:
Specialist Business

Santam's claims statistics from the past few years point to the undeniable truth that the risk landscape has rapidly become more hostile. From the abnormally high fire risk across South Africa, to the rise in extreme weather events and the general deterioration of infrastructure – both the commercial and personal lines markets are facing greater risks than ever before.

At the time of writing, South Africa was processing the grim picture that the recent 2019 Medium Term Budget Policy Statement painted about the state of the country's finances and efforts to restore financial sustainability to a struggling Eskom.

The risks that South African consumers and businesses face on a daily basis cannot be detached from our country's struggling economy, nor its political and regulatory risk factors. A clear message delivered by our Minister of Finance, Tito Mboweni at the end of October, is that these problems are far from over, and are likely to intensify over the coming years.

Poor business performance, low levels of business confidence, high incidence of crime, elevated business interruption risk, and accidental damage to personal property, can be directly linked to one or more of the identified concerns.

The knock-on effect of all these factors is diminishing the insurance industry's capacity to absorb monetary losses. The role of insurers to act as economic enablers is becoming more important than ever before. However, insurers face significant risks which threaten our business models, and it has become

clear that the industry will need to make important changes to remain relevant. This means changing the way we do insurance and engage with our stakeholders, especially our clients. The products and solutions we offer must evolve if we are to continue to add value to our clients.

We must recognise that the old way of thinking around risk pricing is becoming less viable with each passing year. Continuously hardening insurance premiums in response to rising claim risks is nothing more than a short-term solution. This hardening cycle has provided some relief for a number of our insurance categories, giving the insurance pool a chance to recover and regain some resilience. However, real growth in terms of policy numbers still eludes us.

As South Africa's largest insurer, with over 101 years of experience, we believe we have a responsibility to drive innovation and do our part in building a more resilient market. The Santam Insurance Barometer Report aims to shine a spotlight on the role of insurance in the economy, risk trends impacting South Africa, insurance as a risk mitigation tool, the important role that intermediaries play, and opportunities for the industry.

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We incorporated data gathered from our in-depth survey involving hundreds of businesses, consumers and intermediaries. This report explores the prevailing perceptions on a broad range of challenges that must be carefully navigated for future sustainability. The survey enabled us to gain valuable insight into how the various markets view their most prominent risks, how well their actual exposures are managed, and the gaps that we as insurers must address.

Combining this with expert insights from industry veterans, we believe we have produced a report that provides a holistic view of the insurance sector today and what lies ahead. This process has influenced our view on how to better service our market and, by sharing the output with all our stakeholders, we aim to raise awareness of the prevailing risks and opportunities.

We hope to stimulate ongoing engagement and encourage conversations to find new ways of adding value within this changing landscape. We thank all the businesses, intermediaries and participants who took the time to provide us with their valuable input. Without them, this report would not have been possible.

Desk research

including telephone interviews with global insurers

1 hour in-depth interviews with 24 intermediaries

9 independent brokers

11 national brokers

4 tied agents

10 corporates

9 commercial businesses

5 personal

30 minute

face-to-face interviews with

50 corporates

119 commercial businesses

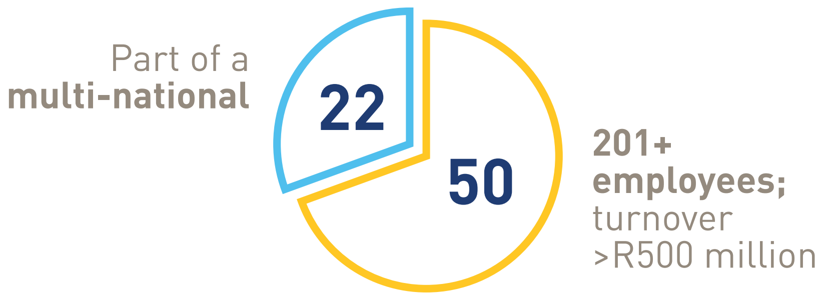
250 consumers

Research period

January - July 2019

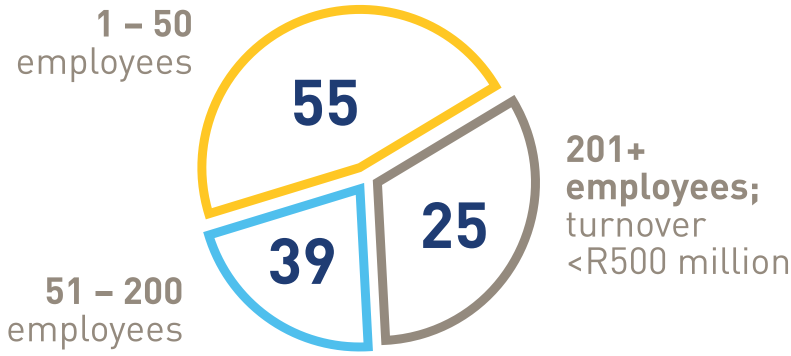
Corporates

total sample size (50)



Commercial

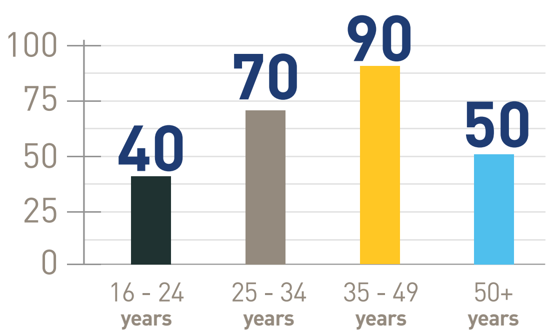
total sample size (119)



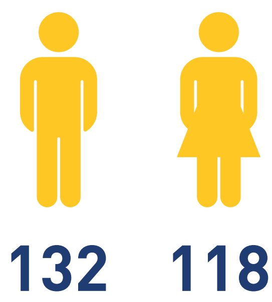
Consumers

total sample size (250)

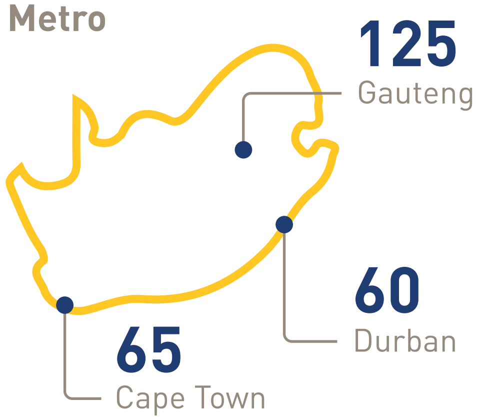
Age



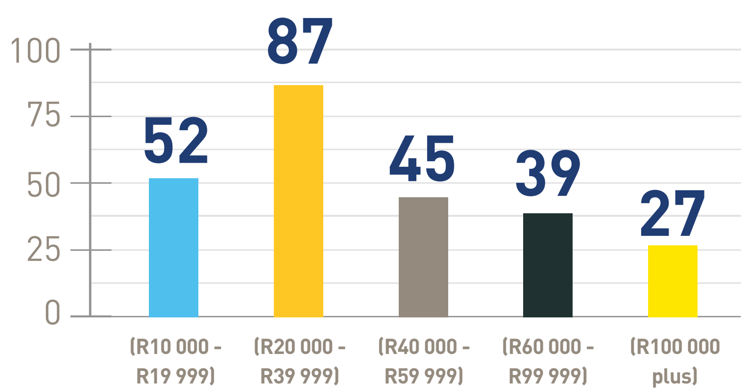
Gender



Metro



Household income (monthly)



Key themes and trends

Crime

- Theft
- Burglary

Political landscape

- Political unrest
- Social change

Economic landscape

- Challenging economy
- Business confidence

Road accidents

- High number of uninsured cars
- Unlicensed drivers

Climate change

- Natural catastrophes
- Loss of crop yield

Fire risk

- Wildfires
- Firefighting capabilities

Cyber crime

- IT failure and business interruption
- Data breaches and theft

Technology

- Increased cyber incidents
- Automation

Regulatory changes

- Increased cost of compliance
- Smaller intermediaries under threat

Skills shortage

- Challenge in attracting young professionals

Intermediated Business

Monetising added value

Andrew Coutts,
Head: Intermediated Business

The nature of insurance in South Africa is changing from risk transference to risk mitigation, and the relationship between the insurer, client and intermediary is evolving as a result. While this is a positive trend for everyone in the insurance value chain, it is crucial to understand how the evolution of the industry will affect the role of the insurer and the intermediary within this new dynamic.

It is important to acknowledge that market and regulatory changes are fundamentally moving the entire financial services industry to a more outcomes-based model. For insurers, this means adapting the way that our businesses are structured to models that are much more client-focused, as opposed to the product-focused models of the past.

Historically notorious for its 'fine print', insurance is still seen as a grudge purchase, particularly in the tough economic climate. Given these challenges, Santam has shifted its focus and is working hard to transform the way we do insurance. Santam's aim is to be viewed as a lifestyle partner in the personal lines market, and a business enabler in the commercial lines market. This means that we must evolve from providers of insurance through risk transfer, to providing more than insurance through risk mitigation.

Market and regulatory changes are fundamentally moving the entire financial services industry to a more outcomes-based model.

The simple truth is that any insurer that does not offer more than insurance is increasingly going to struggle to maintain relevance in the market.

The intermediary is central to making this a reality. Intermediated insurers rely on intermediaries for a number of critical functions including marketing, sales and servicing, advice and to an increasing degree risk management. Insurers count on them to conduct valuable, in-depth needs analyses in order to properly understand the complexities around a client's risk exposure. Insurers and intermediaries must use that information to ensure we add value for clients where needed, thereby demonstrating the true value of insurance in a changing world.

Intermediaries add significant value to the insurer and the client as a distribution channel. According to the research findings, the majority (**82%**) of commercial businesses surveyed said they relied on intermediaries for advice based on their knowledge and expertise. Consumers closely echoed this, with **71%** stating the same. Over **68%** of businesses listed receiving the best deal as the second leading benefit of using an intermediary. However, this ranked 8th among consumers with just **32%**. For consumers, understanding their needs came in second with **60%**. A further **64%** of businesses ranked identifying risk exposure as their third reason for using an intermediary, and **45%** of consumers listed explaining products as the third best benefit of using an intermediary.

At Santam, we believe that the intermediary's value proposition is not only entrenched in the sales process; it is equally embedded in the claims handling process. Advocacy for the client at claims stage is crucial, in our view. In the survey, **63%** of businesses ranked efficient claims handling as the fourth leading benefit of using an intermediary, while consumers ranked removing claims hassle fifth at **36%**. Standing on behalf of the client ensures equitable treatment at policy renewal stage and aids greatly in client retention. The intermediary also fulfils a vital role at renewal stage – a discussion that should be centred on finding out how a client's risks have evolved.

While it could be argued that the intermediary's role (especially in personal lines) is diminishing as aresult of increasing competition from direct insurers, emerging trends in the direct insurance market demonstrate the importance of intermediated insurance. In an industry where the churn rate is high, many direct insurers recognised the role that intermediaries play in lowering this, leading to some introducing liaisons to interact with the client personally.

Technology is another major driver of change in our industry, with connectivity and the Internet of Things (IoT) playing an increasingly important role in risk management. For instance, interventions such as leak detectors on geyser units can identify problems with a unit long before they escalate to the point of bursting. This means that insurers can replace geysers before they lead to massive consequential losses in the form of electrical, structural and other damage to home contents. Many other examples like driver telematics, app-enabled home security, water pressure management and electricity supply management help clients and insurers reduce claim size and frequency by proactively managing their risks.

Looking from the viewpoint of insurers, and their shareholders, there is great benefit to avoiding consequential losses, since these tend to make up the bulk of the final claim. There is also a considerable advantage for the client, as consequential losses often affect uninsured items. By removing the need to claim through better risk management, one reduces the disruption to an individual's life or to a business.

However, this is also where the intermediary is most affected. Positively, intermediaries are well positioned to generate new revenue streams as technology enables clients to spend more effectively on risk management to reduce claims and save on insurance premiums. Adversely, if insurance premiums decrease as a result of better risk management, commissions reduce proportionately, which places more strain on an intermediary's already reducing margins.

In addition, the regulatory environment has impacted the intermediary's business model. One of the points raised by many respondents in the survey is that the time and cost of compliance has started to put smaller brokerages under threat. Regulatory changes have already pushed some intermediaries out of the market and certain requirements has the effect of creating barriers for new business start-ups.

This is not merely a perception. Intermediaries have historically expended the lion's share of their time servicing clients, but current regulations have them spending up to **70%** of their time doing administrative work compared to just **30%** servicing clients. It reduces their capacity to find new clients and to service more clients effectively to make up for their truncated profit margins.

Insurers and intermediaries are now faced with the question of how to reconcile this new approach to reduce risk and premiums whilst still retaining and growing their revenue streams. Firstly, we must view risk mitigation as a means of adding value to the client.

82% commercial businesses VS **71%** consumers rely on intermediaries for advice based on their knowledge and expertise

In an industry where the rate of client churn is high, many direct insurers recognise the role that intermediaries play in lowering churn rate.

We must convince the consumer and businesses that an insurer and intermediary that remove the need to claim, are more valuable than an insurer that just pays claims.

Keeping the aforementioned argument of the potential for reduced premiums in mind – another option is to keep premiums unchanged but increase the inclusive value added benefits to the consumer in order to justify the cost.

Giving the client access to risk management information and alerts, adding technology such as geyser sensors and offering a direct line to the insurer and intermediary through online portals and apps would improve client service while ensuring that the insurer benefits from reduced claims, and the intermediary by maintaining their profit margin.

By the same token, insurers can improve their service to intermediaries by means of Artficial Intelligence (AI) enabled portals and services that will reduce the excessive amount of time that intermediaries spend on administration while ensuring that they are compliant with regulations. Santam has made great strides in this area, with a host of services available to intermediaries via digital platforms, from risk services and pricing to administration. The adoption of an omni-channel approach provides both intermediaries and their clients with a choice of interaction mechanisms.

Providing options that help intermediaries function optimally frees them up to properly service existing clients while still being able to secure new business, resulting in a win-win for all stakeholders in this relationship.

As stated, the intermediary adds immense value in the insurance value chain. However, the client is still at the centre of this relationship, and intermediaries are adapting and upskilling themselves to remain relevant and valuable.

It is vital for intermediaries to acknowledge that their business models must change to keep pace with the evolving market. The survey indicates that there is already a significant amount of change taking place in the intermediary market, with most respondents noting that there is a trend towards intermediaries becoming more niched, as advisors to mid and large commercial clients. We have seen that the intermediaries that choose to specialise in specific fields, tend to be more successful.

In addition to this, we have seen many independent intermediaries consolidating in order to expand in scale and expertise, and facilitate investments in technology to enhance their competitive edge. Consolidation in the market enables

63%
of businesses
+
36%
of consumers

ranked efficient claims handling as a benefit of using an intermediary

intermediaries to share a back office and focus more of their efforts on growth. There are also those who are moving from a pure intermediary model to an agency model, such as Sanlam Blue Star where they can receive a greater degree of support and specialist training.

Consumer expectations are changing, and so are their preferences for interacting with their service providers.

At Santam, we continue to believe that there are significant benefits for all stakeholders in introducing our products to the market via intermediated channels. Not only is the intermediary able to promote his or her business, but the client gains a much better understanding of the insurance solutions available.

On the one hand, marketing has never been more accessible thanks to social media. However, the biggest challenge in this regard is that the digital know-how can be problematic for many intermediaries. Indeed, many do not even have websites. If this is the case for an intermediary, our advice is to bring young employees into the practice that can use alternative channels to market while existing employees continue to provide the core insurance acumen.

It is also worth noting that direct insurance has gained a lot of traction, especially in the personal lines market, because it capitalises on perceived ease of use. Being able to access an insurer via online channels or even at the tills of major retailers makes it significantly more easy for consumers to acquire insurance, and feeds into the perception that all aspects of the product (from underwriting to claims stage) are quicker and faster than working through an intermediary.

The consumers that we surveyed listed the main benefits of direct insurance as being cheaper, quicker and having less paperwork. We can logically argue that dealing with an intermediary can be better in all three of the above categories, but the only real way to combat these perceptions is for intermediaries to evolve in the way that they reach and interact with their client base more frequently and demonstrate the ease of doing business with them.

With all this in mind, we believe that significant responsibility lies with insurers to make sure that clients and intermediaries are able to function optimally in this evolving landscape. Enacting change collectively as an industry, finding new ways to monetise the value that we add to clients through risk mitigation, and leveraging digitisation to reduce cost and actively expand our market reach are the elements of a roadmap that moves everyone in the value chain forward.

The IoT is playing an increasingly important role in risk management.

Expanding the Black Intermediary Base

Embracing transformation

Sagie Pillay, Special Projects Manager: Black Broker Development

Transformation is a key driver in the evolution of the short-term insurance industry. To keep pace with these changes we must adapt and develop inclusive solutions. We are at the point where all major commercial entities in South Africa has set transformation goals for itself; goals that must seek to address the deep-rooted challenges that prohibit real growth and inclusivity.

With a renewed focus to prioritise our black broker development programme, Santam set out clear objectives to grow the number of black intermediaries that have contracts. We believe that with the right focus and execution, this could be a vital component in transforming the sector. The impact of transformation in the insurance industry goes far beyond increasing employment opportunities. Indeed, our efforts in this arena are now informing the way forward for the evolution of products and services in order to remain relevant in an ever-evolving, dynamic market.

For the year 2019, Santam's target is to expand the black intermediary base by **20%**. However, to do this effectively, we also need to expand our client base in order to have the required numbers to support these individuals in their respective regions.

The opportunity to expand our black intermediary base presents great potential, and points towards the fact that there is still a significant lack of real market penetration for insurance across the country. This is growing with the support of our programme. This year's winner of Santam's regional Diamond Broker Award for the Limpopo region, is a black intermediary. This is particularly encouraging, as the recipient of this coveted award must outperform all their peers by premium against a metric that rewards the growth and profitability of their portfolio.

Though slow, transformation is progressing and the South African market is evolving. The black middle class is growing and has disposable income to buy vehicles, property and build businesses. However, we have yet to tap into this thriving segment of the market that represents the largest proportion of our population.

With that in mind, the key to effectively growing the number of black intermediaries in the short-term insurance industry is to provide them with the right level of support and remove some of the existing challenges that these intermediaries face.

Regulatory changes, though beneficial in many ways, have brought new challenges for emerging intermediaries and many of the new entrants are not yet Financial Advisory and Intermediary Services Act (FAIS) compliant. To overcome this hurdle, guidance throughout the initial steps is required. This is where joining an agency model such as Sanlam Blue Star is beneficial. We help smooth out this

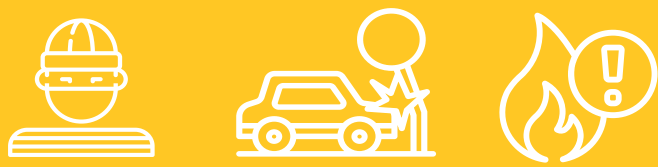
Santam's target is to expand the black intermediary base by 20% in 2019.

Regulatory changes have brought new challenges for emerging intermediaries and many new entrants are not yet FAIS compliant.

process by providing the necessary training to upskill and empower this new era of intermediaries. Additionally, we need to introduce and establish connections between the relevant industry bodies and our black intermediary base to assist them with navigating regulatory and licensing conditions.

Attracting young, new intermediaries into the industry has proved difficult. One of the challenges we see is many new entrants to the insurance industry prefer to start their careers at large corporates instead of becoming intermediaries. In aid of attracting more young black intermediaries, we use training as a

We cannot be prescriptive, we must allow our solutions for the emerging market to be informed by our black intermediaries.



The most significant risks to commercial respondents are **theft**, **motor vehicle accidents** and **fire**.

means of incentivising them to consider building careers as intermediaries.

Expanding the base of black intermediaries in the market is a necessary measure for adding new talent to the industry.

As part of Santam's renewed focus to develop this segment, we established 15 target regions during the past year and appointed a relationship manager for each region. The mandate of these relationship managers is to interact with black intermediaries and provide the necessary administrative support, so that the intermediaries can focus on servicing and securing new business.

We had to establish open lines of communication. We did this through regional engagement forums to better understand their specific challenges and frustrations. These sessions proved to be invaluable and have resulted in a significant amount of information we are using to drive our transformation programme forward.

Through our interactions with intermediaries in underserviced regions, we are gaining critical insight into the unique needs of this market. We are realising that many of the common assumptions regarding the risk profiles in underserviced areas are inaccurate.

By way of example, the survey shows us that the most significant risks to commercial respondents are theft, motor vehicle accidents and fire. These line up with our claims data in regions where there is a reasonable degree of insurance market penetration. However, through the information that we received from our growing black intermediary base, it is becoming clear that theft risk is much lower than expected in certain regions, while risks such as fire and floods rate significantly higher. This new information prompted us to re-evaluate certain aspects of our geographic rating models.

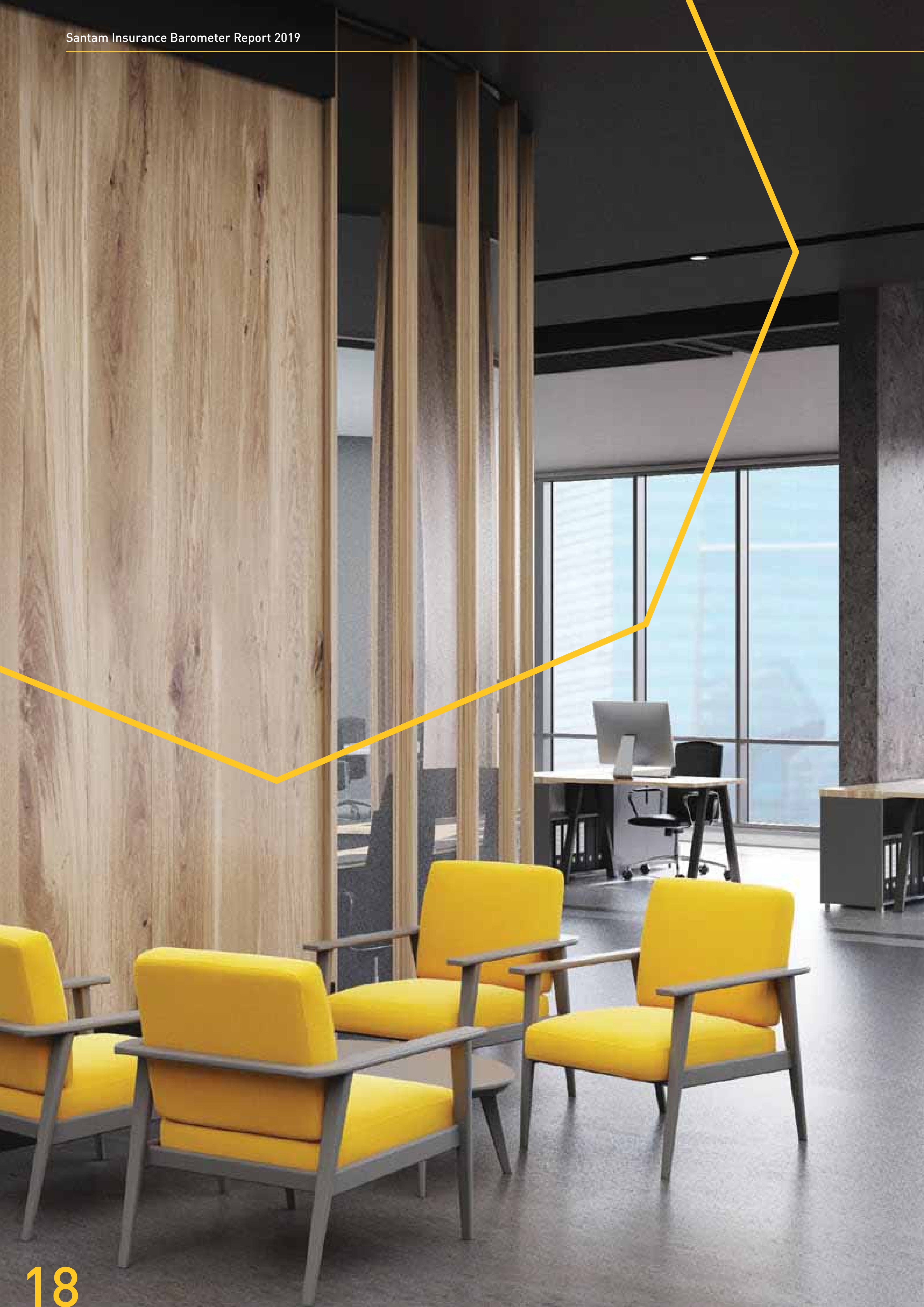
The survey also shows that for respondents that have experience in dealing with intermediaries, there are clear advantages – with knowledge and expertise being the foremost of these. We need to be sensitive to the fact that black intermediaries have to establish this same level of understanding among clients with little to no experience with insurance.

We need to go back to the insights gained on how our products and price points should be structured in order to meet the needs of this new market. The feedback that we receive informs the evolution of insurance and risk management solutions that will guarantee insurance remains relevant and elevates the benefit that we offer clients.

The next step is to design relevant solutions that are tailor-made for the rising black middle-class, thereby allowing intermediaries to introduce insurance to this untapped market.

In order to make real strides forward, it is imperative that we engage with our black intermediaries in a meaningful way and that they are skilled in selling our products. For a relatively small investment of time and money, we believe the returns can be hugely beneficial. We cannot, however, be prescriptive, and will allow our solutions for the emerging market to be informed by our black intermediaries.

At our current pace we are well on our way to meet the **20%** target we have set for ourselves, which will hopefully see Santam bringing increasingly more skilled black intermediaries into the fold.



Business Development

Change is required to harness the small business market

Gerald van Wyk,
Head: Business
Development

Challenging the insurance industry to evolve is a core component of our work in Business Development. This includes driving the development of customised insurance solutions to serve different, more complicated markets, such as the growing small business segment.

Overall, small businesses tend to be some of the most risk-exposed clients on an insurer's books. They face nearly all the same risks as large commercial businesses, but have significantly less capacity to absorb losses. Changing economic conditions, along with emerging risks, also have a tendency to impact small businesses the hardest.

The three key risks that pose the most significant threat to the vast majority of small businesses across all sectors are physical loss or damage to critical assets, business interruption, and emerging cyber risks.

Even with insurance in place, any claim for loss of physical assets has the potential to debilitate a small business and leave lasting damage to the operation. For example, in the case of a last-mile delivery service consisting of only one or two trucks, the immediate impact of a loss event can bring the business to a halt. While the vehicles can be replaced within a relatively short period of time, the damage caused to the business in the interim may be far more severe in terms of lost income and market opportunities, as well as damage to their reputation for reliability.

The business interruption that follows a loss event often has an even more enduring impact. Not being able to procure or transact for prolonged periods remains a critical risk for small businesses. Business interruption cover has limited efficacy in helping an operation rebuild its client base and re-establish supplier networks. The critical role that risk management plays in the small business market, cannot be emphasised enough.

The Santam Insurance Barometer survey shows that 38% of commercial businesses interviewed had claimed for loss or damage of physical assets in the last 12 months. The mean value of claims for small businesses within this sample was in the range of R185 000.

91%

of all cyber attacks are initiated via email in South Africa.

There are also global emerging risks to be considered. Only **36%** of commercial respondents (compared to **85%** of consumers) consider cyber crime one of the top four business risks in South Africa. However, this growing threat has the potential to ruin a business, particularly a small one.

The asset base of many businesses is becoming more digitalised (client information, research and development and financial records), and an increasing number of businesses now transact and exist almost completely in the cloud. As a result, intangible losses such as data corruption or theft can cause just as much damage, if not more than that of physical assets.

The rise of cyber crime has also exponentially increased third-party liability risks for small businesses. The introduction of legislation such as the Protection of Personal Information Act (PoPI), and its European equivalent, General Data Protection Regulation (GDPR), means that all commercial businesses are exposed to massive fines, third-party liability claims and legal action.

Key risks to small businesses: loss or damage to critical assets, business interruption and emerging cyber risks.

A general lack of awareness is probably the biggest reason why so many local businesses are vulnerable to cyber crime. In South Africa, **91%** of all cyber attacks are initiated via email – which would be more easily preventable with better cyber risk education among employees.

From the above examples, it follows that insurance alone cannot adequately mitigate the threats that small businesses face. Better risk management should therefore be viewed as a key component of the business. Along with this, communication needs to form a greater part of our relationship with the client if we, the insurers, want to remain relevant as business and economic enablers in an increasingly tough environment.

We firmly believe that there is no substitute for the value that intermediaries provide to clients. It is still the best way to get client buy-in on value-adds that elevate policies to provide more than insurance. Furthermore, intermediaries have the ability to act as risk management partners, or coaches if you will, alongside insurers.

The evidence of this is visible in the survey, which shows that intermediaries are still the primary drivers behind insurance product selection for commercial businesses. When asked to evaluate the most important factors that determine how businesses choose their insurance cover, the intermediary's recommendation scored a 9.5 out of 10 – second only to the product meeting the needs of the business (9.6).

This means that, with the exception of being absolutely sure that a particular product is an exact match for the requirements of the business, the vast majority of commercial businesses value the advice of their intermediary above the cheapest price (8.2), the exclusions listed in the fine print (8.4) or their own perceptions of value for money (9.0). Intermediaries are therefore still in the best position to positively influence this market.

However, communicating with the market and providing improved risk management information and assistance is becoming more challenging. The intermediary channel, which has historically provided the insurance industry with the best means of interacting with businesses, is becoming a smaller piece of this market. In many respects, they are the insurer's crucial link to clients. Intermediaries have knowledge of the unique risks that each of their clients face, and are privy to client perceptions that shape their decisions when it comes to choosing cover as well as their attitude towards proactive risk management.

The survey findings show that **62%** of small businesses prefer to purchase insurance via direct channels. Some of the most common reasons given by small and medium-sized business respondents were that it was adequate for their simple insurance requirements (**63%**), cheaper (**51%**) and quicker to access via online portals or over the phone (**49%**).

This challenge that our industry faces points to how we, as insurers and intermediaries, need to evolve to meet the expectations of this market. The rising prevalence of direct insurance has a lot to do with the speed and convenience of access to these perceived simpler solutions.

Given the heightened vulnerability of small businesses, it is problematic that the market penetration of insurance in this segment is estimated to be in the region of just **30%**. Building partnerships with organisations which have a strong connection with small business owners is vital to increase the presence of insurance in this market. This is a big part of what we do in Business Development.

The informal sector presents many opportunities for insurance solutions that could help drive these micro-businesses forward. However, this sector has several unique risks, and adequate solutions based on the specific needs of this market have yet to be designed. This is a challenge that excites us, as we are currently exploring options for providing risk capacity to this important sector of our economy.

Intangible losses such as data corruption or theft can cause just as much damage, if not more than that of physical assets.

How businesses choose their insurance cover

9.6/10

product meeting the needs of the business

9.5/10

intermediary recommendation

It is perhaps our greatest challenge as an intermediated business, to explore ways to better utilise technologies that enhance the intermediary's (and our own) ability to engage with clients as easily as direct channels, while still providing the level of personalised service expected.

For the intermediary, embracing technology is key – and it will only continue to increase in importance over the years to come. Not only should they be exploring better ways to reach their client base through social media and online client portals, but they should also introduce clients to better risk management models that utilise technology to a greater degree. Interconnected technology such as internet-enabled geyser monitors and driver telematics can prove just as effective at minimising catastrophic loss in small businesses, as they have been in other insurance lines.

We see from the survey results that there is an increasing demand for further streamlining our user experience model. One can argue that if intermediaries could improve how they interact with clients, they would be able to match (and in some instances, outperform) the direct market.

It is also important that we find better ways of monetising the value-add that we provide for small businesses. While simpler products may be well-priced, value-adds in the form of advice, technology, and services that mitigate risk, are inherently more valuable to the client if they minimise the impact of potential business interruption.

With all this in mind, it is our responsibility as insurers to lay the foundation that makes it easier for intermediaries to compete with the direct market. The small business market arguably stands to gain the most from using the expertise of an intermediary, yet, as the statistics show; there is still substantial room for growth.

Personal Lines

Building a value-add culture among consumers

Attie Blaauw,
Head: Personal Lines Underwriting

Consumers surveyed for the Santam Insurance Barometer Report ranked the challenging economy, political unrest, social change, cybercrime and climate change among some of the biggest risks South Africans face over the next two years. Delving deeper into these concerns, the respondents go on to clarify that the increased cost of living resulting from the economic downturn, is further exacerbated by negative social trends such as growing crime levels.

The significant losses during the 2012 and 2013 hail season, and recent flooding in KwaZulu-Natal and Gauteng, further indicate an increase in frequency and severity of climate-related events. The truth is that premium rates will increase further if these trends are not addressed. This could be particularly problematic, since lack of affordability was cited as one of the key reasons that increasingly more consumers are underinsured. The survey also notes that around **38%** of consumers have uninsured risks and if rates continue to harden, this statistic is likely to rise.

The trends that are shaping motor and home insurance today are evident in the claim statistics experienced by Santam.

Claims for motor vehicle accidents (**58%** of survey respondents list as their highest risk) have reduced at Santam over the past few years. It is interesting to note that there is a positive correlation between rainfall and the frequency of motor accidents, which is best demonstrated by the recent drought in the Western Cape, which caused the frequency of motor vehicle accidents to decrease in that region.

It could be speculated that the economic downturn has contributed in some way to driving down the accident rate – a trend that is most clearly visible over shorter periods such as school holidays when the drop in traffic density results in less accidents. This is because higher fuel prices and subdued economic performance generally tend to reduce the amount of non-essential driving that people do. With that said, vehicle accidents are still the single largest source for claims on our motor portfolio, making up more than **70%** of the total spend. Glass, which also makes up a fairly large portion of the number of vehicle claims, has been relatively stable over recent years.

Around 38% of consumers have uninsured risks.

Crime is an interesting risk to analyse in terms of personal lines insurance. Risk mitigation against crime-related losses has evolved significantly, and is largely technology-driven. While theft features high in the rankings of consumer concerns – it is a perception understandably shaped by the violence and anxiety that is associated with these events. Yet, very few incidents of theft and hijacking occur in motor lines – in relation to vehicle accidents. Santam's claims spend on this type of incident is relatively low. We spent as much as **30%** of total paid claims on these incidents in the mid-90s, whereas theft and hijacking now account for less than **10%** of all motor vehicle claims per year.

Theft and hijackings are continuously decreasing due to vehicle tracking and security technology – features that are now built into most new vehicles to mitigate against these risks. This is a prime example of how technology

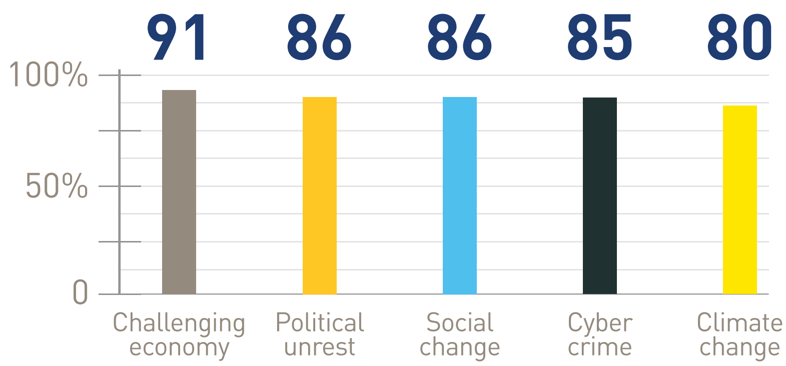
is lessening the need for certain types of cover.

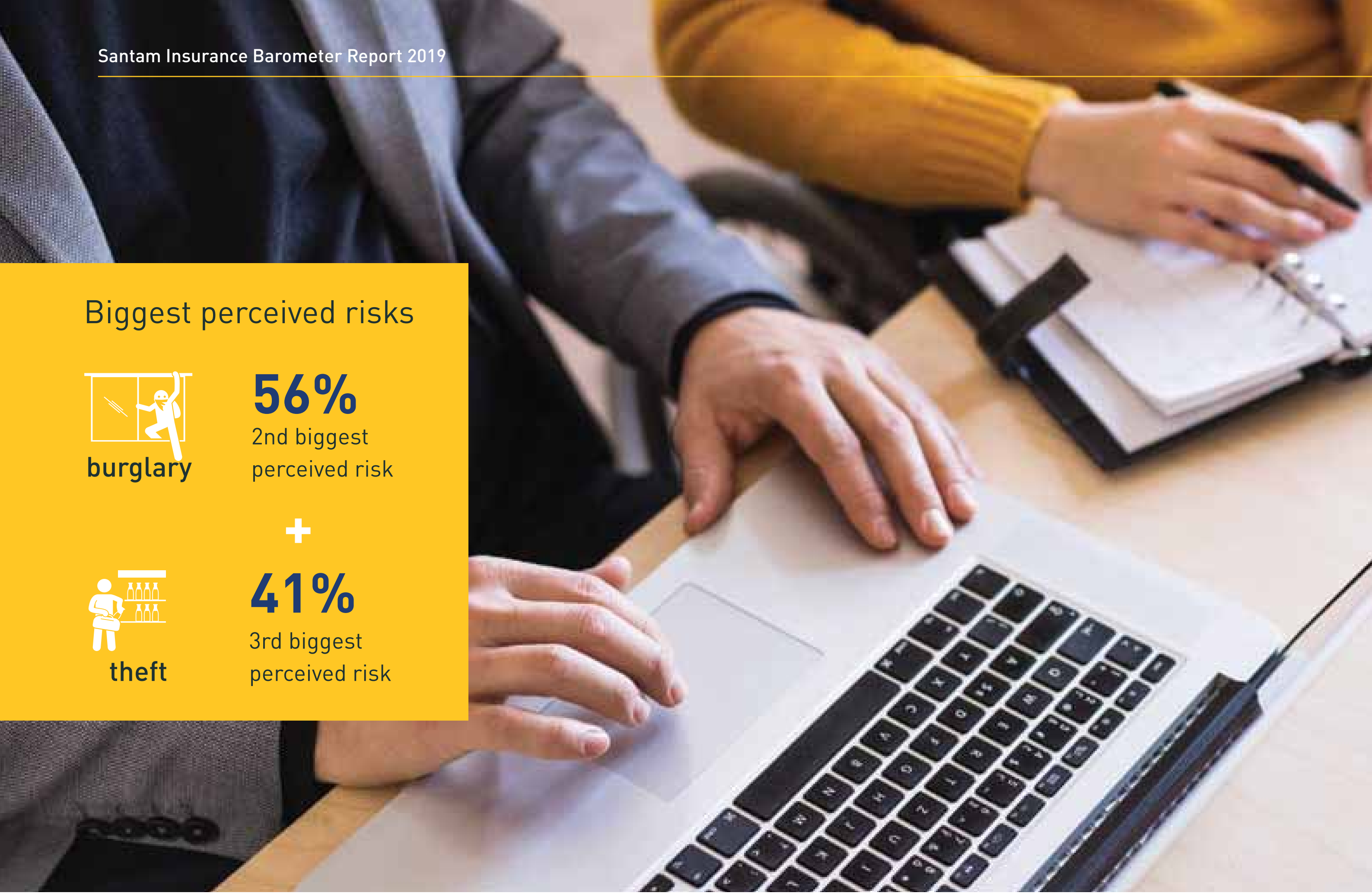
With all of that said, motor insurance premiums are still on the rise, albeit at a slower rate. While the frequency of vehicle accidents may have declined, the severity of claims is steadily increasing. This is due to the inflationary increase in the price of car parts, labour and paint, which are strongly influenced by a weakening South African exchange rate.

Further efforts to drive down risks through better technology which benefits the industry greatly are facing challenges. Telematics devices that do real-time tracking of people's driving habits are a prime example of this.

Driver behaviour tracking has proven to be effective at reducing the likelihood of driver error if used in conjunction with positive reinforcement, such as a premium reduction for good driving behaviour.

The biggest risks South Africans face over the next two years





Biggest perceived risks

burglary — **56%** 2nd biggest perceived risk

+

theft — **41%** 3rd biggest perceived risk

We have seen limited scope for telematics in personal lines, with many clients still expressing concerns over privacy. We believe that there is a lot that should be done to improve client perceptions in this regard.

Only an estimated **30%** of motor vehicles in South Africa are insured, including third-party liability. This is making the landscape progressively more difficult for insurers, who are often unable to recover any costs after paying out a claim.

In the absence of compulsory third-party insurance for all South African drivers, the only realistic solution is for insurers to increase the level of client awareness and to grow their client base among the middle class.

Electronics drive up claims on home policies

On the home front, burglary and theft are the second and third biggest perceived risks, with consumers showing a high level of awareness of these perils.

Admittedly, crime makes up the largest portion of claims for home contents. Burglary accounts for more than a third of the total number of claims for home contents insurance, and together with theft, **50%** of our total claims spend on the portfolio is crime related. Fortunately, both of these factors have seen a marked decline over the last decade, with claims flattening out somewhat since 2016.

A possible explanation for this may be an increased awareness among clients regarding home security, as well as the safety requirements imposed by insurers for which clients are incentivised through reduced premiums. These measures are particularly stringent in geographical areas where crime risks are known to be higher.

On the all-risks side, which relates to insured items taken outside of the home, there has been about a **5%** decline over the past six years, and no real increase in crime-related claims.

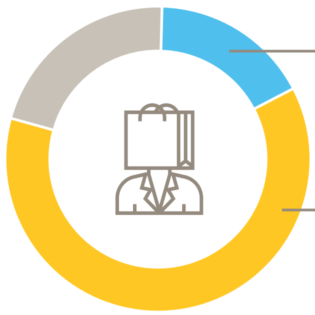
Lastly, we have not yet seen the effects of rising cyber crime filter through into the local personal lines insurance market. However, it is worth pointing out that the potential effects of this type of crime can become incalculable if South African consumers and businesses, as well as the insurance industry, do not adopt the same level of awareness and risk management that they have towards more 'conventional' types of crime.

Emerging risks associated with the advancement of technology probably have the biggest impact on the home contents category. Damage to electronic goods is progressively becoming a larger proportion of our claims spend in this market.

Home appliances such as dishwashers, dryers and refrigerators are becoming more advanced and expensive to replace, and claims are generally related to accidental damage, power surge or

Only an estimated 30% of motor vehicles in South Africa are insured, including against third-party damage.

Preferred channels



17%
of consumers make use of an intermediary

62%
of consumers have policies with direct insurers

Top ranking benefits of using an intermediary

71%
knowledge and expertise

54%
benefit from intermediaries explaining products

60%
intermediaries understand their needs

> **It is vital that risk management becomes an even greater part of consumers' lives.**

lightning strikes. The frequency and value of these claims have increased to the extent that power surge cover has now become a standard component of home contents cover.

The number of claims resulting from geyser damage has also risen by nearly **20%** to almost **50%** of total home building claims in recent years across all geographical sectors. As for the reason why more geysers are failing and/or bursting, it has been speculated that the overall build quality of geysers has declined over recent years, resulting in units with shorter life cycles.

As we become more technology driven, expensive electronics become increasingly integral to our way of life. Concepts such as Smart Homes have become a reality and the value of these claims continues to rise exponentially. This will inevitably lead to a hardening of premiums and ultimately impact the client. The only way forward is to leverage this technology, become more proactive in our risk management efforts, and for it to form part of the overall insurance solution.

One of the most valuable solutions to mitigate the growth of consequential loss is using connected devices as early warning systems. Adding leak detectors to home geysers as a value-added feature on home insurance policies has proven effective in avoiding major asset damage resulting from burst geysers. Lastly, home security can benefit from value-added features such as gate sensors and security call centre services to alert homeowners of suspicious activity while they are away.

Even with improvements in the risk landscape for both motor and home insurance, it is not enough to counter the effect of the increase in claims severity in both of these categories.

It is vital that risk management becomes an even greater part of consumers' lives. Ongoing communication from insurers that highlights the importance of risk management is crucial.

While intermediaries are arguably the optimal channel for educating clients, their stake in the personal lines market is shrinking. Just **17%** of consumers we surveyed make use of an intermediary when purchasing personal lines insurance and around **62%** of consumers have policies with direct insurers.

Having said that, consumers that have used an intermediary recognise the value that they add. Knowledge and expertise were the top ranking benefits of using a intermediary at **71%**, a further **60%** of consumers said that intermediaries understand their needs and **54%** said that they benefit from intermediaries explaining products to them.

The low percentage of those surveyed that use an intermediary reveals a massive risk of underinsurance for many consumers due to a lack of information. It is also a clear sign that we, as insurers, will have to work at finding new ways of effectively communicating and sending a clear message that we need to become partners in risk management to jointly mitigate against emerging risks.

Commercial Lines

Education on emerging risks is necessary

Philippa Wild,
Head: Commercial
Underwriting

We believe that the current risk landscape is quite accurately reflected in the level of business confidence recorded in the Santam Insurance Barometer survey. While corporate businesses indicated an overall confidence level of **76%**, that number drops quite dramatically in the smaller business categories. Large commercial businesses recorded a confidence rating of **52%** and mid-sized companies and small commercial businesses were less confident (at **46%** and **45%** respectively). The lower confidence levels among smaller businesses is probably based on their ability to absorb the consequences of a subdued economy.

Businesses in the construction and retail sectors emerged as the most pessimistic about their prospects. A sectoral breakdown of the survey results shows that companies in these market segments were notably less confident than those in transport and community/personal services.

A glance at the business pages of late seems to back up these statistics, with reports that the construction and retail sectors have been disproportionality affected by setbacks ranging from poor business performance and crime, to liability suits and massive asset losses.

Proper insurance and risk management in businesses become even more important in a tough economic climate, and the role of intermediaries in getting this right is even more significant.

Upon examining the business sector's insurance preferences, the survey revealed that **24%** of large commercial businesses and **38%** of mid-sized companies access insurance via direct channels. While intermediaries still dominate this market, there is a notable increase in businesses that prefer to source their own insurance.

Based on our own experience, we believe that the current economic landscape may play a part in this trend. Harsher economic conditions tend to motivate businesses to cut back on insurance spend, and there seems to be a prevailing perception that acquiring insurance via direct channels is cheaper than acquiring it through an intermediary. This is evidenced in the survey, which shows that **33%** of large commercial businesses and **51%** of mid-sized companies that prefer direct channels, believe that it offers better value for money.

The perception of the organisations' risks also forms a significant part of

24% of large commercial businesses and 38% of mid-sized companies currently access insurance via direct channels.

Business confidence rating recorded by participants

52% large commercial businesses

76% large corporates

46% mid-sized companies

45% small commercial businesses

the decision-making process. Around **82%** of businesses that work with an intermediary list their expertise and knowledge as the most important reason for their preference. It is interesting to note that **47%** of the large businesses that prefer direct insurance channels make use of internal risk advisors to inform their decisions. Lastly, **63%** of mid-sized companies believe that their needs are simple enough to be adequately addressed by standard insurance solutions.

While there is space for direct and intermediated channels to co-exist in the commercial lines market, it is important to consider how the perceptions of these commercial businesses are formed. There is an abundance of information in the market regarding certain risks, but one must account for how this data is interpreted.

A good case in point is the claims data available in the insurance community. Arguably, these numbers can provide some insight into the risk landscape, but it does not paint the full picture. One such example is highlighted in the survey, which shows that **62%** of commercial businesses rank theft as the most prevalent risk to their organisations.

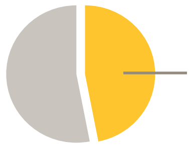
Harsher economic conditions tend to motivate businesses to cut back on insurance spend, and there seems to be a prevailing perception that acquiring insurance via direct channels is cheaper than acquiring it through an intermediary.

However, if one looks at the **38%** of commercial respondents who filed an insurance claim over the past 12 months, theft is not the most frequent claim category. Around **59%** claimed for motor vehicle damage, and theft was the second highest at **37%**. Following this, the claims in order of frequency were accidental damage (**19%**), goods in transit (**19%**), electronic equipment (**14%**), machinery breakdown (**13%**) fire/explosion (**13%**), office contents (**13%**), and cell phones (**11%**).

Theft shows up even less in our own claims data, constituting a notably smaller percentage of total paid claims per year. By no means does this mismatch disprove the survey. The findings are correct, and theft belongs at the top of the perils list. However, it is not the biggest claims category because theft also happens to be one of the best managed risks in the commercial space.

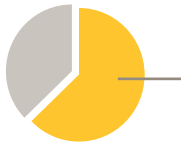
Around 82% of businesses that work with an intermediary list their expertise and knowledge as the most important reason for their preference.

Direct insurance channels



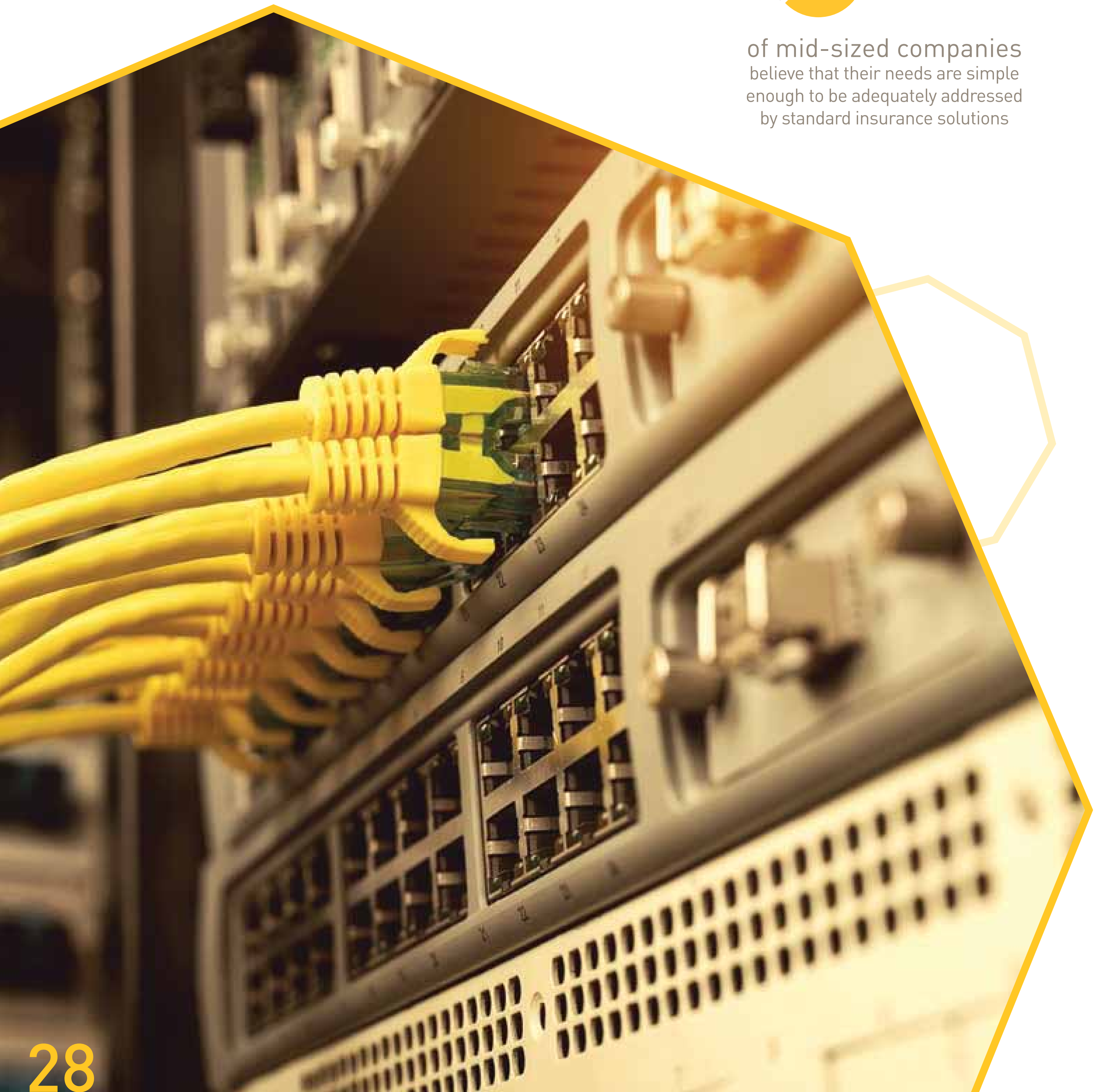
47%

of large businesses make use of internal risk advisors to inform their decisions



63%

of mid-sized companies believe that their needs are simple enough to be adequately addressed by standard insurance solutions



Security staff, CCTV cameras and alarm systems are standard for commercial businesses because this market is aware that crime is a major issue across all market sectors.

In other risk categories where insurers' claims spend witnessed a general upsurge over the years (such as motor vehicle), we must also interrogate whether it is as a result of the rising cost of replacing assets, or whether claims frequency has increased before the severity of the associated risk becomes clear.

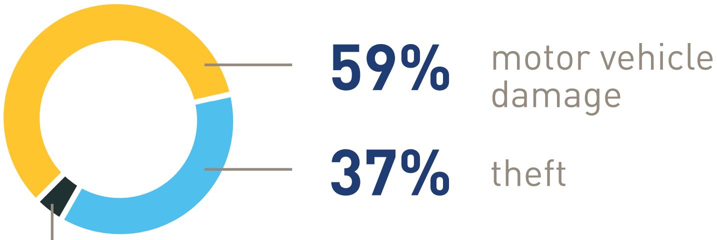
The lack of reliable information is incredibly influential in shaping risk perceptions, and is placing business decision-makers at a large disadvantage. The biggest of these threats is cyber crime, which is exposing organisations to growing liability risks, business interruption and physical asset damage.

There is some level of awareness, as the survey also shows in various places, but the slow uptake of products such as cyber liability cover proves that this is not yet considered an imminent threat by many organisations. This is hardly surprising since cyber attacks are currently underreported in South Africa.

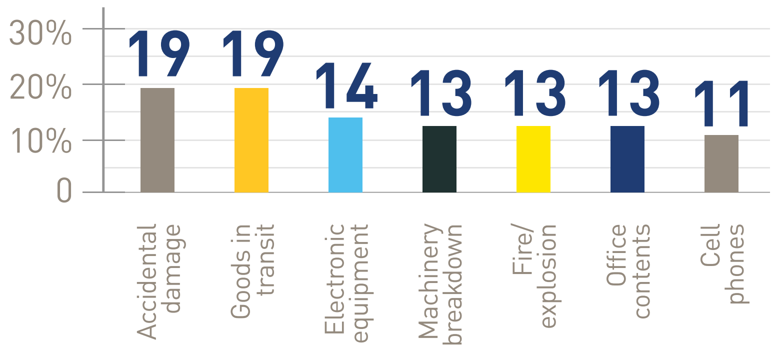
PoPI compels all businesses to disclose any instances of data theft or other cyber crimes where clients' personal information is involved. However, this is not yet being enforced, so it is not unreasonable to assume that there are many companies that have not reported actual incidents – thus perpetuating the perception that cyber risks are not a significant concern in South Africa.

We know that cyber risks have the potential to put a company out of business. The cost of third-party liability and fines that could follow a major data breach could run into millions of rands, and loss or damage to digital assets (which is makes up a valuable part of most businesses) are not covered by existing insurance solutions.

38% of commercial respondents filed an insurance claim over the last 12 months for:



Rest of claims in order of frequency:



It is therefore clear that for insurers to remain relevant beyond this evolution, we must place greater emphasis on educating our clients about the changing risk landscape and the potential impact of the threats to which they are exposed. In a market where clients are selective about the risks that they are willing to insure, we should be using our expertise to provide the market with accurate interpretations of the available risk data. This includes education on the right risk management tools and practices for their specific businesses.

While the survey also shows that the majority of intermediary-served businesses value the expertise provided by their intermediary, there is always room for improvement. There is value in helping clients understand the importance of ensuring their risk remains insurable. We find that especially in challenging economic conditions, there is a tendency for clients to underspend on maintenance and inflate claims, which is something that we have become much more adept at detecting. Unfortunately, this does mar the trust between insurer and client. This is, however, also where the intermediary has the ability to ensure that their clients remain insurable.

Tough times often force focus and drive innovation – and significant opportunities remain for intermediaries who are able to improve their service to their clients and evolve to keep up with their demands. Understanding their needs and utilising technology to better engage with them are enablers of success.

As a market segment, commercial lines is evolving to one where clients are demanding more flexibility in the way that they interact with insurers and intermediaries. We now need to respond by ensuring that greater flexibility does not come at the expense of true value.

Cyber crime is not yet considered an imminent threat by many organisations. This is hardly surprising since cyber-attacks are massively underreported in South Africa.

Specialist Business and Agriculture

Committing to future sustainability

Quinten Matthew,
Executive Head: Specialist Business

A key theme that manifested strongly throughout the Santam Insurance Barometer survey was the impact that low economic growth, combined with political and regulatory uncertainty, have had on the private sector. Over **65%** of commercial respondents agreed that a challenging economy is a key factor in reducing profitability, diminishing demand for their core products and services, increasing operating costs and business interruption.

In the specialist insurance environment, we have seen first-hand how these factors are driving up the perils and cost of risk mitigation for commercial businesses.

Firstly, city planning is an important factor in risk management and becomes more complex when one takes into account urban growth and the resulting deforestation. There are instances where poor planning and poor maintenance have negatively impacted businesses and communities.

The simplest illustration of this can be seen in the St Francis area, which frequently experiences wild fires and persistent flooding that impacts residential and commercial areas, which in part can be managed by better infrastructure maintenance.

Further exacerbating the issue is a severe backlog in the maintenance and repair of public-owned infrastructure, which requires more attention from a governmental standpoint. Deteriorating roads, port and rail infrastructure have severely impacted the risk profiles of businesses that rely on logistics services. Climate change is a notable emerging risk for the specialist insurance category. Rising sea levels are affecting the design of new harbours and harbour extensions, and is negatively impacting property values in areas such as Camps Bay due to ground erosion on sea-front real estate. It is increasingly becoming the responsibility of insurers to engage with the public sector to find solutions to these complex risks.

There is a clear correlation between the growing political unrest and general social dissatisfaction among citizens and the abnormally high rate of fire losses in South Africa. Reports of assets such as trucks being burned during protests and riots increase every year. The line between damage resulting from protests, and outright criminal activity is also becoming blurred. This has been particularly problematic in the marine and heavy haulage industries, where escalating instances of malicious damage coupled with public disorder have been responsible for a substantial rise in business interruption and physical asset loss.

This means that the chance of the South African Special Risk Insurance Association (Sasria) repudiating certain claims for damage following a politically motivated protest, is also increasing. The bottom line is that we as an industry need to ensure that the blurring of risk between Sasria and conventional insurance must not disadvantage the client. This is vital to ensure that the reputation of the industry is maintained at the highest level.

A struggling economy and the international community's perception of South Africa's basis risk are both contributing to the increasing cost of insurance. Uptake of travel insurance for South Africans travelling abroad has seen a deterioration; this is largely due to the weakening currency and increasing medical costs. Equally, the cost of reinsurance to insure certain marine, liability and property classes is increasing due to either lower risk appetites or a move to more sustainable insurance practices.

Agriculture insurance under strain

In terms of industry risk, the agricultural sector stands out, since it has experienced the most substantial proliferation in exposure across the board. Given the vital role that agriculture plays in the economy as a significant source of job creation, large losses in this sector have far-reaching effects.

Deteriorating roads, port and rail infrastructure have severely impacted the risk profiles of businesses that rely on logistics services.

Farming operations have recorded some of their highest losses in recent years as a direct result of climate change. Drought losses have been most pronounced in the western parts of South Africa, while hail, flooding and prolonged cold and hotter periods are affecting agricultural operations in various other regions with increasing severity each year.

Non-irrigated crops are the most vulnerable to failure because of climate change. The documented increase in average temperatures is affecting optimal planting dates for many types of crops, often forcing farmers to plant later in the year. This delay often results in reduced yields.

Additionally, the severity of weather-related claims also appears to be increasing. In recent years, most of the claims we received originated from hail damage to insured crops.

R255 000

average size of crop claims paid by Santam

for hail damage in the 2018/19 production season

Political risk in the form of ongoing uncertainty regarding land redistribution is severely impacting investment and farmers' ability to obtain funding for expansion.

Even with insurance to fall back on, inclement weather severely hampers the farmers' ability to earn an income, and on a macro level puts strain on food production throughout the country, as well as export to international markets.

To remain commercially viable, many farming operations have evolved into big, technology-driven businesses, exposing them to virtually all of the same risks as most other enterprises. For example, premiums for physical asset cover have risen as machinery and equipment have increased in technological complexity (and subsequently in replacement and repair cost).

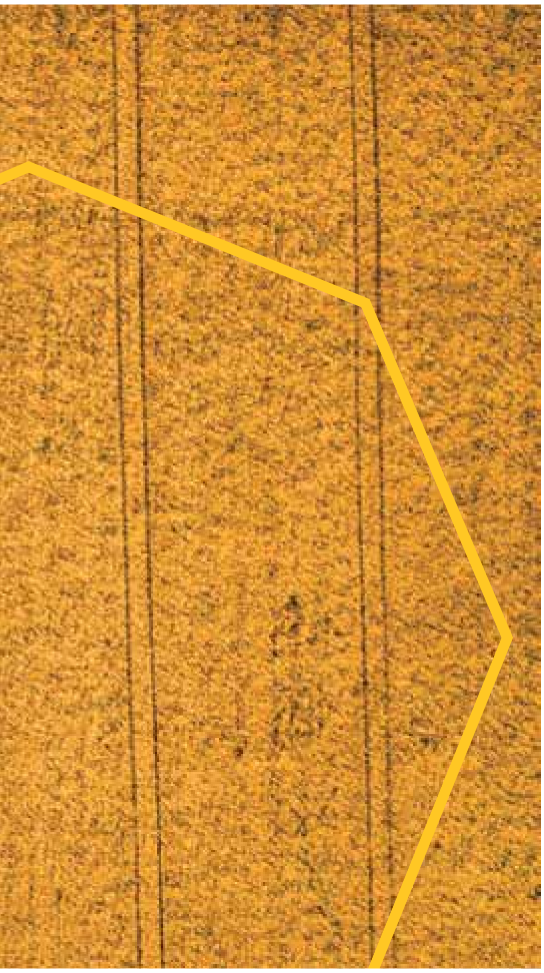
Further to this, fluctuating exchange rates, poor economic growth and political uncertainty have affected the risk profile of agricultural operations. Political risk in the form of ongoing uncertainty regarding land redistribution is severely impacting investment and farmers' ability to obtain funding for expansion.

In light of the above risk factors, farmers have been forced to adapt in various ways to ensure their sustainability. Some have switched from crops to cattle, or even converted to game farms (which can offer multiple revenue streams).

Others have diversified their crops, increased their crop rotation, or started using seed cultivars that are more resilient against drought or other extreme weather conditions. In addition, many commercial farmers are spreading their geographic risks by renting or buying land in different regions. This option presents more logistical challenges, as well as the aforementioned issues around land reform, but it is an effective means of removing the risk of all crops being lost to a single weather event.

The insurance industry has been forced to adapt and evolve, and as a result has become more scientific in the way that it underwrites agricultural risks. We now evaluate risk exposures over smaller areas and risk assessments are therefore more precise. With the use of global positioning technology, Santam is able to price individual crop insurance risks more accurately based on the exact geolocation of the risk.

However, even with improved risk pricing, it is fast becoming unsustainable for insurers to offer insurance against crop failure resulting from climate factors, if those crops are grown in areas where the climate is no longer suitable. In instances where our clients still need to insure crops in riskier regions, we now work towards more bespoke solutions



Premiums for physical asset cover have hardened as machinery and equipment have increased in technological complexity (and subsequently in replacement and repair cost).

that see the farmer carrying a bigger portion of the risk.

In other instances, we may find that more of the risk can be transferred to the insurer. More than ever before, ensuring that farmers have the right level of cover has become a matter of collaborating with the farmers and finding a balance that benefits both them and the insurer.

South African crop insurers are under pressure to provide affordable and sustainable insurance solutions to small semi-commercial and subsistence farmers, which necessitates a business model consisting of a partnership between the private and public sector. The best suited insurance product for emerging farmers will be index insurance, which uses satellite images and data to assess risk and losses.

Future-fit mindset required

In light of the above, the reality is that not all risk can be transferred to an insurer anymore. There has to be a greater emphasis on risk management, on the part of the insurer and the business sector.

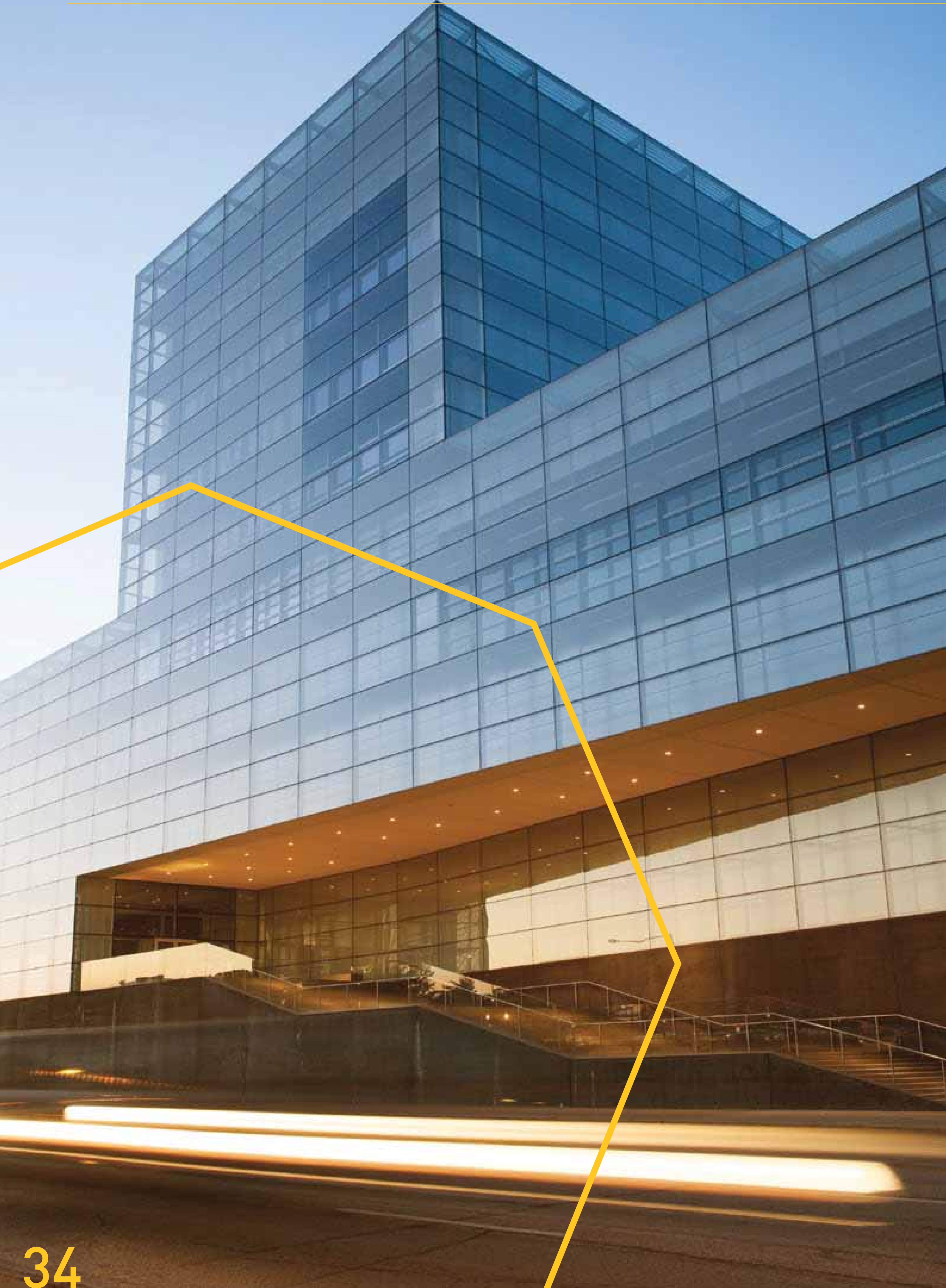
There are future-focused businesses that, in times of heightened risk, take on more of their own risk burden through smart risk management measures (including employee training and education), and as a result, are performing well in the current economy. We have noted that strong companies with good leadership that invest in technology and prioritise risk management benefit from continued growth. Companies that are not performing well do not invest in technology and manage their risks appropriately, often reducing their insurance spend, and tend to remain trapped in a low-growth cycle.

There is a clear need for a culture of risk management on a far greater scale if the corporate and commercial sector is to flourish. However, changing behaviour takes time, and we (intermediaries, clients and insurers) need to continue to build and share our understanding of the risk landscape. Just as clients must adapt to manage their risks better, insurers must work towards developing relevant and sustainable solutions for all.

One of the more positive things to note is the fact that the value of the specialist intermediary has heightened in the current increased-risk landscape and, despite increased premiums, more clients want to engage with intermediaries. This bodes well for the tripartite relationship dynamic between insurers, intermediaries and the commercial sector, and should ultimately filter through and go some way towards improving the economy.

However, for this to happen, all organisations have to be future-fit. By this we mean thinking and employing skills for the future. For instance, insurers would employ more data scientists to improve our processes. For intermediaries, this could mean employing more engineers to help and support clients and give appropriate advice.

Just like the business entities we insure, insurers must continue to adapt and evolve to invest in an industry for the future. Working together is key, and if this mindset continues to gain momentum in the commercial sector, there is every chance that the market and economy will become more robust.



Niche Business

The importance of insurance during tough economic times

Vuyo Rankoe,
Head: Niche Business

There have been important shifts in South Africa's insurance landscape that will affect commercial businesses in the years to come. For the specialist insurance sector, in particular, these shifts are increasing premiums for businesses operating across multiple sectors.

One of the most prominent reasons for the impact on premiums is linked to global climate change risk, which has had a greater indirect impact on the local insurance market when compared to factors such as socio-political insecurity, or other recent emerging risks such as cyber crime.

Interestingly, **30%** of the commercial businesses interviewed ranked climate change as the fifth biggest threat to South Africa. In 2017, the local insurance sector was impacted significantly during the rampant Knysna wildfires and floods in Durban. Aside from these events, the other climate change-related losses have been relatively small in comparison.

Most catastrophic losses attributed to climate change have occurred in various parts of the world, with reinsurers effectively bearing the biggest losses. As a direct result, Lloyds of London was forced to re-assess its own risk exposure in 2017. This resulted in Lloyds withdrawing much of its support from several key international markets, including South Africa – with other reinsurers recently following suit.

Reinsurers have historically taken on the bulk of local insurers' risk exposure. This trend has increased competition and resulted in an extended cycle of softening rates. This cycle allowed many insurers to stay in the game and cut premiums for much longer than should reasonably have been possible.

However, with reinsurers reducing their capacity in the South African market, local insurers have had to take on more risk, re-evaluate their exposures, and adjust their pricing models accordingly. It has only been a short time since this cycle of higher rates began, but its effects are being felt in the local market.

Adding to this, regulatory changes in the financial services industry have driven up the cost of insurance products over the past seven years.

It should be said, however, that the stricter regulations have changed industry for the better as far as clients are concerned. The implementation of measures such as continuous professional development (CPD) has helped promote better skills and raise standards within the financial services industry. However, insurers' and intermediaries' administrative costs have increased, resulting in additional costs being passed on to clients.

The cycle can also be seen as a positive for local insurers, resulting in increased market resilience through boosting the insurance pool – particularly in light of the economic challenges faced by the country which makes premium challenging.

However, it poses some potential problems for the commercial and specialist market. Time and again we see that businesses cut their insurance spend when faced with increased premiums and the economy underperforms, leaving them underinsured. However, the risk landscape is also becoming more hostile for organisations, which is why business decision-makers have to make informed decisions before defaulting, or cutting down, on comprehensive insurance cover.

30% of the commercial businesses interviewed ranked climate change as the fifth biggest threat to South Africa.

With reinsurers now reducing their capacity in the South African market, local insurers have had to take on more risk, re-evaluate their exposures, and adjust their pricing models accordingly.

The challenging risk landscape

Most commercial businesses surveyed listed theft (**62%**), motor vehicle accidents (**28%**) and fire (**27%**) as some of their top perceived risks, but existing governmental and infrastructure risks remain largely underestimated.

Utilities and municipal services hold significant risk for property and business owners. Reports suggest there is a high likelihood of large-scale service delivery issues such as load shedding returning more frequently as well as the potential for drought and water cuts – resulting in increased business interruption.

Fire is one of the most potentially destructive perils that commercial properties face. This is due to inadequate municipal water pressure in many parts of the country, which results in the failure of sprinkler systems activating when a blaze breaks out. There have been instances where fire departments have not responded in time, resulting in losses far larger than insurers had initially underwritten.

Aside from this, the pool of skilled professionals is shrinking across all market sectors in South Africa.

Santam's own claims data shows a remarkable increase in the number of liability and professional indemnity (PI) claims where professionals displayed a level of negligence that can only be attributed to inadequate skills or experience.

With market conditions becoming more challenging, it is becoming common for professional firms to supplement their incomes by diversifying into services that are outside of their core skills. This increases the risk of incurring liability.

Our data shows that the potential impact that instances of professional negligence can have on businesses in this sector has grown. Between 2013 and 2018, the average intimated value of PI claims filed by professionals in the built environment has gone up from R5.7 million to R8.5 million – an increase of **49%**.

As far as niche insurance is concerned, a shortage of skills has had a major impact on guarantees and loss of profits. We have seen more projects not meeting deadlines, due to inadequate project management, or an ongoing liability issue.

Fire is one of the most potentially destructive perils that commercial properties face.

Compounding this problem is the lack of follow-through from industry bodies and regulators to ensure that skilled professionals comply with their respective market sector regulations. This lack of enforcement within regulators means that low level of skills within organisations, such as engineering firms, is undetected and unchallenged for much longer than it should, often to the point of peril.

The emerging risks around technology should not be underestimated. Cyber risks are escalating. Yet, the uptake of policies for products such as cyber liability is still low, when compared to more mature markets, which seems to indicate that the local commercial market is not yet taking it seriously enough.

Taking into account that the third-party liability related to cyber crime is enough to cause ruinous loss to any size organisation, we believe there needs to be more education around how to mitigate against this serious, and growing, global risk.

As for technological advancements such as AI and IoT, there has not been any real impact on the specialist insurance category yet. We only expect this to change meaningfully in around 15 to 20 years' time when 'smart' buildings become more prevalent locally.

As the above risk trends indicate, commercial businesses cannot afford to change their risk exposure in the current landscape.

Rising premiums do affect insured businesses, who will more often find themselves having to make a choice between paying salaries or facing the risk of not being adequately covered. In order for insurance to remain affordable for these businesses, their risk management measures must be prioritised.

Intermediaries are critical in this regard. Given their proximity to the client, as well as their access to in-depth risk information from insurers, intermediaries should be the first stop for clients looking to implement better risk management strategies.

Intermediaries should encourage their clients to change the way that they view their insured risks. It is

no longer adequate to simply transfer all aspects of risk to an insurer – it is vital that insured clients eliminate their need to claim as much as possible through improved risk management.

Intermediaries are in a better position to negotiate lower premiums than clients insuring through direct channels, especially when their clients are able to demonstrate an improved capacity to carry more of the risk burden.

Considering that businesses have to start diversifying the ways in which they mitigate their exposures, insurance is an indispensable component to guaranteeing long-term survival. It is crucial for the South African market to start working closely with intermediaries and insurers to allow efficient and cost-effective risk mitigation across all aspects of business.

average intimated value of PI claims filed by professionals in the built environment

49%
increase in claims

R5.7 million 2013 > **R8.5 million** 2018

John Lomberg,
Manager: Stakeholder Relations

Stakeholder Relations

Building resilient societies

We often talk about the importance of providing more than insurance, but we can argue that it is important to become more than insurers. The insurance industry as we know it today is unsustainable, and the old model of only analysing and attempting to control the risks of our clients is rapidly fading into obsolescence.

We have had to change the way we look at our own corporate social responsibility (CSR) efforts. On the surface, it may seem to be about addressing the needs of the most vulnerable members of society, but sustainable CSR initiatives should also directly address our own commercial viability as insurers.

As seen in the Santam Insurance Barometer survey, political risks and social change rank high on the risk radar of commercial businesses and consumers alike. This is not surprising. Social unrest is on the rise, and dissatisfied individuals have taken to the streets on numerous occasions following major catastrophic events that left many underserviced communities without basic infrastructure or adequate housing. This has the potential to cause untold damage to government and privately owned assets.

While the average insured individual or business can recover almost immediately from catastrophic loss events, it takes the uninsured individual up to five years to get back on track. Municipalities throughout South Africa are struggling to repair and replace damaged infrastructure. This places significant strain on continued business growth and profitability in the private sector.

The question for us is – "How should insurers utilise their expertise to build resilience into the entire ecosystem (as opposed to only insured parties), for the benefit of both the insured and the underserviced communities?"

Through Santam's Partnerships for Risk and Resilience (P4RR) programme, we are identifying geographical areas that are considered to be high risk. Today we have the benefit of technology, big data and the analytical capabilities to identify and predict where the

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biggest potential risk exposures lie and why. This allows us to identify certain trends and emerging risks, and informs the proposed interventions that may be required down the line.

Our research has shown that fire is the biggest risk faced by communities in South Africa. It is something that the majority of the survey respondents (**80%** of consumers and **30%** of commercial businesses) highlighted as a growing concern. Our data shows that the two most common reasons for this are drought caused by climate change, and dense clusters of alien vegetation.

Mitigating fire risks forms a significant part of the work that we do through the P4RR programme. Our first course of action when mitigating fire risks in any given area, is to lead efforts to destroy the surrounding alien vegetation. However, this in itself is not enough to effectively manage fire risk sustainably.

Many communities do not know what to do in the event of a fire and many firefighting facilities are severely underfunded, under-equipped and under-resourced. Community education and equipping local fire stations are therefore the next important steps. It enables the municipality to respond appropriately and mitigate damage to its own infrastructure. The risk resilience built into the system benefits all of the stakeholders in the ecosystem.

A very strong case in point, which plainly shows the holistic benefit of building risk resilience in underserviced communities, is St Francis Bay.

The fire that raged through this community in 2012 caused destruction on a monumental scale, destroying just about everything in its path. The loss on Santam's books alone was in the region of R400 million. This catastrophe, however, also presented us with our first opportunity to put our philosophy of long-term resilience into practice. We approached the municipality to gain better insight as to why the losses were so severe.

Building resilient communities and seeing the effects thereof is a long game, but the value of this approach is proven often.

We contracted Aurecon to conduct an investigation to identify the challenges and limitations that the municipality was subjected to. A key issue that we discovered, was that the nearest fire station was located in neighbouring Humansdorp. It was too far away to respond to fires in the St Francis Bay area within the required timeframe. After a lengthy multi-stakeholder discussion, we coordinated and jointly developed a disaster risk management plan that included establishing of a mobile fire station in the area.

This, along with a handful of other interventions, significantly decreased the impact of subsequent fires. There has been a high re-occurrence of fires in St Francis Bay, but the damage left in their wake has been much less severe. The fire of 2018 burnt 11 homes, while the 2019 fire damaged 19 homes. The insurance losses have been significantly lower and we believe that this can be attributed to the fire risk reduction efforts that Santam launched in partnership with the municipality.

Building resilient communities and seeing the effects thereof is a long game, but the value of this approach is proven. This example repeats itself in every region that we are able to successfully foster partnerships for risk resilience with private and public sector role players. With every event, there is a marked reduction in loss of infrastructure and assets, not to mention loss of life.

In other underserviced communities, we found that simple, inexpensive interventions such as installing smoke detectors in every dwelling had the same effect of minimising loss of both property and lives. From an economic standpoint, this also has a positive impact, since the individuals in these communities are able to continue working, earning an income and providing for their families. This means that there is the potential for these individuals to continue contributing to a faster growing middle class.

The devastating Knysna fire of 2017 is another interesting case study. Santam conducted similar investigations and uncovered a number of key points where adequate risk management was lacking. Based on the research, Santam was able to suggest additional measures to the local municipality.

These included managing or controlling the presence of fire-prone vegetation and other combustible or flammable material on tracts of land, especially along wildland-urban interfaces.

It was also important that the fire department started attending to all fire callouts (even those that did not appear threatening), and there had to be a greater focus on public education and awareness programmes regarding the risks associated with wildfires.

The research identified a need for insurers to develop more affordable insurance products for the households that do not qualify for government welfare programmes, but who are also unable to afford insurance (we often refer to this demographic as "the missing middle").

In this scenario, the biggest challenge that insurers face is rallying all stakeholders in the value chain in order to build truly sustainable, self-sufficient municipalities. One of the main impediments in achieving this is that insurers are perceived as the sole problem solver to whom all of the risk can be transferred. This is a notion that must be dispelled if we are to see sustainable economic growth in South Africa.

From our standpoint, the insurance industry's role is to coordinate and act as risk advisor to local municipalities and private businesses. Both these parties need to be convinced to invest their time and capital into repairing infrastructure and managing risk sustainably. This is the only way that the disruptive effect of these types of losses in underserviced communities can be mitigated.

Additionally, we have learned that interacting with stakeholders solely on a municipal level is severely limiting. We have seen our risk management efforts benefiting one municipality, while an adjacent municipality in the same district suffers massive, senseless losses due to a lack of access to the risk prevention measures available in the neighbouring community. The only solution to this is to think bigger and to engage with the decision-makers at national and provincial government level. Building truly holistic partnerships for sustainable risk resilience must start at the very top.

R32 million

invested by Santam into underserviced communities

All stakeholders must fully commit and invest their own resources in order to uplift the country, this can only be done if enacted as a collective effort. Since the inception of our P4RR programme, Santam together with the Emthunzini Trust have invested R32 million into underserviced communities. Santam has committed to double that amount directly from our profits – and we urge our fellow insurers and other stakeholders in this value chain to do the same.

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Conclusion

Pursuing a state of holistic risk management

Andrew Coutts,
Head: Intermediated Distribution

It is clear throughout this report, that not only do traditional risks pose a much greater threat of severe loss in the current risk landscape, but new and emerging risks are already making an impact and forcing us to re-evaluate how our industry must operate into the future.

Climate change is a recurring theme throughout the report, affecting all of the insurance categories one way or another. In the agriculture sector, it has been responsible for a marked increase in large-scale crop losses due to drought, flooding and hail – which are eating away at insurers' risk pools. For the niche insurance lines, it has indirectly influenced the availability and pricing of insurance cover, and in the property sector, we have seen a slow but steady increase in the risks related to fires and soil erosion.

Another pervasive threat is cyber risk, which has the potential to lead to asset loss (digital and physical), and to litigation that can drive commercial businesses and consumers into financial ruin. What is of concern here is that there has not yet been a significant uptake of cyber cover, meaning there remains significant exposure to this growing risk.

What is evident from the survey results is the growing misalignment between the market's perception of its risk exposure and the reality of the risk landscape. This lack of awareness leaves consumers and commercial businesses exposed, ill prepared and underinsured, which is becoming increasingly dangerous.

The insurance industry currently finds itself in a position where it must change, if it is to remain relevant as an economic enabler. The old notion of increasing rates indefinitely in response to growing risks is no longer adequate as a solution, and the only way forward is to change the mindset about risk transference. A culture of risk management is vital and insurers will have to become innovative in the way that they enable and monetise the value-adds that eliminate clients' need to claim.

This is where the intermediary has always played (and continues to play) a crucial role. They are in a unique position on the front lines, acting as a sales, service and advice channel between insurer and client – and are critical to educating clients on risk mitigation.

However, consumer education is becoming more challenging with the continued growth in direct insurance. Almost a quarter of large businesses and more than a third of mid-sized businesses perceived direct channels to be better value for money. Similarly, **62%** of small businesses surveyed prefer to purchase insurance direct as they perceive it to serve their "simple requirements", be cheaper and quicker. In the personal lines market, only **17%** of consumers surveyed make use of an intermediary and **62%** have cover with a direct insurer.

With this in mind, the dynamic between intermediated insurers, intermediaries and clients needs to change to facilitate the free flow of information between all parties and the better positioning of their value propositions. Technology will be important in this endeavour, and we must use it to become more agile in the way that we extend our reach, communicate, how we underwrite risks and in the way that we add value in the form of better risk management.

We have to grow insurance market penetration in order to ensure the long-term viability of the sector. Innovation is necessary to tap into new markets with suitable solutions. Increasing investment in transformation efforts plays a crucial role. Bringing new intermediaries from diverse backgrounds into the insurance sphere helps to grow the economy by elevating professionals and households, and drives greater penetration for insurance products into new and underserviced markets. It spreads the claims risk of insurers more effectively (staving off the need for more aggressive increases) and interacting with these intermediaries builds a better understanding of how to serve these markets.

Our industry is at the point where the axis of evolution is turning faster than ever before and we are left with no choice but to shift from a mindset of risk transference to holistic risk management. Intermediaries, located on the front line, active in the businesses of their clients and trusted to provide advice are uniquely placed to drive this change and to lead the industry into a new era of consumer value. It is time to start the journey.

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