# ZIMRE HOLDINGS LIMITED
## Security Growth and Profitability

# REINSURANCE TRENDS IN EMERGING MARKETS IN THE LIGHT OF GROWING NATURAL CATASTROPHES:

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# INTRODUCTION

- Condolence message , Madam Evangeline C. Escobillo and husband Retired General.

- Tribute to Organizers of Conference and pertinent theme and topics.

- Role played by Insurance as alternative risk transfer mechanism and aiding economic growth and development.

# CURRENT STATE OF GLOBAL, DEVELOPING AND EMERGING MARKET ECONOMIES

- **Global economy to grow by 3,3% in 2015 and rising to 3,8% in 2016.**
- **Emerging Market Economies expected to grow by 4,2% in 2015 and 4,7% in 2016.**
- **Growth prospects are rather weak mainly due to the decline in oil and other commodity prices on the international market, structural bottlenecks, rebalancing in China and economic distress related to geopolitical factors in Ukraine, the Middle East and parts of Africa.**
- **Sub-Saharan African economies expected to grow by 4,4% in 2015 and 5,1% in 2016 driven mainly by increase in agricultural output and investments in infrastructural projects.**
- **Africa's growth prospect in the long term are very bright given the rising population now estimated at around 1 billion.**
- **The rise in household incomes is creating a growing middle class that is expected to drive the increase in the demand for insurance.**
- **Floods, droughts, storms, earthquakes and man-made disasters are ever present and have the negative impact of retarding the economic gains.**
- **Insurance is expected to play a crucial role in cushioning the countries against the effects of the natural catastrophes on economic growth.**
- **Insurance is one of the major driving forces of a modern financial system and African governments are warming up to the growth and proper regulation of the insurance industry.**

# NATURAL CATASTROPHES

- Christians hold  view that the increase in catastrophic events taking place in this generation were predicted  by Jesus Christ  more than 2000 years ago and are an indicator of the coming to end of the Age.  (Matthew 24:7b---) “and there will be famines and pestilences and earthquakes in different places”.
- There has been an increase in Natural disasters in the last few decades that have never been seen before.
- Scientists attribute these to the effects of Global Warming.
- Natural disasters include flood, tropical cyclones, storms ,earthquakes ,drought ,wild fires , severe weather and windstorms.
- Social risks such as the bird flu and Ebola epidemic also pose grave danger to the industry.
- Natural disasters cause human life and livestock losses and damage to the environment, property and infrastructure.
- Natural Catastrophes cause economic and insurance losses.
- The losses are increasing due to the following reasons:
  - Natural and man-made climatic changes
  - Growing populations and economic activity which leads to increase on the value of losses and vulnerability of insured values.
  - Increase in the existence of exposed areas
  - Increased insurance penetration due to rising wealth levels in the population leading to more people buying insurance.
- In light of the rising natural catastrophes, insurers and reinsurers operating in the region must brace themselves to deal with the growing risks and take appropriate measures to provide the necessary cover and to limit the exposures.

# NATURAL DISASTERS AND ECONOMIC IMPACT

- According to Swiss Re, there has been a rising trend in Natural Catastrophe losses since 1970.
- The losses were below $20 billion between 1970 and 1985.
- The losses rose to $60 billion between 1990 and up to the year 2000.
- Insured losses peaked to over $120 billion between 2005 and 2010.
- The costliest earthquake was in 2011 in Japan where 15 000 people were killed and $40 billion in insured losses incurred.
- Hurricane Katrina in the US accounted for over $38 billion in insured losses in 2005. Hurricane Andrew in the US caused insured losses of $21,5 billion.
- The earthquake (7,8 on Richter Scale magnitude) that struck Nepal on 25th April 2015 killed more that 3 800 people an caused between $2 and $5 billion in economic losses .
- Malawi experienced torrential rains in early January 2015 associated with Tropical Chedza which also affected Zambia, Mozambique and Madagascar.
- The economies of Mozambique and Malawi are natural resource depended and agriculture accounts for at least a third of GDP. Consequently, natural disasters have a significant impact on the performance of the economies.

# AREAS MOST PRONE TO NATURAL DISASTERS

| Floods | Cyclones | Earthquakes |
|---|---|---|
| China | Philippines | Philippines |
| Egypt | Madagascar | Egypt |
| Sudan | Mozambique | Tunisia |
| D.R. Congo | | Algeria |
| Kenya | | |
| Mozambique | | |

# INTERNATIONAL REINSURANCE MARKET

- Global Insurance Capital was at about $4,2 trillion (Aon) as at the end of the third quarter 2014.
- Reinsurer's capital grew by 6% to $575 billion driven by healthy retained earnings, below average catastrophe losses and investment gains.
- A soft market is expected to continue for the rest of 2015 because of excess capacity.
- In addition non-traditional capital continues to show growth.
- The insurance linked securities market was estimated to be around $62 billion.
- In light of increasing natural disasters, insurers and international reinsurers have continued to take measures to manage and prevent poor performance of property and other losses affected by Natural Catastrophes.
- There is real need and demand for new covers to absorb risks from cyber liability and other technology related risks.
- Terrorism related risks also ought to be managed well as indications are that the risk is on the increase given the geopolitical tensions, the security alerts and travel warnings issued by governments in advanced countries.
- Global catastrophe losses were estimated at $39 billion in 2014 ($49 billion in 2013).
- The 10 year average for such losses was estimated at $63 billion.
- Stronger economic activity will propel insurance premium growth in most regions of the world.

# NON –LIFE PREMIUM GROWTH RATES

| 2012 | 2013 | 2014 | 2015P | 2016F |
|---|---|---|---|---|
| **World (%) 3,0** | 3,1 | 2,5 | 2,8 | 3,2 |
| **Advanced Markets (%) 1,3** | 1,9 | 1,7 | 1,4 | 1,6 |
| **Emerging Asia (%) 12,5** | 12,2 | 12,5 | 12,5 | 12,9 |
| **Emerging Markets (%) 8,5** | 8,2 | 5,5 | 8,1 | 8,7 |

# LIFE PREMIUM GROWTH RATES

| • . | 2012 | 2013 | 2014 | 2015P | 2016F |
|---|---|---|---|---|---|
| World (%) | 2,6 | -0,5 | 4,8 | 4,3 | 4,2 |
| Advanced Economies (%) | 2,1 | 1,5 | 3,9 | 3,0 | 2,8 |
| Emerging Markets (%) | 5,5 | 4,5 | 9,1 | 10,4 | 10,7 |

# STATE OF DEVELOPING AND EMERGING MARKET INSURANCE AND REINSURANCE MARKET

| • . | Ghana | Angola | Zimbabwe | Zambia | Uganda | Malawi | Mozambique | South Africa | Nigeria |
|---|---|---|---|---|---|---|---|---|---|
| GDP (2013) | $39b | $120b | $11b | $21b | $21b | $4b | $15b | $84b | $510b |
| Insurance Mkt Size (GPW $m) | $200m | $1b | $194m | $195m | $126m | $20m | $130m | $9b | $1,5b |
| Penetration Ratio (%) | 0,6 | 1,0 | 2,1 | 1,6 | 1,0 | 0,56 | 1,0 | 13,0 | 0,5 |
| Minimum Capital for Insurers ($m) | $5,0m | $6,0m | $1,5m | $0,2m | $1,6m | $0,8m | 1,1m | 1,5m | $20m |

## STATE OF DEVELOPING AND EMERGING MARKET INSURANCE AND REINSURANCE MARKETS

- Very low penetration ratios in emerging markets means that insured losses are also minimal in the event of a natural disaster.
- Insurance penetration in emerging markets is still low at 3,6% in 2005 against a global average of 7,5%, despite the vulnerability of the regions to natural disasters.
- The Tsunami that struck South East Asia in December 2004 was minimally insured.
- In addition, insurers are adapting to Catastrophe risks by raising insurance rates.
- This leads to lower loss ratios after the catastrophic events.

# AFRICAN INSURANCE MARKET

- State of African Insurance market differs from one country to the other, and South Africa has the most advanced Insurance industry mainly due to its diversified and advanced economy.
- Out of the total premium of $46,7 billion generated on the continent in 2008, South Africa accounted for about 74% of the total premium.
- The Maghreb Region (Algeria, Tunisia, Libya, Mauritius, Morocco and Egypt) has one of the most advanced insurance industries on the continent mainly due to its close proximity to trade with Europe.
- Tunisia and Algeria operate Government sponsored Social Security Schemes which cover the poor in the event of a catastrophe.
- Mauritius and Seychelles, which are classified as upper middle income countries, have a vibrant insurance and reinsurance industries.
- Under the umbrella of the African Insurance Organization (AIO), Morocco has set the Catastrophe Risks in Casablanca to monitor and map areas and patterns of Catastrophic economies with ways to ameliorate their impact.
- Other African Countries have in recent years been awash with exploration activities for gas, oil and other mineral resources.
- For the African Insurance market, these are new risk exposures.
- Questions are being raised as to whether or not the required capacity will be available to underwrite the mega risks.
- The risks on those mega projects will be high and will ultimately be covered by international reinsurance Companies.
- Global reinsurers still dominate the Emerging market reinsurance market because of excess capacity.

# RESPONSE TO INCREASING NATURAL DISASTERS

- Catastrophic losses caused by natural disasters do not follow predictable patterns and this presents challenges to insurers.
- Insurers in Emerging Markets have to come to a place where they can predict the occurrence of catastrophes in order to assist with planning.
- Reinsurance Companies need to work with meteorological institutions in order to come up with scientific models to predict the catastrophic event.
- Emerging market insurers and reinsurers need to increase the usage of online natural hazard information and mapping systems such as Swiss Re's CATNET.
- Insurers are also grappling with the issue of the pricing of the risks. Wrong pricing may result in the firm suffering losses well in excess of the value of the premiums charges for the coverage.
- Natural disasters are an opportunity for reinsurers and insurers in emerging markets to add value to the insured provided the risks are priced correctly.
- Pricing methods differ from Country to Country. A lot of companies are moving away from flat pricing to risk based pricing.
- Reinsurers and insurers in emerging markets also face the challenge of adverse selection. At times people that are most at risk being catastrophe producers resulting in an adversely selected insurance portfolio.
- Small reinsurance Companies operating in the emerging Markets are the susceptible to shocks arising from catastrophic events and there is need to increase capacity.
- There is need for large and well capitalized reinsurance companies in the emerging markets in order to avoid passing most of the premiums to reinsurances in advanced economies.
- Emerging market economies have huge populations which are ignorant about the existence of insurance as a risk management instrument.

# ROLE OF GOVERNMENTS

- The interventions by governments in dealing with natural disasters differ from Country to Country, but what is clear is that there is still a long way to reduce the impact and suffering from Natural Catastrophes.
- Governments are expected to work with Insurance Companies to mitigate the effects of natural disasters.
- Governments would have developed information data bases for natural catastrophes that will assist insurance companies and non-governmental organizations to understand the risks better.
- In the aftermath of a disaster, governments play a vital role in mobilizing international and domestic aid in order to assist the victims.
- Governments in emerging markets must set up proper frameworks for the operation of insurance and reinsurance Companies.
- Regulators are strengthening capital adequacy requirements and most are gravitating towards risk based regulation .
- Disasters also cause delays in economic development thereby increasing poverty and social and political instability if there are no resources to cushion society against the losses.
- The other emerging trend is strengthening the national insurance capacity through:
  - Introducing compulsory cessions in order to promote the fast growth of local reinsurance companies and to preserve resources such as foreign currency,
  - Impose mandatory participation of domestic insurance companies in catastrophe pools.
  - Implement and enforced strict codes in construction in order to keep claims at manageable levels.
  - Creation of national institutions to cover catastrophic and other risks such as what South Africa and Namibia did - SASRIA and NASRIA respectively to provide insurance cover on political and related risks.
  - Government to provide premium subsidies for low income people.
  - Government to promote micro-insurance facilities to cover agriculture and related risks.

# INSURANCE REGULATION

- Governments in various emerging markets have set up regulatory bodies to monitor the operations of insurance companies and to protect the interest of the policyholders.
- The regulatory bodies are at different levels of development with some adequately resourced in order to execute their mandates effectively, and others are not.
- Most regulators in the developing and emerging markets are trying to bring insurance practices and procedures in line with best practices in Corporate Governance and stringent solvency Rules.
- Some of the International financial Institutions have offered to train regulators in developing and emerging markets in order to improve the level of supervision.
- Equally important is monitoring and curtailing corruption in some markets which prejudices Reinsurance operations in creating unnecessary costs and delays in underwriting and processing claims.

# CAPITAL ADEQUACY

- Issues of capital adequacy have taken centre stage in developing and emerging market economies especially in light of the rising incidence of catastrophic events.
- Rating agencies and regulators are scrutinizing financial positions of companies to ascertain the quality of the assets, especially liquidity.
- Reinsurance companies operating in some developing and emerging markets are pretty low on capital and there is clearly a challenge with underwriting capacity.
- Reinsurers are forced to write lowly valued risks and take small lines.
- Reinsurers should aim to capitalize at above $100 million if they are to make an impact especially in the light of growing Natural Catastrophes.
- Although losses from natural disasters do not always translate into major insurance losses, there is need to grow underwriting capacity in order to boost retention, which helps to grow the local industry.
- Capacity can also be created through syndicated capitalization, insurance and Reinsurance pools, and mergers and acquisitions, some even across geographical regions.
- While listing on Stock exchanges can also be instrumental in building capacity by raising capital for reinsurance companies, the common trends have been joint venture partnerships to build capacity with institutions such as International Finance Corporation (IFC), African Development Bank etc.
- Regulations such as restrictions on investment thresholds for foreign investors are put in place with genuine intention to promote local entrepreneurship, but they must be implemented with some measure of flexibility and on a case by case basis.
- Sometimes deficiencies in infrastructure are a hindrance to investment.

# CAPITAL MARKETS

- **Stock markets in emerging markets are at different levels of development.**

- **The slowdown in the growth of the Chinese economy and the rapid decline of oil prices and other commodities on the international market have negatively affected the performances of the equity markets in emerging markets in 2015.**

- **Stock markets in emerging markets had registered a negative return of -17,6% on a year to date basis at the beginning of September 2015, compared to a negative of 06,5% for the world index.**

- **The S & P all Africa returned a negative -8,7% (-13,2% in 2014) in August 2015.**

- **The appreciation of the USD against all major currencies is affecting the performance of some bourses.**

- **The creation by BRICS members, of the New Development Bank (NDB) with an initial capital of $50 billion,, is a positive step in reforming the international financial system.**

- **The Bank is to focus on infrastructure funding in the emerging economies on more relaxed lending conditions.**

- **There will be downstream benefits for the emerging market reinsurance companies.**

# RISK MANAGEMENT

- In light of the increasing natural catastrophes, there is a trend for improvement in risk management skills and procedures.
- Reinsurance companies in developing and emerging markets play a pivotal role in risk management activities.
- Survey reports assist in the underwriting and claims settlement processes.
- Organizations are also expected to implement Enterprise Wide Risk management systems to look at emerging risks and take steps to prevent or mitigate the risks.

# INSURANCE POOLS

- Reinsurance pools playing significant role to fill the capacity gaps ,especially in underwriting oil and gas risks.
- International oil companies like Total, Shell and Chevron have their own captive insurance companies.
- The African Oil and Energy Pool was formed in 1989 by the AIO and has been very successful.
- The appetite to write oil and gas risks is on the increase on the African Continent notwithstanding the low capital bases of the companies.
- The increase of insurance capitalization levels in Nigeria has resulted in the placement of more oil and gas business with local insurers, though they still have low retention levels.

# RATING OF REINSURERS

- **Whilst rating of companies in most markets is voluntary, the trend by reinsurers is to go for rating.**

- **Rating carries an advantage in that it facilitates marketing activities for the company.**

- **The common rating agencies used are Syndicate, AM Best,  Moody's and Standard Poor (S & P).**

- **Most African countries especially in Southern Africa, use Global Credit Rating (GCR)  because it is a homegrown agency that understands the dynamics of the markets.**

- **Most rating agencies are also evaluating catastrophe risk aspects apart from sovereign risk, liquidity risk, adequacy of reinsurance and etc.**

- **Most insurance companies operating in African countries do not get excellent ratings mainly due to low sovereign ratings.**

# PROFITABILITY OF REINSURERS

- Market conditions becoming highly competitive in most emerging markets mainly due to the opening up of markets due to liberalization and globalization.

- Most emerging market reinsurers operate in high cost environments.

- Expense ratios are typically above 30% against the international benchmarks of 5-10% for reinsurance companies.

- Cost containment and management is a major issue.

- Claims ratios are also elevated in view of increases in catastrophic losses events.

- All these factors are putting pressure on profit margins.

# SKILLS DEVELOPMENT AND TRANSFER

- Rising risks from natural disasters require effective risk management and underwriting techniques.
- Skills development is a key ingredient in tracking emerging market reinsurers competitiveness on the global reinsurance market.
- There is need for intensive training programmes and maintaining adequate skills bases.
- Partnerships with insurers from advanced countries are necessary for skills transfer.
- Reinsurers in emerging markets are also offering training to other cedant market as a competitive tool to gain market access and grow market share.
- Staff need core leadership and managerial skills as well as technical skills such as actuarial, lost adjusting and specialized underwriting skills.
- Research and development capacity needs to be enhanced in the emerging market players in order to reduce dependence from insurers in advanced economies for product development and underwriting techniques for catastrophes and related risks.
- Insurance companies in emerging markets need to increase investment in ICT.
- New technologies are necessary to improve efficiencies in underwriting and policy administration.

# CONCLUDING REMARKS

- The increasing incidence of Natural disasters all over the world is influencing reinsurance trends in many markets.
- Clearly, there are gaps in insurance for catastrophe events mainly due to low incomes and lack of awareness about the need for insurance in some countries.
- Governments and NGOs often have to bear the cost of rehabilitating the victims of natural disasters.
- Most companies in emerging market do not have the financial capacity to compensate the victims.
- People and Institutions need to be educated about the need to take insurance for catastrophe risks and losses.
- There is need for active partnership between Governments, Corporate Bodies, Civil Society and the Insurance/Reinsurance fraternity to gather data and Information about natural disasters and design programs to avoid or reduce their effects.
- Insurance must be responsive to the broader needs of societies and make a positive contribution to the socio-economic development of countries in the developing and emerging markets.
- Appropriate institutions and products to cover natural catastrophe risks must be developed and be widely available to the populace.
- I salute the President of AIRDC.
- I salute leadership and I salute the membership and Delegates.
- I thank you.