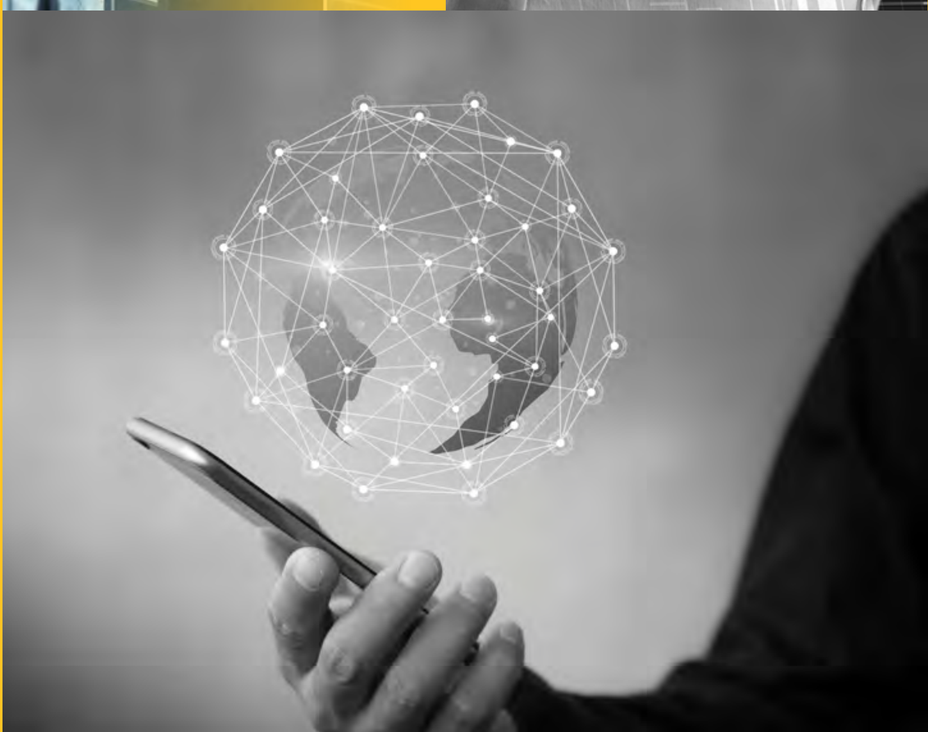


SANTAM INSURANCE BAROMETER REPORT 2020/21

CONTENTS

01
INTRODUCTION

Risk is constantly evolving, though it usually changes shape at a relatively gradual pace.

For example, social disquiet has been brewing under the surface of life in South Africa for some time now, driven in no small part by high and rising unemployment. Even before the rioting, looting and violence experienced in July 2021, we were seeing an increase in malicious damage to property, especially among our vehicle fleets.

READY FOR CHANGE

Edward Gibbens
Executive head: Commercial and Personal

Further vandalisation and destruction of productive assets will have significant consequences for the insurance industry and the economy at large, which are already reeling from the impact of a global pandemic

> The COVID-19 pandemic has turned out to be a powerful accelerant of risk – an example of risk changing shape in a swift and unexpected way. It has forced rapid and meaningful change in our collective behaviour.

As a result, the insurance industry is facing seismic shifts to which it must adapt quickly in order to meet market needs.

In the 2020/21 Santam Insurance Barometer Report, we surveyed 400 corporate and commercial entities, 401 consumers, and 150 intermediaries across South Africa. Our goal was to discover how the risk landscape has changed, measure the general level of awareness in the market about both current and emerging risks, and explore what stakeholders can do to remain relevant in the insurance value chain.

Some of the notable findings in the report: over 97% of large corporates had staff working from home during the lockdown, with commercial businesses and small and medium enterprises (SMEs) reporting figures of roughly two thirds; the average consumer is now driving 90 km per week, down from 162 km; and three out of four people are using more technology than before the pandemic hit.

Over 97% of large corporates had staff working from home during the lockdown; the average consumer is now driving 90 km per week, down from 162 km

These significant changes in our behaviour have had an immediate impact on the insurance industry. While there have been a general reduction in claims volumes across both Personal and Commercial Lines of insurance, we have seen a marked increase in claim values on the converse.

The pandemic has also brought forward the need for changes that, just 18 months ago, formed part of long-term planning initiatives. This applies to the full length of the insurance value chain, from commercial and personal clients, to intermediaries, insurers, and reinsurers.

> A weak economy and political unrest, both catalysts in the widespread looting we bore witness to in July this year, remain high on the list of survey participant concerns. Combined, these systemic risks make insurance less affordable, resulting in increased vulnerability of South African citizens and businesses.

In addition, this year's findings also detail a plethora of risks that have been accelerated and amplified by the pandemic. The rapid adoption of technology is a dominant theme throughout given that it impacts not only how customers are engaging with their intermediaries and insurers, but also their specific insurance needs – the technology trend comes packaged with a rising threat of cyber crime. Business interruption (BI) remains a concern as the risks associated with pandemics, cyber attacks, and climate change gain momentum and recognition.

Another visible step change relates to the role of the intermediary. With the rising tide of risk, and its complexity deepening, the traditional off-the-shelf insurance products face affordability headwinds.

> To continue to provide their clients with cost-effective but comprehensive cover that meet their needs, intermediaries will need to take a more client-centric approach, offering tailored insurance services.

An integral part of those solutions will be advice on how clients can better manage their risks to prevent them from occurring in the first place. Whereas the traditional role of an insurance provider was to transfer risk, risk mitigation is now becoming a critical value proposition.

Insurers have a responsibility and the means to help intermediaries navigate the changing risk landscape, as well as the parallel challenge of rapidly evolving client needs.

For example, the report elaborates on how better collaboration is needed to leverage customer data in providing customised products and personalised services. Insurer-led innovation is another prominent theme, where the likes of pay-as-you-drive insurance, technology-only cover, and cyber insurance add-ons are entering the fray. Santam's pilot of an agricultural index, the first of its kind in South Africa, is also explored.

On a personal note, there is one research finding that I would like to highlight. Of all the constituents surveyed, an overwhelming majority found their insurance providers, including Santam, to have been supportive during what has been the biggest crisis in living memory. As risk explodes, the value we provide as an industry has never been more relevant. We are proud to have played a part in being counted for our clients and we believe we should all be proud of being a part of our amazing industry.

Our hope is that the insights found in this year's report will prove valuable to all our insurance stakeholders. In addition, we encourage the intermediaries who partner with Santam to use its contents to challenge us to be better, to spark tough but necessary conversations, and to help us innovate.

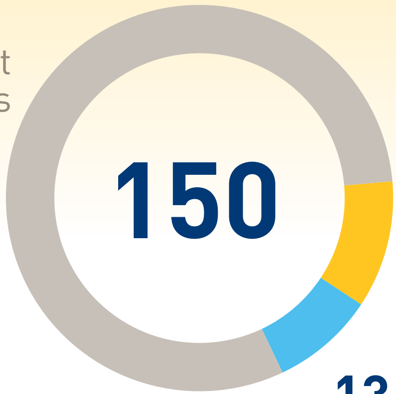
> By pulling together, we can leverage the current uncertainty to create a stronger, more sustainable, and more prosperous insurance industry where everyone is a beneficiary.

Significant changes in behaviour have had an immediate impact on the insurance industry. While there have been a general reduction in claims volumes across both Personal and Commercial Lines of insurance, we have seen a marked increase in claim values on the converse.

02 SURVEY PARTICIPANTS

951 Zoom-based interviews

121 independent intermediaries



16 national intermediaries

13 tied intermediaries

90 commercial

60 personal

RESEARCH METHODOLOGY

25 minute self-completion online interviews

150 intermediaries

400 corporate/ commercial

401 consumers

Research period

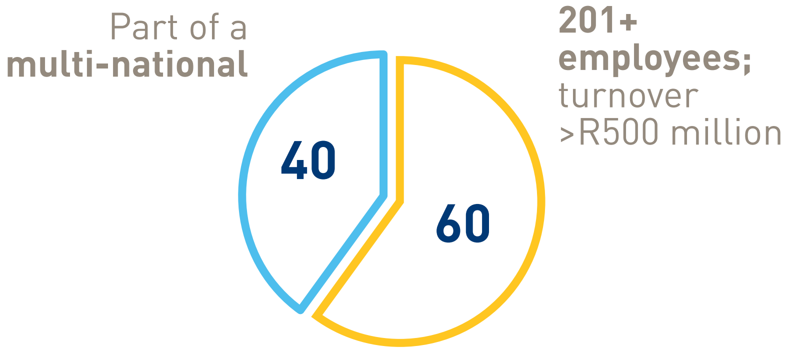
November 2020 – April 2021

Note: 79 intermediaries provide advice to niche industries: agriculture, aviation, construction, marine and transport.

THE SAMPLE

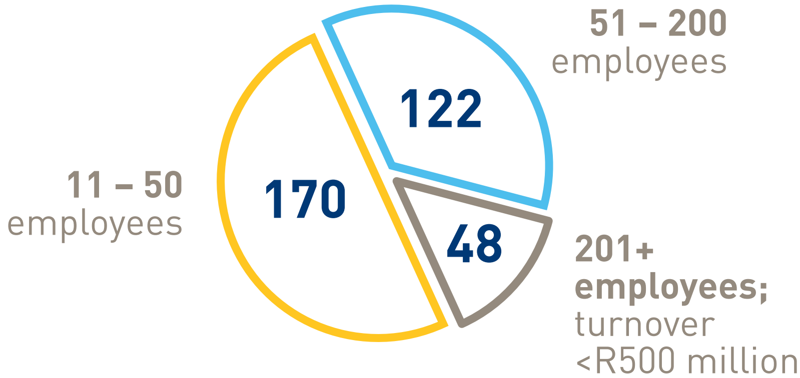
Corporates

total sample size (60)



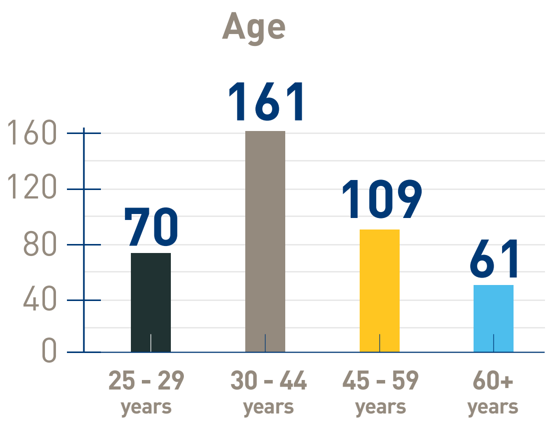
Commercial

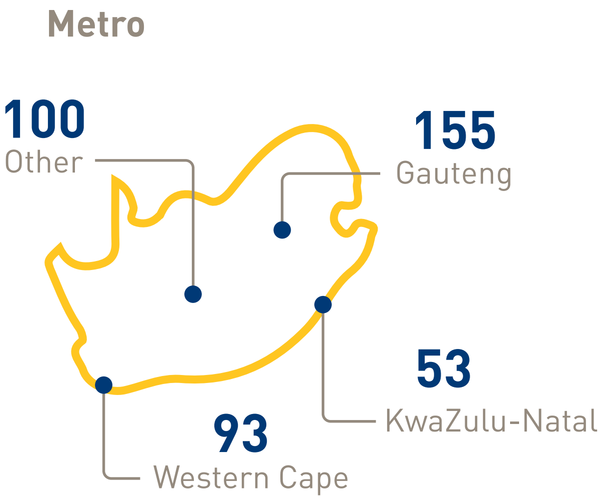
total sample size (340)

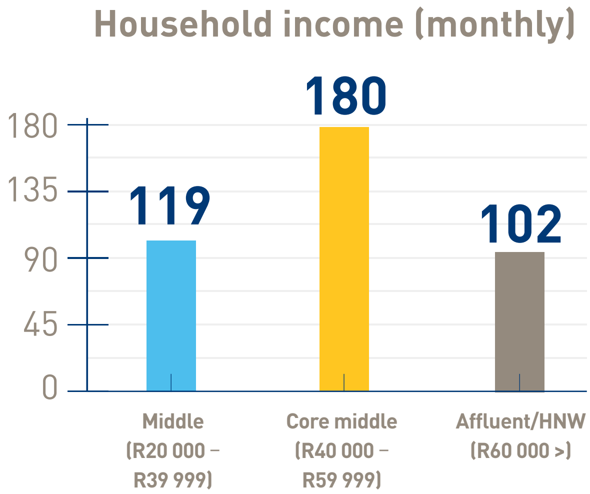


Consumers

total sample size (401)







Mix of industry sectors including 121 from niche industries: agriculture, aviation, construction, marine and transport.

03
KEY THEMES AND TRENDS

"Emerging" risk concerns for corporate/commercial entities over the next two years centre on the economy and the continued fall out from the pandemic in terms of BI.

Challenging economy
2020/21: **62%**
2019: **67%**

Pandemic impact on BI
2020/21: **57%**
2019: **N/A**

Political unrest
2020/21: **48%**
2019: **56%**

Social change
2020/21: **44%**
2019: **46%**

% of commercial respondents rating 8 - 10/10 as a high business risk in the next two years

Base: Corporate/Commercial 2020/21 n=400; 2019 n=169

Cyber crime
2020/21: **36%**
2019: **36%**

Climate change
2020/21: **35%**
2019: **30%**

Regulatory change
2020/21: **32%**
2019: **28%**

Technological change
2020/21: **30%**
2019: **22%**

04 SYSTEMIC RISK AND PANDEMICS

TOP EMERGING RISKS

50% political unrest

45% cyber crime

RESILIENCE AND ACCESS TO CAPITAL IN A TIME OF SYSTEMIC RISK

John Melville
Executive head: Underwriting services, reinsurance and international

A thriving insurance sector is a critical cog in any healthy economy, for two reasons.

Firstly, insurance makes people and businesses more resilient. Adequate cover helps them to bounce back when things go wrong. The knock-on effect of this is that they have more financial confidence, which means they will be happier to spend more in their personal lives and invest in their businesses; both serve as the lifeblood of economic growth.

Secondly, insurance is often a prerequisite for borrowing and gaining access to capital. For example, to get financing for your house or factory, the bank lending you the money will likely require that the property is sufficiently insured against a calamity that reduces or destroys its value.

> If resilience gives you the confidence to spend, access to capital gives you the means to do so.

Systemic risk refers to risks that typically play out as a chain reaction in a system resulting in widespread losses to individuals, businesses, industries, and even countries. Examples of systemic risks are pandemics, climate change, cyber risks, political instability, etc. Indeed, political unrest (50%), cyber crime (45%), and the pandemic impact on BI were three of the top four emerging risks identified by commercial intermediaries in this year's research. Such risks are a threat to both resilience and access to capital because they are increasingly difficult or expensive to insure against.

For example, the COVID-19 pandemic has triggered a raft of exclusions and higher premiums both locally and globally in insurance and reinsurance contracts. This has resulted in reduced capacity in certain lines of insurance for insurers and reinsurers alike. Similarly, reinsurers are raising their catastrophe reinsurance premiums off the back of higher risks associated with climate change. The insurance industry, along with its public sector counterparts, must adapt to meet these challenges to strengthen resilience and access to capital.

The ability of insurers to provide cover for systemic risk largely depends on whether reinsurers are willing to underwrite the risk. As the economic impact of COVID-19 became clear, reinsurers moved quickly to exclude pandemic risk from their coverages.

Without the ability to diversify such risk, even in the context of a global premium pool, the potential liability of a pandemic was simply too large for them to cover, deeming it effectively 'uninsurable'.

> Uninsurable risks, characterised by large numbers of people and businesses suffering a loss at the same time, are usually addressed through government relief programmes.

In such instances, there are simply too many simultaneous claims, making it impossible for insurers and reinsurers to shoulder the financial fallout. Similar exclusions are commonly imposed in the event of a nuclear disaster, terrorism, and war.

It stands to reason that if something cannot be diversified, it cannot be insured, but if you can diversify at a global level, then it can often be insured. Santam is actively working with a global reinsurer to explore how we can provide selective, local epidemic and pandemic cover for the corporate market in the future. Another way of insuring against an event like a pandemic could be to build up a fund over time in partnership with government that everybody can draw from when it hits.

In the meantime, individuals and businesses must share the responsibility to protect themselves against uninsurable risks. For the most part, protection must come in the form of better risk management that culminates in risk prevention. We believe it falls to insurance industry stakeholders to drive awareness around such practices.

Where risk is unavoidable, governments should use their sizeable balance sheets and ability to legislate to form public private partnerships (PPPs) with insurance industry stakeholders, in order to provide some protection.

As an example, consider the small-scale farming industry and the ever-present threat of drought or flooding it faces due to climate change. Practices like conservation tillage and the planting of cover crops can help prevent soil erosion and improve moisture retention. More focus on these types of risk management initiatives will help to reduce the impact of severe weather events.

However, due to the nature of systemic risks, there will always be instances where even the best attempts to manage the risk will fail. In such scenarios, farmers who find themselves destitute after losing their crops or livestock could find relief from a PPP insurance scheme.

What might a scheme of this ilk look like? Government would create the legislation for the structure and operation of the PPP. An aggregator could then collect a small premium from a large number of farmers that would be paid into a fund managed by a private sector insurer. Distributions would be paid out to affected members in the case of a severe weather event, such as drought, flood, hail or frost. If the assets of the PPP were insufficient to provide adequate relief, the second port of call could be a reinsurer, whereafter the government could act as the reinsurer of last resort. We were pleased to see that intermediaries support the PPP model. Six in 10 intermediaries surveyed believe that PPPs will be essential to the sustainability of the insurance industry in the face of systemic risks.

Six in 10 intermediaries surveyed believe that PPPs will be essential to the sustainability of the insurance industry.

In South Africa, we already have a successful blueprint of such a model in South African Special Risk Insurance Association (SASRIA). Instead of reinventing the wheel, we believe its mandate should be expanded to provide more protection against the rising risks we face. Leveraging the expertise in the private sector would add further impetus to such a model. Encouragingly, **we are seeing evidence that the trust deficit between the public and private sector is narrowing, making these types of essential partnerships more likely.** They have a particularly important role to play in fostering resilience among our citizens.

The reality in South Africa is that many individuals do not have the resources to buy insurance. Yet these are often the individuals who need it most to keep extreme poverty from their door when systemic risk events occur. Again, the private and public sectors have the combined resources to find a solution; it is already being done elsewhere on the continent.

The African Risk Capacity (ARC), an African Union agency, is a great example of how to protect those who cannot afford insurance. Through collaboration and innovative financing solutions, ARC has helped African governments to strengthen their disaster risk management systems in the form of early weather warnings and contingency planning, as well as securing access to relief funding when disaster strikes.

We are driving similar innovation at Santam. In collaboration with the South African Insurance Regulators, through their innovation sandbox, we have been given permission to conduct a pilot for a Soil Moisture Index where policyholders will receive relief when the index drops below a certain level during periods of drought.

> Indeed, one of the silver linings of COVID-19 is that, facing a complex challenge, we can pull together the smartest minds from around the globe into one "room" faster and more effectively than ever before using the likes of Microsoft Teams or Zoom.

The research shows that three in every four individuals are using more technology than before the pandemic. This rapid adoption of technology has undoubtedly unlocked opportunities, made us more productive and encouraged innovation enabling us to provide better products. From where we stand, innovation in the insurance industry has more momentum than ever before, which is just as well because the rising complexity of the emerging risks we face needs a commitment to innovation.

3 in 4

individuals are using more technology than before the pandemic

Somewhat ironically, the rapid adoption of digital technologies since the start of the pandemic has made us more vulnerable to another potential systemic risk, cyber crime. Instances are still relatively low, but the structural shift towards remote working and digital communication give hackers more opportunity to infiltrate our digital worlds. Again, the initial focus here needs to be on risk management. Simple measures such as making sure your anti-virus software is up to date and educating employees on email phishing techniques would help to prevent the majority of cyber attacks.

Where cyber criminals are successful, having the right cover in place will provide timely access to service providers that will help businesses manage any potential fallout and possible clean-up operations, allowing them to operate as seamlessly as possible while managing the situation. Cyber crime is a complex and continuously evolving risk that requires more attention than it is currently receiving. The binding requirements of the Protection of Personal Information Act, 4 of 2013 (POPIA), effective from 1 July 2021, creates an additional layer of complexity.

If reasonable steps to comply with this regulation have not been taken, and a personal information breach occurs, businesses and individuals may be held liable through hefty fines (up to R10 million) and even jail time. It is of vital importance that the risk protection gap against cyber crime and POPIA is closed given the potential consequences. Underwriting the widespread risk of cyber insurance may be an opportunity to counteract the industry-wide premium reductions in motor and personal lines driven by the rise in pay-as-you-go insurance products.

> Perhaps one of the less appreciated risks in South Africa is the impact of failing power, water, port, rail, and road infrastructure. It clearly chokes the economic growth we so desperately need to reduce our debilitating unemployment.

The second order effect of poor infrastructure is more costly insurance. For example, a lack of fire hydrants or inadequate stormwater drainage may result in greater fire or flooding damage than would otherwise have been the case. That filters through into a higher cost of insurance, ultimately reducing resilience and access to capital. That insidious transfer mechanism makes it more difficult to do business and create jobs.

In the context of infrastructure development, it is interesting to note the impact of government regulation and corporate responsibility on the trends in underwriting risk. In some cases, we are already seeing reinsurers scaling back or zeroing their willingness to underwrite new risk in the fossil fuel industry to help meet the raft of emissions targets set to combat climate change. In theory, this will reduce access to capital for "dirty" energy projects, redirecting capital to more sustainable infrastructure development.

At Santam, we have embraced this shift. Our underwriting support of the Renewable Energy Independent Power Producers Programme (REIPPP) over the past decade has given those tasked with greening our energy mix access to the capital they need, as well as the resilience that is key to the development of any nascent industry. At the same time, we are working closely with reinsurers to ensure that our legacy infrastructure remains insurable during what is likely to be a lengthy transition to cleaner energy.

Systemic risk will continue to evolve into an ever more complex animal. As insurers, we need to prioritise our understanding of these risks and drive the innovation and collaboration needed to help individuals and businesses remain resilient and ensure continued access to capital.

05
ROLE OF THE INTERMEDIARY

For the insurance industry, the pandemic stress-tested the products and relationships that tie together insurers, intermediaries, and their end clients. In some cases, those bonds held firm, and even strengthened; in others, weaknesses were exposed.

INTERMEDIARIES MUST BECOME TRUSTED RISK ADVISERS TO REMAIN RELEVANT

Andrew Coutts,
Head: Intermediated business

The paradox of the COVID-19 pandemic is that while it has been devastating for many South Africans, it has made visible the cracks in the way we do things, giving us the opportunity and motivation to effect change.

Why is it so important for insurance industry stakeholders to reflect on their performance during the pandemic? Because this flash of change and complexity was not an anomaly, but rather part of a larger global trend.

> Risks are increasing exponentially – changing weather patterns that cause extreme flooding or drought, deteriorating water and power infrastructure, and rising instances of cyber crime – these are just a few of the emerging risks that South African businesses and individuals are faced with.

Insurers and intermediaries alike must confront the reality that many of their clients, particularly in commercial businesses, will require a more nuanced insurance offering to effectively protect them in an increasingly complex risk environment.

Much of the traditional role of the intermediary was to sell generic products that would transfer risk away from their clients.

> However, the escalation of risk exposure and complexity, coupled with affordability issues and cheaper alternative channel solutions, render a product – push – only business model by an intermediary uncompetitive.

Where the risks are more straight-forward, the product has largely become a commodity that is easily distributed via technology-enabled direct channels. This all points to the urgent need for a shift in focus to remain relevant.

Intermediaries have always been integral to the success of insurers. They are essential players in the insurance value chain, making material contributions across the advice, sales, marketing, and claims handling functions. However, the role of the intermediary will become even more important as the insurance landscape evolves. Their relationship with the end client puts them at an advantage to explore and thoroughly map out the risks that businesses and individuals face. As clients increasingly seek solutions built for them, the insights gained from client interactions will be invaluable to insurers for the development of affordable, bespoke insurance solutions that meet client needs. More importantly, it will arm insurers with the insight they need to step into the valuable role of risk adviser.

WHEN IT COMES TO ADDING VALUE TO COMMERCIAL BUSINESSES AND UNDERSTANDING THEIR NEEDS,

77%

of intermediaries are on par with claims handling and insurance knowledge/expertise

At Santam, we believe the intermediary can help catalyse a necessary shift in how people and businesses think about insurance.

> As professional risk advisers they could bring more focus to the practice of risk prevention and mitigation as opposed to pure risk transference.

Ultimately, this would reduce the number of total claims, an outcome that is in everyone's interest, because every claim, covered or not, is a set-back. The pandemic has highlighted the fact that some risk events are uninsurable – most reinsurers no longer cover pandemics. Therefore, businesses must develop other strategies to protect themselves against an event like a pandemic; better risk management is required to limit exposure and prevent losses.

The need for intermediaries to move away from a product-push approach toward a more client-centric product build approach is unambiguously reflected in the research. When it comes to adding value to businesses and understanding their needs, 77% of intermediaries are on par with claims handling and insurance knowledge/expertise.

During the pandemic, many intermediaries stood up to the latter two demands through strong claims advocacy and the proactive restructuring of policies to save costs or improve the appropriateness of cover.

We are reminded that in times of significant change, the valuable role of an intermediary is amplified.

However, if intermediaries are to transition into the role of true risk adviser, they will need to strengthen their client relationships even further. A lack of time is one of the primary hurdles preventing them from doing so.

Many intermediaries have found themselves swamped by administrative tasks, particularly policy amendments and cancellations brought on by the pandemic. This has unfortunately taken some focus away from proactively engaging with their clients on their risk exposures and risk management practices.

Furthermore, the demands of regulatory change remain an omnipresent drain on time and has prompted – along with the added pressures of the COVID-19 pandemic – speculation about consolidation within the industry. Though we have not yet seen much evidence of consolidation, we do expect to see more over time. The benefit of consolidation is that it provides the scale necessary to invest in technology, which is now an imperative for intermediaries. We also expect a trend towards more intermediaries joining a tied network. Additionally, there is evidence that multi-line intermediaries have fared better through the pandemic due to their diversified services across both life and short-term products.

Other key deliverables for intermediaries who want to remain relevant include expert product knowledge and the keeping of a thorough record of advice. The contention around the pandemic-induced BI claims has highlighted the importance of understanding not only what is covered by a product, but also what the exclusions are as well as the intention of the product at the time of sale – all of which should be explained to the client in detail and must be meticulously recorded.

The silent cyber risk is of particular concern to insurers and a good example of a very real and widespread threat to which non-damage BI exclusions apply.

Understanding the products, and the intention behind them, will be particularly important in the context of the emerging risks that intermediaries are concerned about, such as cyber crime (45%) and climate change (31%). Having experienced a global pandemic, both the public and regulator will have an expectation that intermediaries have considered every potential risk exposure and aspect of cover to ensure they have provided their clients with sufficient protection. If another black swan event occurs – an Eskom grid failure is not a far-fetched notion, for example – there will be an expectation that the intermediary offered optional non-damage cover extensions (of which there are many) to match their client's potential risk exposure. If the intermediary is found not to have advised their client appropriately, they may find themselves liable for Professional Indemnity claims.

The silent cyber risk is of particular concern to insurers and a good example of a very real and widespread threat to which non-damage BI exclusions apply. For example, if a client who does not have any cyber cover on their policy suffers a hack, he may try to claim against another part of the policy such as the prevention of access extension under the BI section, resulting in resource-draining claims disputes. This is a similar scenario to the pandemic claims, where many businesses did not have disease cover. These types of scenarios around non-damage BI claims create a lot of complexity for intermediaries. It is therefore essential that intermediaries have strong product knowledge and keep a good record of advice which clearly states what is being sold and what the client understands is being sold.

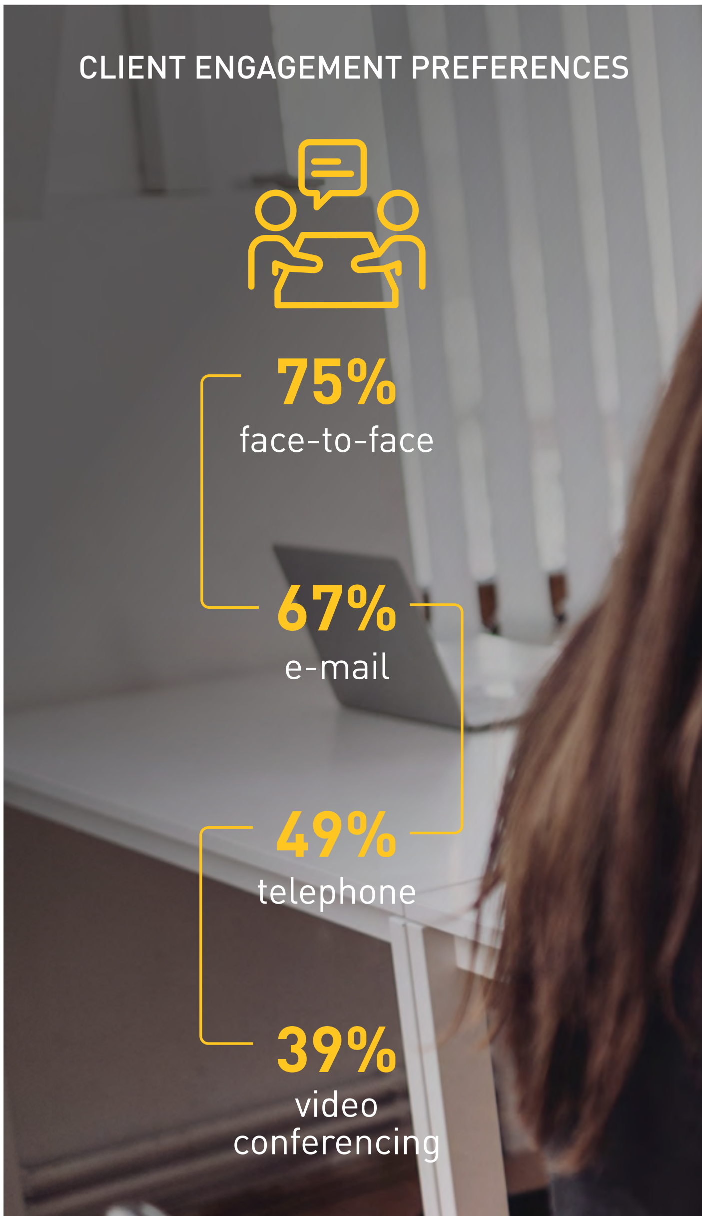
Many insurers are currently working on less ambiguous, yet detailed, policy wordings specifically outlining the intent of the cover to avoid lengthy claim disputes in the future. Policy wording will remain a challenge on this front.

> While 81% of intermediaries said that more simplistic policy language is needed, the industry-wide desire for increasingly comprehensive cover, at lower cost, within a more complex risk environment puts a natural ceiling on the simplification of policy wording.

In addition to an intricate understanding of the insurance policies sold, intermediaries will need to place greater emphasis on the client's record of advice as evidence that cover options (and the intent of the cover) and exclusions were thoroughly explained. Records that state plainly and thoroughly the purpose and extent of insurance provided will help to manage client expectations, reduce claims disputes, and foster healthy working relationships with insurers. Of the intermediaries surveyed, around half expect to put more resources towards helping their clients understand their policies. Clarity around what is covered should also help to prompt questions and debate around what is not covered.

Against this backdrop, it is perhaps not surprising that 50% of intermediaries predict they will need to offer expert product and risk advice within the next two years. However, an intermediary cannot be an authority on everything, which means a certain amount of industry specialisation is to be expected. This is also true for underserved segments of the market, particularly the emerging middle class, where intermediaries are yet to make inroads. However, market entrants in this space can expect to face strong competition from direct insurers.

Another key change expected in the next 24 months is the increased use of technology by intermediaries, both for client interaction and back-office processes.



> The majority of commercial clients using an intermediary (75%) would prefer a return to face-to-face client engagement, but in the absence of those in-person meetings, email (67%) and telephone (49%) are still preferred to video conferencing (39%).

Digital marketing and online multi-quote technologies hold further opportunity for intermediaries, but remain expensive. With regards to back-office functions, an encouraging finding from the research was that many intermediaries will be pursuing better systems integration with insurers in order to speed up the claims and quoting processes.

Intermediaries are seeking better support from insurers in a number of other areas too – 51% would like a broader selection of cover options at different price points. Tools for client education around their own risk management as well as systems training for their staff also featured prominently.

The take-up of Santam's extensive product and systems training initiatives, as well as the dedicated intermediary portal, is providing much-needed support to intermediaries. However, greater awareness of other valuable initiatives like the interactive platform for intermediary feedback, Insurance Sector Education and Training Authority accreditation courses, and the business coaching offering is needed.

There seems to be consensus around the three key value-added services that clients want from their intermediary and insurer. The first is information on how to reduce or better manage their risk. The second is detailed claims monitoring and what impact that activity will have on premiums in the following year. The third is real-time SMS notifications when risk is heightened. These findings support the proposed evolution from insurance facilitator to professional risk adviser.

What is the defining characteristic of a risk adviser? They can sense and respond to risk in real-time. In that vein, a good starting point for any intermediary would be to sit down with their clients at every policy renewal and ask the question, "What could happen next?" What could the next black swan event be? Will the Eskom grid fail? Is there another severe drought around the corner? What if a hacker holds your business to ransom? Constantly exploring such scenarios will not only improve the suitability and affordability of cover, but also differentiate the intermediary as a trusted risk adviser. The next step is to monetise that advice so that intermediary's revenue is not reliant on product sales alone and they are able to confidently embrace their new role.

It is essential that the value proposition of the intermediary aligns with client needs. In an increasingly complex risk landscape, intermediaries will add the most value by ensuring their product knowledge is of the highest quality and that they keep a good record of advice for all clients. Additionally, intermediaries that offer clients value in the form of advice, will struggle less in the price versus value debate.

06 PERSONAL LINES OVERVIEW

ADAPTING TO A NEW RISK LANDSCAPE FOR PERSONAL INSURANCE

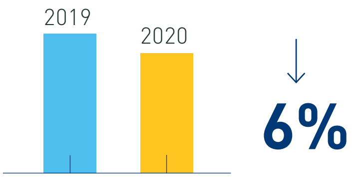
Attie Blaauw
Head: Personal Lines Underwriting

Driving to work every day can be a risky business. Accidents are common, stones hit windshields, and the threat of vehicle theft is ever present. Staying at home is, however, not risk free either; the more you use the things in your house, the greater the chance of them breaking – but that is what insurance is for.

It should come as no surprise then that the pandemic-induced shift to working from home has had a material impact on the shape of the personal insurance landscape. In addition to the amplification of risk, eight in 10 consumers surveyed said the pandemic had a negative effect on their finances, making the affordability of cover a concern. However, the survey found that when cutting back on expenditure, mainly luxury items were relinquished, with general insurance remaining a priority to cover their valuable assets.

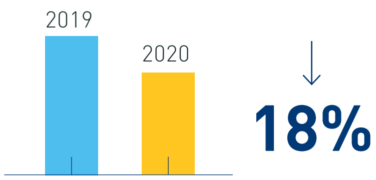
This finding was synonymous with our experience. At Santam, we saw very few cancellations in personal insurance despite consumers being under financial pressure. We put this down to a combination of consumers' perception of their biggest risks and insurance being low down on the list of expenses to cut; the delaying of renewal increases; offering premium relief and refunds to our clients to keep them insured; and less movement across the industry due to significantly fewer requests for quotes during the pandemic.

The **overall volume of Personal Lines insurance claims was down by 6% year-on-year (YOY) in 2020**.



While there was a notable rise in building and household content claims (the second and third largest claim categories respectively), they were offset by a significant decline in motor vehicle claims, which normally accounts for the lion's share of personal insurance claims.

With vehicles parked at home more often, the **volume of motor claims for accidents, glass (windscreen), and theft declined by 18% YOY in 2020**. On the positive side, curfews reduced the number of accidents due to drunk driving, among others. However, the reduction in claims volume was somewhat negated by a hike in the average value claim.



The severity of vehicle accident damage increased due to more people speeding because there are less vehicles to contend with on the road. Additionally, the cost of repairs increased due to the constrained supply of parts resulting from the pandemic.

> Our motor vehicle claims data for Q1 2021, relative to the same period in 2019, is indicative of an irrevocably changed landscape. Despite the easing of lockdown restrictions, the volume of motor vehicle claims is still down 13%.

This suggests that many people are still working from home and may continue to do so even after South Africans have received their vaccine and the COVID-19 threat is no longer pervasive. This trend towards sustained low levels of traffic density is reflected in the research findings;

82% of Personal Lines intermediaries and 46% of consumers surveyed are interested in discounted motor vehicle premiums based on less frequent driving.

The continued downward trend in the number of motor claims is unprecedented; historically, motor claims have risen steadily each and every year without exception.

Conversely to the motor experience, building and household contents insurance claims rose 16% and 6% respectively in 2020. Looking at the research findings, the consumers surveyed might have put this down to what they perceive to be a rise in criminal activity – 82% noted an increase in crime in their area – since the beginning of the pandemic. However, our claims data paints a different picture, with both theft- and burglary-related claims lower in 2020 than they were in 2019. Santam's all risk claims were also down by 16% over the same period.

Staying at home reduces the probability of items being stolen off your person while out and about and deters would-be burglars from entering your home. The additional time spent on social media could explain why crime is perceived to have been worse than our claims suggest. It is worth mentioning that people's perceptions are likely formed by daily news reports and quarterly crime statistics, which did report an increase in crime during the pandemic. However, a lot of the crime reported over the period related to gender-based violence; our claims data is, however, only reflective of insurable crime, where claims due to burglaries and theft declined by 16%.

Burst geysers continue to be the primary contributor to building claims, in which we saw a marked increase of 16% YOY in 2020. This considerable rise in frequency is unusual, pointing to the hidden impact of the pandemic on our homes.

People showering and bathing more often increases wear-and-tear on geysers, which could be one possible explanation for this anomaly. The same reasoning could extend to a similar increase in other plumbing-related claims. On the home contents front, the more time spent at home, the greater the wear-and-tear on our appliances, and the greater the opportunity for accidental damage.

In addition, 16% of consumers upgraded their computers and connectivity to enable them to work from home; three in every four reported an increase in their use of technology.

The heightened frequency of power surges due to load shedding, combined with more expensive technology devices in the home, has undoubtedly played a role in the higher household claims figure for 2020. We also think it reasonable to expect that once the restrictions on movement are eased, claims for theft and burglary may increase as criminals look to lift valuable technology from homes.

While the nature of risk has shifted, perhaps in a structural manner, affordability remains an issue. To reduce underinsurance and narrow the risk protection gap, insurers and intermediaries are looking to offer more cost-effective products, like first-loss or limited cover insurance policies (only fire, or only theft, for example). In addition, client education and engagement that adds value is no longer optional – expert risk mitigation advice from intermediaries is a must.

To illustrate the need for improved communication on all fronts, consider that only 10% of our clients with car insurance have taken advantage of the SmartPark product that gives them a discounted premium depending on their annual mileage and vehicle type. We know that a greater percentage of our clients are working from home and would therefore save on their monthly premium by adding this benefit to policies.

> Product innovation and more effective communication can improve affordability, but they must be underpinned by better risk management practices for the best possible outcome.

Of the Personal Lines intermediaries surveyed, 65% said they want insurers to explain how claims behaviour impacts premiums; 52% want SMS updates for clients when risks are heightened; 51% think a variety of cover options at different price points are needed; 47% want crime statistics per area; and 45% want access to apps that help their clients manage risks better.

Many of these value-adds are already available and ongoing communication will raise awareness of these benefits.

Rewards-based initiatives that encourage a greater focus on risk management are also entering the fray. For example, installing devices that pick up geyser leaks, performing periodic tests on alarm systems, and taking vehicles for voluntary roadworthy tests can help prevent the associated risks from occurring in the first place. Preferential rates for clients who manage their risk using these tools could be used as an incentive for behavioural change. It is a win-win outcome for both client and insurer if we can reduce the number of overall claims through heightened awareness around risk management.

In terms of the preferred channel for purchasing personal lines insurance, direct insurers continue to lead. Our findings showed an upward trend from 74% of respondents in 2019 to 82% in 2020 who make use of direct insurance channels. The number of survey respondents using an intermediary has also increased from 26% in 2019 to 34% in 2020.

It is interesting is that even the direct insurers are acknowledging the value of the intermediary; many now employ tied intermediaries to provide additional support to their clients. To remain relevant in the Personal Lines market, intermediaries should explore new distribution methods, like the referral model where they source quotes on behalf of clients and then, for a fee, hand over the client to the insurer who manages all the administrative tasks.

There is no doubt that the COVID-19 pandemic has altered the risk landscape, maybe for good. The onus now falls to the parties in the insurance value chain to adapt to this new risk landscape. Ongoing client education, improved communication, product innovation, and better risk management all have an essential role to play in ensuring the sustainability of the Personal Lines insurance industry. Ensuring that client needs are met, that they receive value for money and have peace of mind is the ultimate goal.

07 COMMERCIAL LINES OVERVIEW

Corporate and commercial entities are generally hopeful about the future. 83% of large companies and 73% of SMEs surveyed feel optimistic about their business prospects. These figures are indicative of the remarkable resilience and adaptability of South Africans.

RAPIDLY EVOLVING RISKS EMPHASISE A GREATER NEED FOR MORE RISK MANAGEMENT

Philippa Wild
Head: Commercial Underwriting

The COVID-19 pandemic has had a devastating impact on both lives and livelihoods. Our research shows that it has had a materially negative impact on our corporate and commercial clients. However, that is not to say that it has not sparked some positive changes within the industry.

It has, however, resulted in significant financial loss: 62% of corporate and commercial entities have seen a loss in profit; on average profits declined by 38% in SMEs, by 36% in large commercial entities and by 24% in large corporates.

The hospitality sector was, unsurprisingly, hardest hit of all. A massive 41% closed businesses, 84% reported lost profits and 59% indicated they had retrenched staff. Profits were also negatively affected for 80% of transport and 77% of construction companies.

Even against this backdrop, corporate and commercial entities are generally hopeful about the future. According to our research, 83% of large companies and 73% of SMEs feel optimistic about their business prospects.

While these figures are down on 2019's 88%, they remain high and are indicative of the remarkable resilience and adaptability of South Africans. Since the start of the pandemic we have seen evidence that businesses are pivoting to better take advantage of the opportunities presented by our "new normal".

The rapid adoption of technology has disrupted traditional business models, with many firms forced to digitise faster than originally planned; the research found that 97% of large corporates have staff working from home. In many cases, this has prompted a review of risk and insurance coverage.

> What is both interesting and concerning is that despite a significant increase in remote working, and the proliferation in cyber risk that comes with that transition, demand for cyber-related cover has not risen meaningfully over the past 18 months.

Intermediaries have the means to play a critical role in helping clients understand intricate policy details, in demystifying what can often be complex policy language, in handling claims, and in sourcing solutions that meet client needs.

The cost of third-party liability and fines following a major data breach can easily run into millions of rands. Additionally, loss or damage to digital assets is often not covered by standard insurance solutions.

That said, cyber risk is now widely recognised as a global emerging risk and it was encouraging to see a notably higher level of awareness than previously reported among commercial businesses. The 2020 survey findings showed that 45% of commercial intermediaries ranked cyber crime as the third highest business risk, while 36% of corporate and commercial entities ranked it their fourth biggest risk over the next two years. There is, however, still a widespread perception that "It won't happen to me" among South African businesses, which is concerning because the risk protection gap in this category is vast.

We understand the inertia around cyber insurance to some extent, because reported cyber crime incidents are still at a relatively low level in South Africa. However, we believe it is a serious and rapidly escalating risk that must be confronted. With POPIA having just come into effect, companies will be compelled to report cyber-related crimes in which personal information is compromised. We do therefore expect to see an increase in cover required for cyber risk over the coming months.

There is also a misconception that cyber crime is a "big business" problem. This is reflected in the survey findings which show that the uptake of cyber cover is highest among large corporates. While large institutions may represent more lucrative targets, smaller businesses are easier to attack because they often lack the advanced security measures required.

It's crucial that both big and small businesses recognise the significant threat that cyber crime poses, and ensure they are adequately protected against its potentially crippling effects. We believe that intermediaries will be key in driving broader and sustained awareness around cyber crime. They have an important role to play in educating their clients about the benefits of cyber insurance and explaining how the cover works.

> The research found that intermediaries add the most value where knowledge and expertise is required to identify risks and find solutions that match client needs. Such knowledge and expertise will undoubtedly be required in the case of a complex, emerging and as-yet relatively unfamiliar risk like cyber crime.

This is just one area in which we think the guidance of an intermediary will be crucial for commercial entities. Intermediaries have the means to play a critical role in helping clients understand intricate policy details, in demystifying what can often be complex policy language, in handling claims, and in sourcing solutions that meet client needs.

Despite this, the demand for purchasing insurance from direct channels continues to increase. Where clients understand their insurance needs well and can navigate their insurance policy schedules and wordings effectively themselves, purchasing insurance directly may be appropriate. However, care is always required to ensure your insurance policy responds in the manner you expect it to when something unforeseen happens. Having an intermediary really helps in this regard.

> The risk landscape is becoming increasingly complex. Given the critical role insurance plays in facilitating business continuity in the event of a claim incident, the decision to purchase insurance must involve more than a cost analysis.

For example, using an intermediary gives the client access to a wealth of in-depth market knowledge and claims handling expertise. It is vital that these benefits are weighed up in conjunction with cost considerations.

The overall volume of property claims increased by 7% YOY in 2020 while the average cost per claim shot up by a staggering 103% in the same period. This was mainly driven by contingent business interruption (CBI) claims.

Admittedly, insurers could be doing more to support intermediaries in educating their clients. The survey results show that intermediaries need insurers to provide better training to customer service and claims handling staff, facilitate client education and provide tools to help them engage in their own risk management, and work towards simpler, clearer policy wording. This last point remains a priority at Santam, but the need for it was amplified by the COVID-19 pandemic.

Santam's claims data paints a picture of the risks that had the biggest impact on clients. **The overall volume of property claims increased by 7% YOY in 2020 while the average cost per claim shot up by a staggering 103% in the same period. This was mainly driven by CBI claims** – cover that is wider than traditional business interruption cover that only covers losses following property damage.

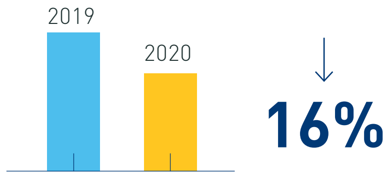
The average cost per claim shot up by a staggering 103%.

In terms of other traditional risks, the top five ranking risks according to commercial intermediaries are fire (51%), motor vehicle (44%), business interruption (41%), theft (29%) and public liability (17%).

There was some misalignment between intermediaries and commercial entities who, ranked theft (34%), economic downturn (34%), fire (26%), motor vehicle (21%) and business interruption (17%) as their top five risks.

In terms of Santam's claims experience over the same period, there have been fewer fire claims than usual as business premises were unoccupied for an extended period. In a normal year, we would expect the value of our fire claims to be the highest of all the categories, but this year the value of CBI claims is significant.

Looking at the other commercial insurance classes, **motor claims volumes, which have been steadily rising every year pre-COVID-19, are down meaningfully: -16% YOY in 2020, and -6% between Q1 2020 and Q1 2021**. That said, motor claims are still our biggest category by volume despite this drop in volumes.



The average cost per motor claim is up marginally between 2019 and 2020 (2.8%) and a higher 8.2% between Q1 2020 and Q1 2021. This was the second largest commercial claims category by value after CBI.

Motor claims volumes are down because people have been driving less since the pandemic started. However, the average cost of claims is up because those accidents that do happen are more severe. This could be because with fewer cars on the road there is more opportunity to speed. We do not believe traffic density is going to return to pre-pandemic levels anytime soon for the simple reason that remote working is likely here to stay, at least to some degree.

In light of the complex risks the new normal brings, it is more important than ever for businesses to fully understand exactly how their insurance cover is structured, and how they can reduce the frequency and severity of risk events through suitable risk management practices. It was positive to see that of the 400 companies we surveyed, all said they have risk management measures in place, though large companies typically have more than SMEs: 92% of corporates, 87% of large commercial entities and 78% of SMEs take proactive risk management seriously. Though these relatively high numbers are encouraging, it is businesses that do not take it seriously that are of grave concern to us.

All of the 400 companies we surveyed have risk management measures in place

There are easy and cost-effective ways to reduce a company's exposure to both traditional and emerging risks. To manage fire risks, commercial entities can promote clean and uncluttered workspaces, train staff on firefighting, store documents and equipment safely, maintain good standards around electrical wiring and distribution boards, plant and machinery, and provide easy access to well-maintained firefighting equipment.

In terms of theft, burglar bars, alarm systems, security access and walls (whether physical or digital) can all contribute to lowering the chances of a significant theft event. Telematics is an option for managing motor risk, while providing suitable education, training and incentivisation of staff can help to mitigate against severe risk incidents involving human capital.

Many businesses have spent the last 15 months fighting to keep their doors open. In some instances, this has led to basic risk management practices, that should be part of routine business maintenance, falling down the priority list. Business owners are urged to remember that insurance cover and good risk management go hand-in-hand to provide the necessary protection.

Traditional risks aside, pre-pandemic emerging risks are ever present in South Africa: political unrest, a challenging economy, cyber crime, and social and climate change. Corporates and commercial businesses need to be as prepared as possible to protect themselves against these and other emerging risks. Adequate insurance cover and effective risk management will be key to achieving that goal. However, this will require closer relationships between insurers, intermediaries and their clients.

08 SPECIALIST AND NICHE BUSINESS

In terms of emerging risks the corporate and commercial entities we surveyed ranked their top risks as the COVID-19 pandemic impact on business interruption (57%) followed by political unrest (48%), social change (44%), cyber crime (36%) and climate change (35%).

COLLABORATIVE RISK MANAGEMENT CENTRAL TO A NEW INSURANCE PARADIGM

Vuyo Rankoe
Head Niche Business

According to Santam's research, a struggling South African economy remains the biggest emerging concern for commercial entities – 62% of respondents ranked this as their number one worry.

The economic downturn has impacted businesses across our specialist lines of insurance. In particular, we have seen the marine, heavy haulage, taxis (including e-hailing), aviation, travel and the construction industries contract as a result of the economic challenges. The fallout from the COVID-19 pandemic has resulted in businesses facing closure or operating at a significantly reduced capacity, and we have also seen industry consolidation and reduced insurance cover. We expect some of these to reverse as the economy recovers, presenting opportunities for growth in specialist lines.

Conversely, we have seen property and liability classes remain relatively stable for medium to large commercial entities. There is real scope for growth in these two categories, but this will be driven by SMEs and related strategies.

Many businesses were compelled to pivot their business models and reinvent themselves during the pandemic in order to keep operating, thereby exposing themselves to new and unfamiliar risks. Furthermore, companies moved to skeleton staff, resulting in larger losses and rising cost of claims as risk management practices appear to have fallen down the list of priorities.

In terms of emerging risks, corporate and commercial entities surveyed ranked their top risks as the COVID-19 pandemic impact on business interruption (57%) followed by political unrest (48%), social change (44%), cyber crime (36%) and climate change (35%).

While climate change ranks lowest as an emerging risk, we have seen a notable increase in the frequency and severity of weather-related incidents across the globe. Some recent examples include the bushfires in Australia and the wildfires and hurricanes that ravaged the US.

Insurers may look to narrow their offerings away from unsustainable lines, fuelling further consolidation. The segments that are most at risk are the construction, transport and travel lines.

When looking at the more traditional risks that commercial entities face, fire damage and the resulting impact on business interruption is by far the biggest category. There were a number of large-scale fires and explosion-related losses across South Africa in the past 18 months, including the Table Mountain National Park fire that damaged parts of the University of Cape Town, the Charlotte Maxeke Johannesburg Academic Hospital blaze and an explosion at the Astron Energy oil refinery in Cape Town, to name a few.

A hardening insurance market shows no signs of abating through 2021 and beyond. As a result, capacity has been restricted in the liability classes where we have seen a notable uptick in third party events. We have seen an increase in demand for directors and officers (D&O) cover in particular. Indeed, the past 18 months have seen risks, especially liability-related risks, intensify the world over and global reinsurance rates have risen significantly as a result.

Higher reinsurance rates as a consequence of reduced capacity and tighter reinsurance terms have impacted local insurers who have taken on more risk, and consequently premiums have increased – particularly in the liability and property classes.

The hard market cycle makes insurance more costly and those looking to insure are likely to be more discerning. Large corporates, while not reducing cover, are shopping around for the best value insurance products, often delaying their policy renewals. At the same time, some niche industries have seen clients amend their cover.

This has especially been the case in the construction sector (given less infrastructure development) while businesses in the marine and heavy haulage industries have amended their policies to match their reduction in turnover. Consequently, insurers may look to narrow their offerings away from unsustainable lines, fuelling further consolidation. The segments that are most at risk are the construction, transport and travel lines.

The aviation and travel industries were particularly hard hit by the pandemic and the accompanying restrictions on movement. Our insurance volumes for the outbound travel business are roughly 30% of where they were a year ago (recorded volumes are due to regional travel).

The aviation business has also seen lower volumes given reduced charter flights due to 80% of aircraft clients being grounded between April and August 2020, and the closure of flight schools (80 – 90% of whose students are international). We have also seen an uptick in the frequency and severity of large losses in this business. At the beginning of 2021 there were around 10 aviation-related incidents with damages estimated at over R250 million. More than 90% of insurance claims are historically due to pilot error, mostly occurring at take-off and landing. However, issues currently under investigation are for damages resulting from mechanical or maintenance issues due to disuse.

The transportation sector is the veins of the economy and has also been negatively impacted by the pandemic. According to our research, 80% of respondents operating in the commercial transport sector reported a loss in profits in 2020. The numerous business closures in this sector have increased the workload of those still operating, which manifests in employees (including truck drivers) working longer hours and increasing the chances of fatigue-related truck accidents.

Poor economic growth and excessive unemployment are also powerful catalysts for underlying social discontent which has led to rising incidences of malicious damage to property. Compounding the problem is the poor maintenance of the country's road infrastructure. Potholes, shoulder-less roads, and poor lighting all contribute to a higher truck accident tally. The rising cost of imported vehicle parts has added to this problem.

The cost of truck repairs has risen significantly, in some instances by as much as 40%, partly due to original engine manufacturers producing trucks that are far more sophisticated, some of which now cost in the region of up to R2 million. It is also partly due to a constrained supply chain causing a delay in parts supply.

This has the potential to increase costs as the global economy struggles to catch up on congested ports, as well as start-stop economic impacts on scaling demand.

It should therefore come as no surprise that we have experienced higher frequency and severity losses in the heavy haulage industry. **Our claims data shows an increase of 25% in volume and 30% in the average cost of claims.**

The deterioration in public-owned infrastructure is a problem not only for the transport industry, but for the whole economy. The importance of addressing this issue cannot be emphasised enough. We are becoming increasingly concerned about water supply given the dire state, and continued deterioration, of reservoirs and pump infrastructure in South Africa. While we acknowledge that it comes down to a balance of affordability for government, it is well documented that functioning safe infrastructure is one of the crucial building blocks for economic growth; prioritising it will generate social, environmental, and financial returns worth the investment.

Stagnant economic growth puts pressure on business revenues across industries. To ensure both their sustainability and profitability in such an environment, business owners must keep a tight rein on their expenses.

Underinsurance is a problem that we highlighted in the 2019 report, however the prevalence and extent of underinsurance has become more evident due to the pandemic.

> The prevalence and extent of underinsurance has become more evident due to the pandemic.

This was particularly true in relation to BI cover where there is a high level of underinsurance. In some cases this is intentional given the cost involved, but mostly we believe it's due to a lack of understanding of the risk exposure and cover.

An increase of 25% in volume and 30% in the average cost of claims.

This can lead to partial or non-payment of claims, which often results in counterproductive tension between the client, their intermediary and insurer.

Specialist insurance is complex by nature and requires deep technical expertise and knowledge to help clients understand and manage their risks. From the perspective of the insurer, the solution to this is twofold: simplified policy wording and better education for both intermediaries and clients around the extent of their cover. Combining these two initiatives will help everyone understand more clearly what is covered, and what is not. That outcome will not only lead to clarity on expectations between the various stakeholders, but provide a solid foundation from which to address areas of underinsurance.

An important part of the education process is a greater emphasis on risk management. Effectively managing risk leads to fewer claims, resulting in more affordable insurance premiums over the long term. This is preferable to reducing cover and risking underinsurance while the probability of a given risk event remains unchanged. Risks are escalating and becoming more complex and it is no longer financially feasible to simply transfer all aspects of risk to an insurer.

The use of technology has amplified exponentially. It was increasing even before the pandemic, but has escalated rapidly since the pandemic began dictating how we live and do business. This rapid increase in technology has, however, introduced another risk that is not featuring high enough on the list of threats: cyber crime.

While 45% of commercial intermediaries surveyed identified cyber crime as a key emerging risk, only 36% of commercial entities agreed – this number remained unchanged from our 2019 survey despite a significantly larger sample size. This goes some way towards explaining why we have not seen the proportionate rise in demand for cyber insurance cover, even as the growth in both working from home and digital communication materially increase cyber crime risk.

Although the seriousness of this risk is gaining momentum among intermediaries, businesses are not yet as concerned as they should be.

This is an important finding from the research and one which we need to act on. It brings us back to the point that there is more work to be done in terms of educating intermediaries and clients – as insurers we need to provide the right tools and enable intermediaries, who in turn will share this knowledge and understanding with their clients.

Broadly speaking, it is not only the weight of the relevant risks that must be communicated, but also what can be done to better manage those risks. Corporate and commercial entities indicated that they will be focusing on sustainability and laying the groundwork for rebuilding in the year ahead. Better engagement with their insurers and intermediaries to understand their cover and to explore how they can improve their risk management practices should form part of that rebuild. Stakeholders are therefore likely to demand that insurance solutions go beyond traditional risk transfer to explicitly address risk mitigation.

We believe that rebuilding the economy will bring with it opportunities for growth in the specialist markets. Some of this will come through market consolidation or insurers exiting lines that have become unprofitable for them. Other growth opportunities will materialise from the development of new classes of insurance to address emerging risks like those associated with cyber security and drones, which will be especially helpful for the growth of the aviation and liability lines. There is also demand for contingency BI cover which will provide further impetus to the industry's growth.

As complex new risks emerge, we must continue to innovate and be prepared to underwrite the risks that threaten our businesses and economic vitality in order to remain relevant.

The risk landscape is evolving rapidly. We see new correlations, interdependencies and causations; risk no longer presents in traditional ways. There is a plethora of new risks, and as specialist insurers we must adapt to this dynamic. We believe each time there is disruption in the market, underwriting discipline is key to who survives. Overall, we see the specialist market as robust going into the rest of 2021 and into 2022.

09 AGRICULTURE CROP

When you combine the challenges of farming and the complexity of crop insurance, it is perhaps not surprising that affordability is a major factor; the reality is that it often leads to farmers not taking out insurance and the perpetuation of the risk protection gap.

PARTNERSHIPS ARE CRUCIAL FOR SUSTAINABILITY IN CROP INSURANCE

Gerhard Diedericks
Head: Agriculture Crop

Farming in South Africa is not an easy business. Some classify it wryly as a 'calling' rather than a way to earn a living. As evidence of the many challenges that farmers are faced with, consider that in the 1970/80s there were about 150 000 farmers tilling our soil; today that number sits at roughly 35 000.

Most farmers use their land as collateral to secure funding for the infrastructure and equipment necessary to sow, irrigate, harvest, store, and package their produce. Uncertainty around land ownership in South Africa reduces both their access to finance, and their willingness to invest. This sentiment is supported by findings in the Santam Insurance Barometer in which 50% of commercial intermediaries rank political unrest as their number one concern.

Corporate and commercial entities identified the challenging economy as the number one risk. In particular, it is impacting the smaller, emerging farmers, many of who do not own the land they plough and are therefore unable to access finance and scale their operations. Further downstream, implications of the risk posed by low economic growth has been demonstrated by the financial difficulties experienced by the Land Bank, which has reduced the agricultural sector's access to capital.

The sporadic reliability of electricity and water supply is also problematic, and there is no guarantee around personal safety either.

However, the biggest challenge that farmers face is weather-related crop risks. Farmers must deal with the threat of hail, flood, frost, and drought each season. In addition, climate change is causing structural shifts in weather patterns, forcing farmers to relocate some crops to better suited geographies, or be left to perish. Finally, while the COVID-19 pandemic did not negatively impact crop production, there was a significant impact on the agricultural sector value chain. Furthermore, managing farm workforces in the context of lockdown restrictions and regulations increased the administrative burden and pressure on maintaining productivity levels on many farms.

To be a successful farmer is to have the stomach to manage change and uncertainty. However, crop risk is the one threat that can be mitigated by using insurance and certain risk management practices.

Much like the underlying commodities being farmed, crop insurance has a seasonal element to it that makes it unique in the realm of general insurance. As the planting season approaches, premiums are collected from farmers that want cover. The insurer then takes on the risk exposure until the crops are harvested, often amid challenges including various premium payment options and with losses occurring before premiums are due. Managing this financial flow between premiums and claims requires deep technical expertise and a relationship with all stakeholders to ensure fair premiums and accurate claims assessment.

The primary challenge for the crop insurer is to diversify the risk so that they can provide comprehensive and cost-effective cover. As an example, if we were to insure all the livestock in South Africa against severe cold, the premium would be much lower compared to a scenario where only a small number of farmers insure their livestock in the extra cold parts of the country where the mercury often dips well below zero, in which case the cost would be much higher. Effectively diversifying crop risk requires an intricate understanding of how each commodity will perform across the different regions given the prevailing weather conditions – there are many variables to account for.

There have been few out-of-the-ordinary crop losses over the past 18 months compared to previous seasons. On the positive side, we saw a substantial decline in hail-related claims and a very low occurrence of drought claims over the past couple of harvest seasons.

When you combine the challenges of farming and the complexity of crop insurance, it is perhaps not surprising that affordability is a major factor; the reality is that it often leads to farmers not taking out insurance and the perpetuation of the risk protection gap.

However, a very important principle for farmers to consider is that the cost ratio of insurance will reduce if their participation in the insurance pool is over longer periods rather than buying insurance only in years when potential losses are expected. The data we have suggests that 50% of the total crops in South Africa are uninsured in any given year.

There are, however, some farmers that choose to self-insure by building up reserves during the good years, so the 50% of uninsured crops is not an accurate reflection of the crops without any protection at all.

50% of total crops in South Africa are uninsured.

Typically, it is the larger farming operations that take this route as they can diversify their risk, to some extent, across commodities and geographies. Farmers have a good understanding of their risks and some might have a strong enough balance sheet to absorb the risk of a lost crop. Due to this unique situation, farmers expect fit-for-purpose insurance solutions to match their specific needs from insurers.

Farmers expect fit-for-purpose insurance solutions to match their specific needs from insurers.

However, we believe the insurers and intermediaries that offer crop insurance have the tools, resources, and skills necessary to add value to the client no matter their size or level of sophistication. For this to manifest in a greater proportion of insured crops, and legacy thinking and practices that are no longer suited to the current demands that farmers face need to be replaced by stronger partnerships and more flexible crop cover.

A good starting point would be to acknowledge the need for two different value propositions.

Mega-farmers will naturally have more complex operations that require bespoke crop insurance solutions. To provide the tailored cover they need, insurers and intermediaries must increase and improve their client engagement efforts. In addition to their ongoing site visits, they should endeavour to make use of the digital communication tools that many of their clients are now comfortable using due to the pandemic. More frequent, higher-quality engagement will create the partnerships needed to build custom-made solutions.

The temptation for every farmer is to take out crop insurance only when they expect adverse weather conditions. Arguably the most important role of the intermediary and insurer providing such cover is to demonstrate to their clients that paying premiums consistently turns out to be more cost effective and less risky than paying them once off. This also helps to ensure sustained capacity by insurers. Again, improved communication can help drive home this critical message.

For smaller farming operations that are perhaps more price sensitive, technology needs to be leveraged to reduce the amount of human intervention needed to provide cover, thereby lowering the cost of insurance. Giving clients the ability to source quotes online, as well as to implement and manage their cover by themselves, is something worth exploring. Done right, the lower premiums in this segment will drive an increased number of premiums written.

Product innovation can also help improve crop insurance inclusivity. With the government's approval, Santam is currently working on an indexed, soil moisture insurance product. It will pay out as and when soil moisture drops below a certain level, an innovation that will make emerging farmers more resilient and give them easier access to capital.

The need for such partnerships is echoed in our research, which found that six in 10 intermediaries believe that PPPs are essential to the future sustainability of the insurance industry in the face of systemic risk.

Segmenting the crop insurance market and providing differentiated levels of service suited to each cohort should result in a greater number of mutually beneficial business relationships between insurer, intermediary, and their agricultural clients.

> To position crop insurance as a product that every farmer could benefit from, the cost involved needs to be more closely aligned with the client risk profile as well as the services offered by the intermediary and insurer.

Insurers and intermediaries should therefore work together to see how they can keep the total distribution cost for risk solutions as cost effective as possible for farmers.

It is vitally important to stress that the responsibility to bring about these changes lies with both the insurer and intermediary. They will need to collaborate effectively, as partners, if the industry is to transition to one that offers more client-centric crop insurance solutions at an attractive price for farmers both in the large corporate segment as well as in the emerging/small holders segment to ensure that access to financial markets and long-term wealth creation is sustained.

Paying premiums consistently turns out to be more cost effective and less risky than paying them once off. This also helps to ensure sustained capacity by insurers.

Santam is currently working on an indexed, soil moisture insurance product. It will pay out as and when soil moisture drops below a certain level, an innovation that will make emerging farmers more resilient and give them easier access to capital.

10
CONCLUSION

It is clear from the survey results and from the insights in this report that the past 18 months have presented both challenges and opportunities for the insurance industry.

JOINING FORCES TO REBUILD THE ECONOMY

Quinten Matthew
Executive head Specialist Business

We have not only dealt with increasingly devastating waves of COVID-19 and subsequent economic lockdowns over this period but, more recently, widespread public discord and unrest that has resulted in serious damage to property and most tragically, loss of lives. Businesses have once again had to close in the wake of violence and looting causing further business interruption. At the same time many are still battling to emerge from the challenges associated with the pandemic lockdowns. In addition, the extensive damage to infrastructure, manufacturing plants and businesses is putting further strain on our already struggling economy and further delaying economic recovery. What is concerning from an insurance perspective is that this prolonged destruction could have long-term implications on the cost of insurance.

The pandemic has obviously also severely impacted businesses in almost every sector. More than 6 in 10 intermediaries reported adverse impacts on profits as a result of the pandemic, while 80% of commercial, corporate and consumer respondents described the pandemic as having had a negative impact on their business or personal finances. Our research suggests that it may take more than three years for the industry to recover economically. During this time we expect to see a degree of consolidation, particularly among intermediaries.

That said, at the time of our survey industry players were optimistic about the market outlook notwithstanding recent events. The majority withstood a one-in-200-year event and are still standing, albeit some more sturdily than others. As a group, insurers have risen to the challenge presented by the volume and significant rise in cost of claims resulting from the pandemic. But there are opportunities that should not be overlooked.

> One of the positives of the pandemic-induced upheaval has been that we have learned to think in new and innovative ways.

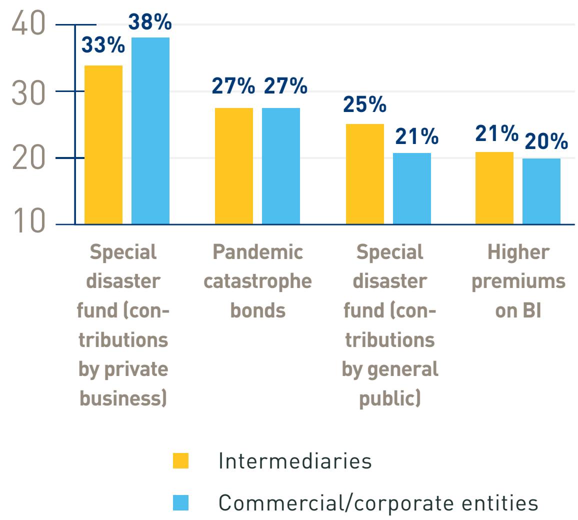
The considerable investment in technology and accelerated shift towards the digital age brought on by the pandemic is something insurers need to capitalise on. It is enabling insurers and their intermediaries to build new distribution channels and gain access to new markets.

With more South Africans technologically connected, there is more opportunity for the industry to reach those who currently do not insure or are underinsured, thereby providing greater support to broader society.

For the most part, we have been seen as supportive during the pandemic. Intermediaries are now more likely to recommend Santam based on our response to the pandemic. While this is encouraging, we acknowledge that trust needs to be rebuilt in the particularly hard-hit construction and hospitality sectors where respondents did not feel as supported by insurers as businesses in some other sectors.

Views are mixed on how the industry should respond to pandemic risk in the future. The most popular choice was the provision of a special disaster fund that either private business contribute to (33% of intermediaries, 38% of commercial/corporate entities) or that the general public contributes to (25% of intermediaries, 21% of commercial/corporate entities). This was followed by the issuance of pandemic catastrophe bonds (27% of both sets of respondents) and higher insurance premiums on BI policies (21% and 20% of intermediaries and corporate/commercial clients, respectively).

Views on how the insurance industry should respond to pandemic risk in the future



For our part, we believe risk management has to be central to dealing with future risk, be it pandemic-related or not. We wrote in our last report that the industry has to shift the collective mindset from one of risk transference to one of holistic risk management. This is still true today, possibly even more so in a post-pandemic world. We want to see the industry move from repairing and reimbursing after a loss to more investment in risk preparedness, so that insurers can add value every step of the way, especially in terms of risk prevention, rather than only adding value once a loss has been incurred. This is essential if we want to ensure the future sustainability of a strong local insurance sector that is able to continue to provide support to our state-owned insurer SASRIA, that has been hard hit by the current unrest in South Africa.

The pandemic has also shone a light on just how crucial it is to focus attention further afield than on physical loss alone. Climate-related risks such as floods and fire are still highly relevant but as the pandemic has shown, unexpected events can cause unforeseen business interruption that has nothing to do with physical damage to property, and these can have far-reaching consequences. Insurance plays a critical role in protecting and building resilience in order to recover from such economically devastating events.

While new BI products will be brought to market in response to the pandemic, these are likely to be very specifically worded and finite in terms of their application so as to avoid any ambiguity. Cover will likely be limited to core costs such as rent, utilities and staff and will be there to tide businesses over, to get them through the pandemic rather than covering the total loss of income.

While these undoubtedly have their place, insurers can not shoulder this burden alone. Protecting against something as monumental as a global catastrophe would render insurance unaffordable which would defeat the objective. Rather, industry stakeholders need to come together to work as strategic partners and share responsibility for better risk management practices that encompass a wider range of preventative behaviours. These will include relevant insurance products, robust business continuity plans and effective disaster recovery.

> At the centre of this evolutionary point we find ourselves in is the intermediary, who must act in the role of a trusted risk adviser to help navigate this new path. It is through the invaluable relationships that intermediaries have fostered with both client and insurer that better risk management can transpire.

Intermediaries must now play a bigger role in this system and insurers must enable them through accelerated, fit-for-purpose training. At the end of the day, the onus is on insurers to ensure their products are easily understood by both the intermediary and end client.

Another critical stakeholder in the risk management process is government. While we applaud the leadership government has shown throughout the pandemic, we recognise that it is a big job to get the economy kick-started again. What was an undercurrent of social disquiet threatening the country's ability to get back up on its feet, has now erupted into full-scale violent and destructive looting and protests in KwaZulu-Natal and parts of Gauteng that is pushing the country into further economic distress.

As an industry, we need to be asking how can we support government as it tackles this social change, and what role we can play in building better social cohesion. After all, insurance is the very DNA of capitalism, and synchronised collaboration is what will really drive a more sustainable, equitable future for the industry as well as the broader economy.

Ultimately, at Santam, we view risk and opportunity for innovation as two sides of the same coin. To ensure we make the conversion from risk to opportunity, all stakeholders must play an active part and collaborate more closely.

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