Strategic and emerging issues in South African insurance 2012
Assessing the future trends for insurers

Ilse French
PwC Short-term Insurance Leader – Southern Africa

14 September 2012
Setting the scene

Strategic and Emerging Issues in South African Insurance 2012

• Fifth biennial PwC Strategic and Emerging Issues
• Independent research/interviews of 29 CEOs across industry
• The key objectives of the survey are to:
  - Raise awareness of emerging issues and trends in the insurance industry;
  - Understand the views of industry CEOs about these issues;
  - Insight into how the industry may evolve over the next few years; and
  - Assist CEOs to shape their own future
• Main findings consistent with PwC Global research/CEO surveys/Project Blue
• What is the future of South African short-term insurance?
Setting the scene

Project Blue: Assessing the future trends for financial services

• Main purpose of “Project Blue” is to help insurers to:
  - Move focus away from short-term reactive adaptations
  - Recognize the unfolding megatrends that will shape the future of insurance
  - Develop appropriate longer term strategies and competitive advantage
• Backed by extensive documented research
• What should be on the CEO agenda?

• Linking the SA survey findings to Project Blue
## The participants

<table>
<thead>
<tr>
<th><strong>Short-term insurers</strong></th>
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</thead>
<tbody>
<tr>
<td>Absa Insurance</td>
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<tr>
<td>Alexander Forbes Insurance</td>
</tr>
<tr>
<td>Chartis</td>
</tr>
<tr>
<td>Hollard Insurance</td>
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<td>Lion of Africa</td>
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<tr>
<td>Mutual &amp; Federal</td>
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<td>Outsurance</td>
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<tr>
<th><strong>Long-term insurers</strong></th>
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<td>Absa Life</td>
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<td>Clientele Life</td>
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<td>Discovery Life</td>
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<td>Hollard Life</td>
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<table>
<thead>
<tr>
<th><strong>Reinsurers</strong></th>
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<tbody>
<tr>
<td>Hannover Re</td>
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<tr>
<td>Munch Re</td>
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<tr>
<td>Swiss Re</td>
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</tbody>
</table>
**Major strengths and weaknesses**

**Strengths**
- Ability to innovate;
- Well capitalised with good penetration;
- Strong balance sheets;
- Focus on risk management; and
- Strong brands.

**Weaknesses**
- The power base of brokers;
- Poor performance on consumer education;
- Motor premiums are expensive, resulting in lower interest in coverage;
- Too much competition in the short-term industry based on price; and
- Inability of intermediaries to reach all segments of the market.
# Market environment

## Short-term companies

<table>
<thead>
<tr>
<th></th>
<th>2012</th>
<th>2015</th>
<th>Change</th>
<th>% Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>Branches in South Africa</td>
<td>179</td>
<td>162</td>
<td>(17)</td>
<td>(9.5)</td>
</tr>
<tr>
<td>Brokers/Intermediaries</td>
<td>15 847</td>
<td>14 408</td>
<td>(1 439)</td>
<td>(9.1)</td>
</tr>
<tr>
<td>Full-time employees in SA</td>
<td>15 991</td>
<td>17 353</td>
<td>1 362</td>
<td>9.0</td>
</tr>
<tr>
<td>Policyholders (millions)</td>
<td>9.6</td>
<td>12.7</td>
<td>3.1</td>
<td>32.3</td>
</tr>
</tbody>
</table>

## Long-term companies

<table>
<thead>
<tr>
<th></th>
<th>2012</th>
<th>2015</th>
<th>Change</th>
<th>% Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>Branches in South Africa</td>
<td>1 514</td>
<td>1 562</td>
<td>48</td>
<td>3.2</td>
</tr>
<tr>
<td>Brokers/Intermediaries</td>
<td>37 840</td>
<td>51 540</td>
<td>13 700</td>
<td>36.2</td>
</tr>
<tr>
<td>Full-time employees in SA</td>
<td>57 667</td>
<td>61 600</td>
<td>3 933</td>
<td>6.8</td>
</tr>
<tr>
<td>Policyholders (millions)</td>
<td>22.2</td>
<td>28.6</td>
<td>6.4</td>
<td>28.8</td>
</tr>
</tbody>
</table>
Market is changing and opportunities exist for those who see it

Key drivers of change

Social

Economic

Technology

Environmental

Political

Do we adapt or change?
Social

“The problem is not whether business will survive in competition with business, but whether any business will survive at all in the face of social change”

Laurence Joseph McGinley, President of Fordham University
Implications of social and behavioural change

• Balance of power is shifting towards customer
• Distribution dominance to distribution destruction
• Demographic change
• Social and online networks, affinity groups etc. are growing in their ability to influence decision making
Social and behavioural change a major driver of change in SA insurance industry

- TCF – biggest of all new regulations especially for larger organisation
- Power base of brokers
- Move away from ‘blanket’ insurance cover
- More unbundling of products
- Not enough products in middle class market

Source: PwC Strategic and Emerging Issues in South African Insurance 2012
South African perspective on social and behavioural change

Top distribution challenges

- Improving distribution productivity
- Aligning customer, company and salespersons interests
- Effectively using technology to create distinctive value with customers or producers
- Aligning compensation programs with desired behavior and performance
- Recruiting, training and retaining salespeople
- Broker education requirements
- Ageing broker networks
- Breakdown in consumer trust of intermediaries

Source: PwC Strategic and Emerging Issues in South African Insurance 2012
South African perspective on social and behavioural change

Joint ventures and partnerships will be key to South African insurers’ expansion plans

19 insurers will engage in joint ventures or partnerships

Source: PwC Strategic and Emerging Issues in South African Insurance 2012
Technology

“Innovation distinguishes between a leader and a follower”

Steve Jobs, co-founder of Apple
Implications of technological change

- Loyalty replaced by price comparison
- Mobile technology
- Who is your competitor?
- Specialist underwriting linked to ‘big data’
Implications of technological change

The type of data that we can exploit has progressively moved from structured to semi-structured to unstructured data.
South African perspective on technological change

- Move to mobile (smartphones & tablets)
- Self service for commodity products
- Major change expected towards 2020

Institutions representing the most significant competitive threat to South African insurers

- Established broad-based financial institutions already competing in your market
- Established broad-based financial institutions moving from one market to another
- Niche players
- New competitors moving from retailing into financial services
- Foreign insurers entering the market
- Start-up institutions
- Other

Source: PwC Strategic and Emerging Issues in South African Insurance 2012
Top applications of technology in insurance by 2015

- Direct insurance / online distribution
- Real-time data mining capabilities
- Actuarial systems
- Smart systems to proactively manage risk
- Systems to deliver IFRS and regulatory compliance information
- Linkages between insurance and call centre systems
- Claims modeling
- Other

Source: PwC Strategic and Emerging Issues in South African Insurance 2012
Areas SA insurers experience the greatest shortage of skills in:

- Specialist underwriting
- Actuarial
- Non-executive directors
- Audit committee
- Capital management
- Risk management
- Information technology (IT)
- Executive directors
- Compliance
- Financial reporting
- Internal audit
- Administration

Source: PwC Strategic and Emerging Issues in South African Insurance 2012
Environmental

“Nature provides a free lunch but only if we control our appetites”

William Ruckelshaus, Business Week, June 1990
Implications of environmental change

- Government policy
- Uninsurable risks
- Mitigation through behaviour and sustainable solutions
- Catastrophe events and modelling
Economic
Implications of economic change

- Urbanisation

World population (urban and rural) from 2000 to 2040, 2009 figures

Forecast

Source: United Nations, Department of Economic and Social Affairs, Population Division (2009 Revision)
Implications of economic change

• Trade flows between SAAME territories

- Trade value: $6.92tr
  CAGR 2002–10: 8.0%

- Trade value: $2.16tr
  CAGR 2002–10: 12.9%

- Trade value: $2.67tr
  CAGR 2002–10: 13.6%

- Trade value: $2.82tr
  CAGR 2002–10: 19.4%

Sources: WTO; PwC analysis

* Compound Annual Growth Rate (CAGR)
South African perspective on economic change

- Africa focus
- South America down from 8 – 3 in 2012
- Low penetration rates
- Margins / profitability

### Non-life premiums as % of GDP in 2010

<table>
<thead>
<tr>
<th>Region</th>
<th>% of GDP</th>
</tr>
</thead>
<tbody>
<tr>
<td>South Africa</td>
<td>2.8%</td>
</tr>
<tr>
<td>Namibia</td>
<td>2.3%</td>
</tr>
<tr>
<td>Kenya</td>
<td>0.19%</td>
</tr>
<tr>
<td>Nigeria</td>
<td>0.4%</td>
</tr>
</tbody>
</table>

Source: Swiss Re

Source: PwC Strategic and Emerging Issues in South African Insurance 2012
South Africa perspective on economical change

Challenges investing in the rest of Africa

- Regulatory restrictions
- Cultural issues/conflicts
- Lack of insurance skills

Score

Source: PwC Strategic and Emerging Issues in South African Insurance 2012
South African perspective on economic change

- Micro insurance opportunities
- Market competition
## Market competition

### Alternative risk transfer (ART)

<table>
<thead>
<tr>
<th>Competition level</th>
<th>Competitive response</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>No change</td>
</tr>
<tr>
<td>Intensive</td>
<td>8.3%</td>
</tr>
<tr>
<td>Moderate</td>
<td>16.7%</td>
</tr>
<tr>
<td>Light</td>
<td>16.7%</td>
</tr>
<tr>
<td>None</td>
<td></td>
</tr>
</tbody>
</table>

Source: PwC Strategic and Emerging Issues in South African Insurance 2012
## Market competition

**Property (excluding motor)**

<table>
<thead>
<tr>
<th>Competition level</th>
<th>No change</th>
<th>Minor change</th>
<th>Significant operational and organisational change</th>
<th>Fundamental change in strategy and positioning</th>
</tr>
</thead>
<tbody>
<tr>
<td>Intensive</td>
<td>11.1%</td>
<td>22.2%</td>
<td>11.1%</td>
<td>16.7%</td>
</tr>
<tr>
<td>Moderate</td>
<td>22.2%</td>
<td>5.6%</td>
<td>11.1%</td>
<td></td>
</tr>
<tr>
<td>Light</td>
<td></td>
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<tr>
<td>None</td>
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<td></td>
</tr>
</tbody>
</table>

Source: PwC Strategic and Emerging Issues in South African Insurance 2012
### Market competition

#### Motor insurance

<table>
<thead>
<tr>
<th>Competition level</th>
<th>No change</th>
<th>Minor change</th>
<th>Significant operational and organisational change</th>
<th>Fundamental change in strategy and positioning</th>
</tr>
</thead>
<tbody>
<tr>
<td>Intensive</td>
<td>21.1%</td>
<td>15.8%</td>
<td>31.5%</td>
<td>26.3%</td>
</tr>
<tr>
<td>Moderate</td>
<td>5.3%</td>
<td></td>
<td></td>
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<tr>
<td>Light</td>
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<td>None</td>
<td></td>
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<td></td>
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Source: PwC Strategic and Emerging Issues in South African Insurance 2012
Political

“The rise of state capitalism - the emerging world’s new model?”

The Economist, January 2012
Implications of political reform

- Do we adopt or can we change?
- Will the regulator succeed at global insurance regulations?
- Resource scarcity driving geopolitical instability
- Government wrestles with implications of demographic change
- Rise of state-directed capitalism
South African perspective on political reform

Impact of recent regulatory developments

• National Health Insurance
  - Will impact disposable income and insurance spend
  - Greatest impact bottom of the market
  - Public/private partnership

• Micro-insurance
  - Strong interest in new entities
  - Formalise the sector

• Treating Customers Fairly
  - Major impact – company wide
  - Culture shift required – will take time
  - Larger insurers will be challenged
South African perspective on political reform

Impact of recent regulatory developments

• Binder Agreement
  - Major impact – business model under threat
  - Affects white label products
  - Intermediary model will become very expensive
  - Opens opportunities for direct insurers
South African perspective on political reform

• The estimated cost of implementing regulatory developments
  - Short-term insurer estimated implementation of SAM to be more or less **R50 million**
  - Two companies projected costs of around **R100 million**
Other survey findings
Projected growth in revenue – short-term companies

Based on responses from 27 companies

Source: PwC Strategic and Emerging Issues in South African Insurance 2012
South African perspective on reducing operating costs

Cutting costs over the next 3 years

• 13 companies expected to reduce cost by 0 - 5%
• 13 companies by 5 – 10%
• 1 believe it could reduce costs by more than 10%

Source: PwC Strategic and Emerging Issues in South African Insurance 2012
# Peer review

<table>
<thead>
<tr>
<th></th>
<th>First</th>
<th>Second</th>
<th>Third</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Products</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Alternative risk transfer</td>
<td>Guardrisk</td>
<td>Centriq</td>
<td>RMB</td>
</tr>
<tr>
<td>Motor insurance</td>
<td>Outsurance</td>
<td>Santam</td>
<td>Telesure</td>
</tr>
<tr>
<td>Property (excluding motor)</td>
<td>Santam</td>
<td>Mutual &amp; Federal</td>
<td>Hollard</td>
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<tr>
<td><strong>Other</strong></td>
<td></td>
<td></td>
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</tr>
<tr>
<td>Customer relationship management</td>
<td>Discovery</td>
<td>Outsurance</td>
<td>Santam</td>
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<tr>
<td>Innovations</td>
<td>Discovery</td>
<td>Outsurance</td>
<td>Hollard</td>
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<tr>
<td>Marketing strategies</td>
<td>Discovery</td>
<td>Outsurance</td>
<td>Telesure</td>
</tr>
<tr>
<td>Technically competent staff</td>
<td>Santam</td>
<td>Discovery</td>
<td>Old Mutual/ Sanlam</td>
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Source: PwC Strategic and Emerging Issues in South African Insurance 2012
Project Blue framework
Many industry professionals (particularly in the West) are focused on adapting to global instability; however, the market is changing and opportunity exists for those who see it.

<table>
<thead>
<tr>
<th>ADAPT</th>
<th>Global instability</th>
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<tbody>
<tr>
<td>Regulatory environment</td>
<td>Political environment</td>
</tr>
<tr>
<td>Rise and interconnectivity of the emerging markets (SAAAME)</td>
<td>Economic strength</td>
</tr>
<tr>
<td></td>
<td>Trade flows</td>
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<td></td>
<td>‘Global insurers’</td>
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<tr>
<td>Demographic change</td>
<td>Population growth discrepancies</td>
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<td></td>
<td>Ageing populations</td>
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<tr>
<td>Social and behavioural change</td>
<td>Urbanisation</td>
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<td></td>
<td>Consumerism</td>
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<td></td>
<td>Direct interaction</td>
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<td></td>
<td>Loyalty</td>
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<td>Technological change</td>
<td>Disruptive technologies impacting FS</td>
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<td>Digital and mobile</td>
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<td></td>
<td>Loss control</td>
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<tr>
<td>War for natural resources</td>
<td>Oil, gas and fossil fuels</td>
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<td></td>
<td>Food and water</td>
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<tr>
<td></td>
<td>Key commodities</td>
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<tr>
<td>Rise of state-directed capitalism</td>
<td>State intervention</td>
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<td></td>
<td>Country / city economic strategies</td>
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</tbody>
</table>

Source: PwC analysis
PwC is assessing the impact of these changes on all aspects of the leadership agenda

### The CEO agenda

#### Shaping the future:  
*Defining the future market and customer environment*  
*(Play an active role)*  
- Economic rebalancing
- Industry structure
- Investor expectations
- New stakeholders
- Regulation
- Social policy
- Customer expectations

#### Rethinking the strategy:  
*‘Aligning the business model to the new commercial and market reality’*  
*(Adopt fast)*  
- Short-term adaption
- Alignment to global trends
- Managing new stakeholder objectives
- Determining risk appetite
- Redefining performance targets
- Driving competitive advantage

#### Reinventing the organisation:  
*‘Redefining the organisation to derive competitive advantage’*  
*(Respond proactively to changing customer and market demands)*

### Governance
- Board composition and qualifications
- Executive remuneration
- Regulatory compliance
- Risk management
- Financial reporting and controls

### Target operating model
- Legal and physical structure
- Tax and capital efficiency
- Allowable cost structure
- Technology
- Partnership structure
- People and resources

### Competitive advantage
- ‘Seeing the future’
- ‘War of talent’
- ‘Constant reinvention’
- ‘Product innovation’
- Strategic agility
- Operational alignment

Source: PwC analysis