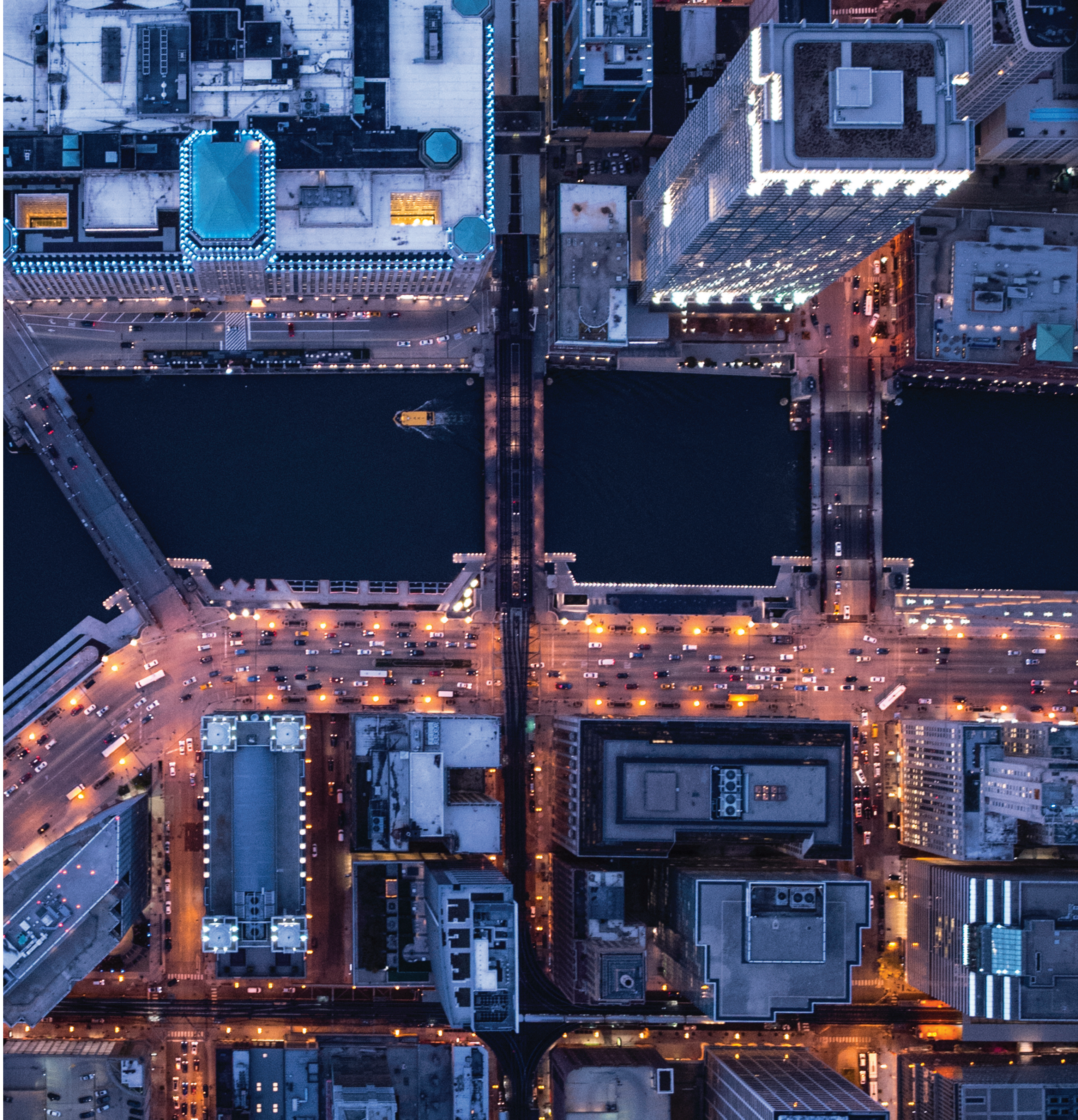
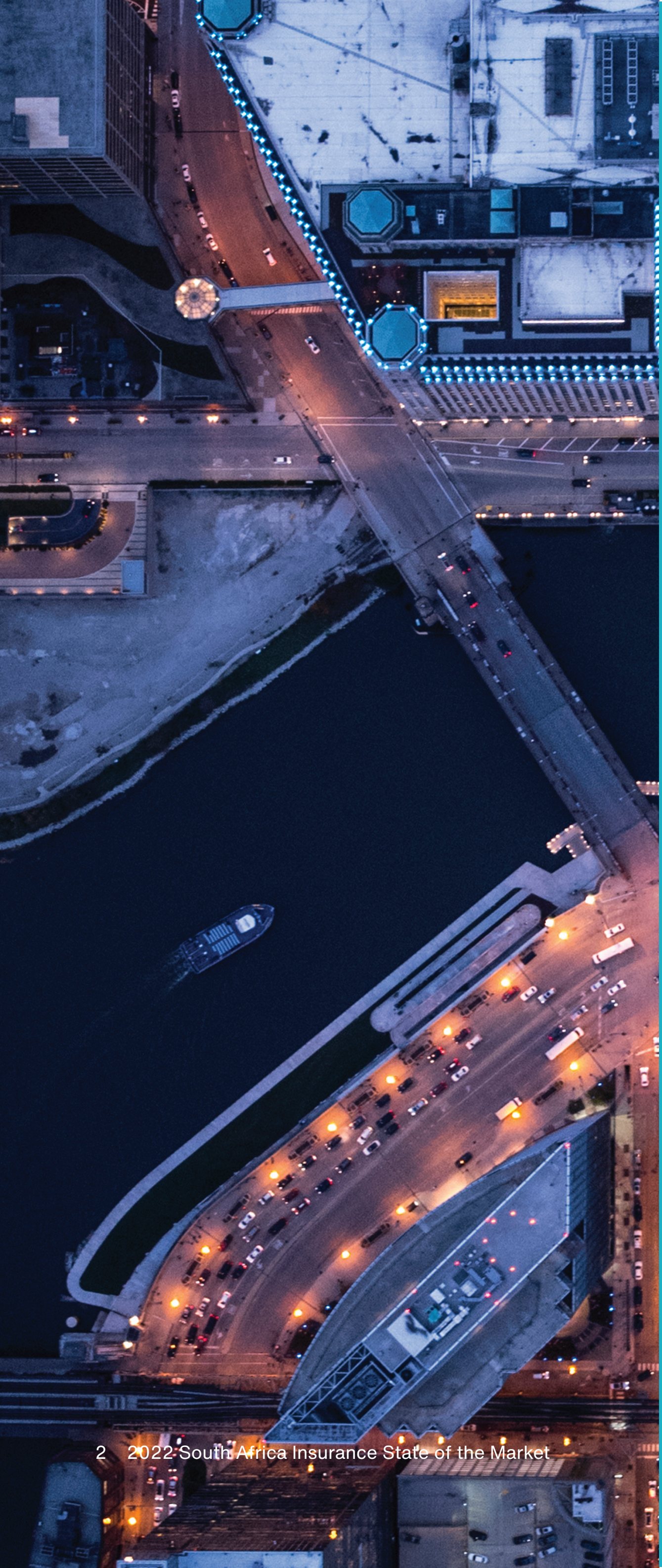
2022 South Africa Insurance State of the Market





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Aon exists to shape decisions for the better — to protect and enrich the lives of people around the world.

Aon is in the Business of Better Decisions.

Report Highlights: Helping you make better decisions

Good Housekeeping

- Start early on the renewal process, explore alternative structures and consider access to new forms of capital.
- As technology improves and ESG starts to dominate boardroom decisions, challenge the point at which you would consider not reinstating an asset,eg. for example. Approach risk management broadly rather than focusing on the renewal of your expiring insurance policies.
- Provide regular updates to Insurers on any claim that is nearing insurance attachment. Reporting delays and failure to report according to contract terms remain two of the top reasons' claims are denied.

Valuations

- Undertake regular replacement valuations, considering the impact of new replacement cost, VAT, inflation and exchange rate fluctuations. These valuations should include the actual cost of rebuilding or replacing any of these items at today's costs including demolition, clearing costs, professional fees and any other improvements to the property insured.

Business Interruption

- On average, 43% of **business interruption insurance** is underinsured by 53%, according to the Chartered Institute of Loss Adjusters (CILA). "One of the reasons for this is that the selected maximum indemnity period turns out to be far shorter than the actual period of disruption caused by accidental property damage. It is worth considering an increase in your maximum indemnity period to reflect the true extent of disruption, including allowing for an increased time for reinstatement.

Cyber Assessments

- A cybersecurity assessment **analyses your organization's cybersecurity controls and their ability to remediate vulnerabilities**. These risk assessments should be conducted within the context of your organisations business objectives, rather than in the form of a checklist as you would for a cybersecurity audit.

Risk Management

- Reduce TCOR beyond the pinch points and bottlenecks you have focused on historically. Explore how risk management practices can be improved to build resilience, focusing on the areas that have the biggest impact.
- Rather than assuming large deductibles on part of your program and small deductibles on other parts, consider consolidating premium and leveraging it to build scale within a captive.
- Review retentions, scope of coverage and sub-limits. Consider alternative sources of capacity, working with Aon to ensure options are fully explored.
- ESG is becoming ever more important for all organisations, including Insurers. Aligning with those that share similar values will ensure a more sustainable relationship, and therefore certainty over time.

Keep us informed

- Even after placement, maintain connectivity with underwriters to reinforce 'out of cycle' relationships across Insurer management levels. Expand relationships to include claims teams to align expectations throughout the claims journey.

South African Insurance Market Overview

Our modern world is unpredictable and volatile. The myriad direct and indirect impacts related to the geopolitical events in Eastern Europe have been profound and are expected to continue as rising commodity prices fuel inflationary pressures, decreased demand dampens global trading and global supply chains suffer further disruptions.

Insurers, looking to manage volatility, have already begun modifying coverage terms and conditions – including those related to cyber, terrorism, sanctions, and war as well as coverage territories. The world is watching anxiously as economic impacts develop, while the risk and insurance industry watches carefully, ready to respond to further impacts on exposures and risk profiles. The economic climate has never been more complex and connected, all while businesses continue to respond to and recover from the aftermath of the challenges posed by the COVID-19 pandemic.

From a South African market perspective, the South African Special Risk Insurance Association (SASRIA SOC Ltd) suffered losses of approximately R33,8 billion due to the unrests in KwaZulu-Natal and Gauteng after businesses were looted and damaged during July 2021. This was followed just a few short months later by devastating floods in KwaZulu-Natal during April 2022 in what is being called the worst natural disaster to hit South Africa according to the South African Insurance Association (SAIA) from a devastation and loss of lives perspective. The result of the floods already exceeds R35bn in losses. Further South, the drought in Gqeberha has reached alarming, crisis proportions. The ongoing drought starting in 2015 affecting the Eastern Cape region of South Africa is one of the worst droughts in the region's history. The drought led the South African government to declare the region a "disaster area" in October 2019. Nelson Mandela Bay Municipality is teetering on the edge of Day Zero where it will run out of water completely.

New challenges and risks continue to emerge from climate change and environmental, social and governance (ESG) pressures, talent, and worker shortages, struggling economies and political unrest, to name a few. Financial losses from large-scale natural disasters and man-made events continue to loom and are adversely impacting lives and businesses.

Key Global Insurance Market Trends in 2022

The market moderation that began in late 2021 continued in H1, especially for products and risk types targeted for insurer profitable growth. Underwriting rigor continued to increase in H1, as insurers remained focused on reducing volatility through best-in-class risk selection. There is generally a deceleration of rate increases, and in some cases stabilisation, however insurers remain focused on profitability.

With risks related to cyber, communicable disease, contingent (non-damage) business interruption, climate change and other factors becoming more volatile, appetite is shifting, coverage terms are being clarified and attachment points are increasing.

Following a volatile two-to three years and with more volatility on the horizon, many reinsurers and insurers are reassessing the risks they are prepared to take on as well as the terms and conditions of providing such cover. The importance of the provision of comprehensive underwriting information including risk mitigation strategies, continues to grow in importance.

Property Insurance

The adequacy of sums insured is increasingly becoming a focus for underwriters, who now often require a valuation for insurance purposes to substantiate the sum insured. This is largely due to significant increases in the cost of building materials in addition to shortages and delays linked to supply chain issues and inflationary pressures. Weather-related catastrophe, notably flood risk, is increasingly a focus for underwriters.

E&O and Cyber Market Trends

- The cyber landscape remained volatile in the first quarter. Complex cyber losses continued to develop with multiple severity cases compounding on large events that occurred in recent years, while the frequency of claims remained relatively constant year-on-year.
- Waiting periods for business interruption related coverage such as systems failure business interruption and dependent business interruption increased. Ransomware co-insurance provisions, ransomware sub-limits, and sub-limits for business interruption, systems failure business interruption, and dependent business interruption were introduced in certain client and industry segments, or when risk controls were deemed insufficient by insurers.
- Insurers scrutinised the coverage offered for critical infrastructure, systemic, correlated events, and restricted coverage on either a generalised or event specific (eg.Log4j) basis. Insurers actively managed their global aggregate capacity, and, in some cases, reduced limits offered. The underwriting process continued to gain rigor.
- Over the past two years, cyber risks have evolved across many fronts. Threat actors are using new, strategic tactics every day. The attack surface has expanded as employees continue to work from home, and supply chain-related attacks perpetuate growing systemic risk concerns. It is no surprise that in Aon's 2021 Global Risk Management Survey, participants around the globe rated the risk of cyber-attacks or data breaches as the number one threat facing companies today.
- The sheer number of cyber-attacks on corporations have increased dramatically over the past few years. For example, **ransomware attacks grew significantly— up 323 percent from H1 2019 to Q4 2021**. Meanwhile, we saw an average of two new Errors and Omissions (E&O) and cyber matters per day in 2021.

As we emerge from the pandemic, the hope is that the worst is behind us, but insurers are still in recovery mode. The E&O and cyber marketplace should brace itself for potential further challenges during the remainder of 2022.

Looking back, 2021 became progressively more difficult for clients, brokers, and underwriters. Clients continued to see dramatic pricing increases, particularly in the second half of 2021 - and in many instances, pricing adjustments were additive to striking increases in retention levels, reductions in capacity available and the introduction of coverage changes that were new or restrictive in nature.

E&O or cyber insurance placements often required an underwriting process that was far more invasive than previous years. The combination of passing a more demanding underwriting test, only to experience an unfavourable outcome, was a challenging message for organisations.

While the marketplace remains tough, we anticipate pricing pressure will be less severe than 2021, particularly for placements in the second half of 2022. Clients may experience more comfort as insurer underwriting strategies become clearer, and they gain greater perspective regarding the challenges faced to secure E&O and cyber coverage.

Organisations now recognise the criticality of timing, with a focus on starting the placement process early. They are generally more prepared, collaborating internally to gather and present strategies around contractual risk management, network security, privacy, and operational continuity to the insurance market. As difficult market conditions continue to prevail, Aon remains focused on timing, process, and innovation as we support and advocate for our clients.

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Aon expects the following core themes in the global E&O and cyber market for the remainder of 2022:

- **Climbing Rate Environment**
  While the majority carriers implemented significant rate increases during the first half of 2022, comparable to the second half of 2021, we anticipate potential stabilisation in the second half of 2022.

- **Increased Underwriting Rigor**
  Like 2021, we anticipate all insurers offering cyber and E&O insurance to continue to bring new scrutiny, applications, and underwriting questions into the placement process. In addition to the ongoing evaluation of "standard" security control questions, insurers will continue to focus on "real time" issues related to new attack methods or emerging tactics and threat actors' leverage to exploit emerging vulnerabilities. A recent market survey showed all carriers list a lack of multi-factor authentication, endpoint detection and response measures, and backups as criteria for declination.

- **Aggregation Risk**
  Throughout 2021, many insurers focused on capacity deployment on a risk-by-risk basis. The economic benefit of reducing exposed limit across a portfolio while obtaining more premium per million in limit deployed can quickly solve profitability issues for many insurers. As 2022 develops, we anticipate many insurers will shift focus to systemic and correlated risk concerns and their impact on the insurer. Supply chain attack strategies and geopolitical tensions, paired with the reliance many companies have on common technology service providers, will likely drive a focus on war exclusions and infrastructure language in cyber policies.

- **Client Segment Differentiation**
  Insurers continue to face challenges in specific industry verticals, particularly public sector, healthcare, manufacturing, and higher education, and across small to mid-sized companies. Industries with decentralised security strategies, and those that tend to have heavy merger and acquisition growth strategies, continue to show increased loss activity compared to other industries. Consistently aligning security controls can be difficult for companies in these verticals. When looking at differentiation across company size, many fast-growth companies are still developing strategies and determining resourcing for network security, privacy, and contractual risk management. Smaller organisations may experience more rigid positions from underwriters with respect to specific security controls perceived to be critical when protecting against certain attack methods. Retention and pricing challenges will likely be ongoing for these organisations as they seek to secure and expand their E&O and cyber coverage.

- Our goal is to share loss and pricing trends to date, feedback from insurers, and – most importantly – key recommendations for clients to consider as we navigate a challenging E&O and cyber market. While we still expect the marketplace to be tough, we anticipate pricing pressure will be less severe than 2021, particularly for placements in the second half of 2022.

Key South African Insurance Market Trends in 2022

Reduced cover and increased rates

Sasria – increased rates and withdrawal from the Excess of Loss market

Sasria advised in October 2021 following the losses resulting from the political unrest that they have undertaken a review of all Sasria rates which has resulted in structural rating changes and rate increases to certain classes of business. The rate increases became effective 1 January 2022 for new business and will be applicable for existing policies on renewal or anniversary of the policy. Sasria SOC Ltd further announced in March 2022 that they will no longer offer cover for Excess of Loss (XOL) due to the challenges of securing reinsurance partners with the appetite to continue with this facility.

Knock on effect on the Property Terrorism and Sabotage market – both locally and in the UK

Violent events in South Africa have resulted in a significant number of claims in the Political Violence (PV) space with reports estimating a figure around US$1 billion. As a result, the PV market has been inundated with requests and enquiries, which in turn has resulted in the increase in the utilisation of finite aggregates, and this again has caused rates to increase dramatically, in some instances up to a 500 - 600% as capacity becomes limited.

Reduction of cover - Business Interruption - Removal of non-physical damages extensions

The COVID-19 pandemic has highlighted the need for insurers and re-insurers to re-evaluate their risk exposures to large-scale events, particularly with regard to BI cover and non-physical damages extensions. As a result, reinsurers and insurers have advised that they will no longer provide capacity for any non-material damage-related incidents on Business Interruption insurance covers.

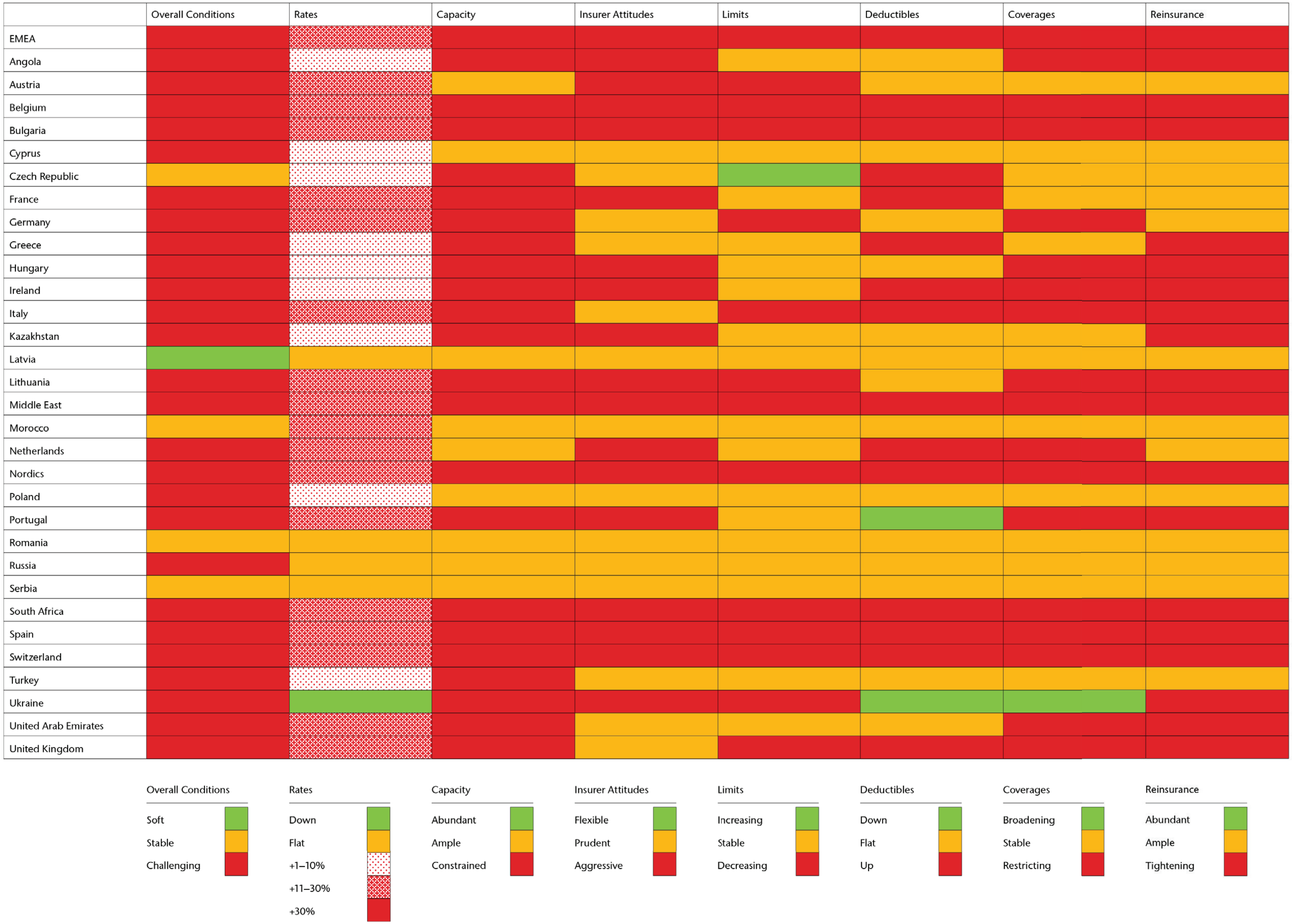
Reduction in cover – weather related losses

On the back of weather-related losses both locally and internationally, insurers are starting to pay careful attention to weather-related risks - particularly flood risks - on property portfolios. This is driving premium rating and affecting deductible levels in relation to these risks. In some instances, cover is being sub-limited for weather-related claims

Material Shortages – Sum Insured Adequacy

Material shortages are being experienced across the construction industry with no reassurances from suppliers/manufacturers of when things will improve. Shortages are impacting estimated delivery dates for core materials with lengthy delays. This continued pressure is increasing material costs, and significant delays are greatly impacting clients' commercial asset and business interruption values. In the last 12 months, material damage sum insured values have increased approximately 10–20% due to increasing replacement cost estimates and a reforecasting of inflationary provisions.

Insurance Market Heat Map



Market Dynamics Summary

Pricing:

Rate increases continued in H1 but have decelerated across large portions of the market, becoming generally modest, with the key exceptions of cyber as well as higher-risk sectors and risks with adverse claims experience.

Limits:

Limits have stabilised as portfolio mandates have become less prevalent. Adjustments were made in H1 on a case-by-case basis.

Retentions:

Retentions/deductibles have broadly stabilised, although increases applied in H1 to trending loss areas and poor performing risks. In addition, minimum deductibles have been applied to designated business sectors. Insureds continue to explore deductible options to help offset premium costs.

Coverage:

Coverages have broadly stabilised, except in targeted areas including Sasria, cyber, terrorism, war, and sanctions (particularly those relating to Ukraine, Russia, and Belarus).

Capacity:

Capacity has expanded in some areas targeted for insurer growth and stabilised across most lines with the key exceptions of cyber and natural catastrophe exposed property. Property insurers may write down capacity based on valuation increases.

For existing Insurers – it is important to check with them early to gauge any change in their capacity.

For all Insurers – it is important to establish early what their maximum capacity could be if needed.

Underwriting:

Underwriting rigor continues to increase. Insurer appetite broadened in some growth-focused targeted areas, although this remained limited in nature as insurer caution related to bottom lines continues. Quality underwriting information remained a key enabler of superior renewal outcomes.

Claims:

Information requests can be onerous, and timelines can be challenging. Insurers, adjusters, and others have been placed under a tremendous burden due to the volume of claims arising across multiple lines of coverage.

About Aon plc

Aon plc (NYSE: AON) exists to shape decisions for the better — to protect and enrich the lives of people around the world. Our colleagues provide our clients in over 120 countries with advice and solutions that give them the clarity and confidence to make better decisions to protect and grow their business.

About Aon South Africa

Aon South Africa is a leading provider of Risk Management Services, Insurance and Reinsurance Broking, Employee Benefits Solutions and Specialty Insurance Underwriting. The company employs more than 700 professionals in its 12 offices in South Africa with its head office in Sandton, Johannesburg.

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