AON

2024 Insurance State of the Market

Global and South African Insurance Market Insights

Contents

Global Insurance Market Trends

Resilience shaped the risk and insurance community in 2023. Economic inflation, a slow supply chain recovery, rising labour costs and persistent natural disaster activity pressured property loss costs and extended recovery periods. The regulatory environment also became more complex and focused on addressing matters related to insurer solvency, cyber incident disclosures, and the use of generative Artificial Intelligence, amongst many other issues.

By contrast, challenging risk types and areas not targeted for insurer growth faced greater underwriting scrutiny, higher pricing and had fewer options. Across all risks, robust underwriting information and risk differentiation were key drivers of superior renewal outcomes, and evidence of investment in corporate responsibility initiatives continued to positively impact underwriting decisions.

Over the course of the year, insurers responded to these and other dynamics of the risk and insurance environment by implementing their own resiliency measures, some of which impacted insurance market conditions. These market dynamics played out decidedly in the final quarter of 2023. We saw healthy appetite, underwriting flexibility, the availability of coverage options, and abundant capacity for well-performing, preferred risk types, as insurers sought to meet year-end performance targets.

Resilience has helped organisations weather the challenges of 2023.
In 2024, it will become a fundamental enabler of business strategies.

Looking ahead, we expect many of the economic, geopolitical, and humanitarian events that shaped 2023 to continue to evolve in 2024, and new trends to emerge, creating challenges as well as opportunities.

South Africa Insurance Market Trends

Securing sufficient insurance capacity from local and global insurers continued to be challenging, especially for global programs and for risk types that were not preferred.

The requirement to provide granular information such as geo-co-ordinates and value splits between property damage and business interruption remained burdensome and challenging for clients.

Inflation impacted underwriting and claims processes.

Natural-catastrophe related coverage restrictions / exclusions were applied to specific locations, for example KwaZulu-Natal.

Grid Collapse exclusions (Eskom loadshedding risks) were fully embedded in underwriter placement terms.

Alternative Risk Transfer mechanisms, valuation services, and business interruption analysis have become more prevalent.

Key Trends to watch in 2024

Cyber Attackers Will Continue to Exploit Vulnerabilities and Adapt Their Methods

Delays in cyberattack recognition were common in 2023. Aggregating several years of ransomware threat actor skillset trends into a single profile has resulted in risk modelling and defender preparations focused on detecting and responding to an "average" ransomware threat actor. But defenders can be slow to catch on to new attack processes that do not fit into the "average" ransomware threat actor profile, especially if the defenders do not have a broad view of the attack landscape. This often resulted in delayed recognition of an attack.

From a risk transfer perspective, insurers experienced an uptick in ransomware losses in 2023 compared to 2022, with ransomware events increasing in each quarter. In fact, there was a 205% increase in ransomware incidents in Q3 of 2023 compared to Q3 of 2022. In addition to seeing an increased frequency of events, a number of high severity ransomware incidents hit insurers' books. Many cyber-attacks observed in recent years have sidestepped cyber controls as attackers, leveraged basic and sophisticated attack methods to take control over systems and information, causing many business disruptions and brand damage.

Looking ahead, we see five important trends developing:

- Ransom and extortion pressure strategies will intensify - Threat actors will innovate and utilize asynchronous paths to apply extortion pressure to encourage victim companies to pay ransom and extortion demands, including aggression and targeted harassment of employees, customers, and board members. Companies need to be prepared for what may be an unruly situation.
- Insider risk may increase - Companies may experience increased insider risk as employers enforce return-to-office requirements and as economic challenges and layoffs in the Information Technology security industry continue to impact staff. Ransomware threat actors have and will continue to recruit company staff and pay for their credentials for remote access to facilitate an attack.
- Accountability requirements will drive investments - Cyber accountability, including regulation and representation of security controls/response, may require an increased investment in cyber security. Companies need to demonstrate cyber security progress.
- New technologies will demand new risk management measures - As companies adapt and explore AI and other emerging technologies, new challenges will emerge related to cyber security, data privacy and governance. Investment in and commitment to risk management around new technologies will be critical to manage risk effectively.
- Litigation especially related to data privacy will increase - In addition to the cyber events themselves, resulting litigation, specifically relating to data protection and privacy, will continue to increase. It is critical for companies to educate themselves – initially and continuously – on how cyber security and cyber incidents can create increased risk and how that risk can evolve over time.

Given recent increases in the frequency and severity of ransomware events, Cyber insurance appetite, underwriting, and pricing is expected to moderate from the buyer-friendly market conditions experienced in 2023. Companies should continue to invest in cyber resilient risk mitigation strategies which include risk transfer, cyber defence in-depth, and incident prevention and preparation activities.

Energy Transition Efforts Will Accelerate Amidst Global Population Growth and Growing Demand, Requiring Major Investment

The present-day energy transition has had many profound and widespread impacts, including on trading relationships, local economies, the jobs landscape, and political outcomes, to name a few. With 2023 being the hottest year on record and as the critical threshold of 1.5 degrees Celsius approaches, geopolitical and societal pressure to tackle climate change is mounting.

While the global population and demand for natural resources continues to grow, energy transition efforts have accelerated, as have actions to manage related risks.

Some of the important trends to watch in 2024 and beyond include:

Access to capital will be required to enable the massive investment in infrastructure, technology and processes

The energy transition will continue to require a massive investment in infrastructure, new technologies and process enhancements as demand for cleaner energy sources increases. Most estimates range from $100 trillion to $300 trillion which equates to an annual investment of 2-8% of global GDP between now and 2050. Companies will need access to capital and favourable government policy and regulations. Subsidies and tax advantages will serve as key enablers. Companies will compete for capital for continued investment in transition projects, technologies and assets.

Supply chains will continue to be challenged by weather and geopolitical events

Recent hostilities in the Red Sea, coupled with severe drought in Panama, highlight how serious and interconnected these risks are to global supply routes. Demand for critical and rare minerals such as lithium and cobalt as well as copper and aluminium will grow as reliance on new technologies such as renewable electricity, batteries, electronics and EVs increases. Access to materials and the infrastructure to support the transport and distribution of materials and products will also challenge new supply chain sources.

The regulatory environment will play a significant role in attracting investment

Globally, 2024 is an important election year and governments may be judged on how they support the transition in energy. Government policy remains critical to attracting investment and maintaining continued interest in the sustainable development of new energy supply. Political stability and legislative support are necessary to continue incentivising and accelerating investment in energy transition. Private and public collaboration will continue to drive innovation.

Insurers will be faced with competing demands and the need to innovate

Insurers have modified their appetite and underwriting practices in accordance with their corporate responsibility strategies. Many will continue to face competing priorities and demands, including balancing shareholder pressures with trying to understand and underwrite emerging risks and technologies such as offshore wind, solar, hydrogen and carbon capture and storage. Renewable energy assets are exposed to natural catastrophe perils and will need access to insurance capacity to enable and protect the capital committed to new investments. Changing risk profiles and risk tolerance requires new applications of traditional insurance and continued innovation of products and facilities.

Demand for Parametric Covers Will Increase as Confidence Grows

Gone are the days of static revenue streams and simple supply chains; today businesses operate within a dynamic and complex landscape. At the same time, we see increased asset values in high hazard areas, amplified shareholder attention on risk management, and a challenging traditional insurance landscape. This confluence of factors begs for a broader, more creative suite of risk management tools.

Nowhere is this need more pronounced than in the climate and natural catastrophe space - economic losses from global natural disasters in 2023 are estimated at USD 380 billion of which only USD 118 billion was insured – leaving a protection gap of 69%. Historically this protection gap was relegated to simply being a cost of doing business, but this is no longer the case we now have an additional tool to attack this uninsured gap: parametric risk transfer.

The parametric concept (triggering a payout based on an independent third-party index) is not new; these covers have been structured and placed since the 1990s in the weather trading and catastrophe bond markets. While these instruments used to be reserved for large (re)insurers and sophisticated energy traders, we are now finding new and innovative ways to apply them in the corporate and public entity space.

As we look into 2024, the trends that took shape the past few years are likely to continue, and in some cases, get more pronounced. Many of these are risks that contribute significantly to the protection gap, and they can be directly addressed via parametric mechanisms.

From our vantage point we see four important trends developing in 2024:

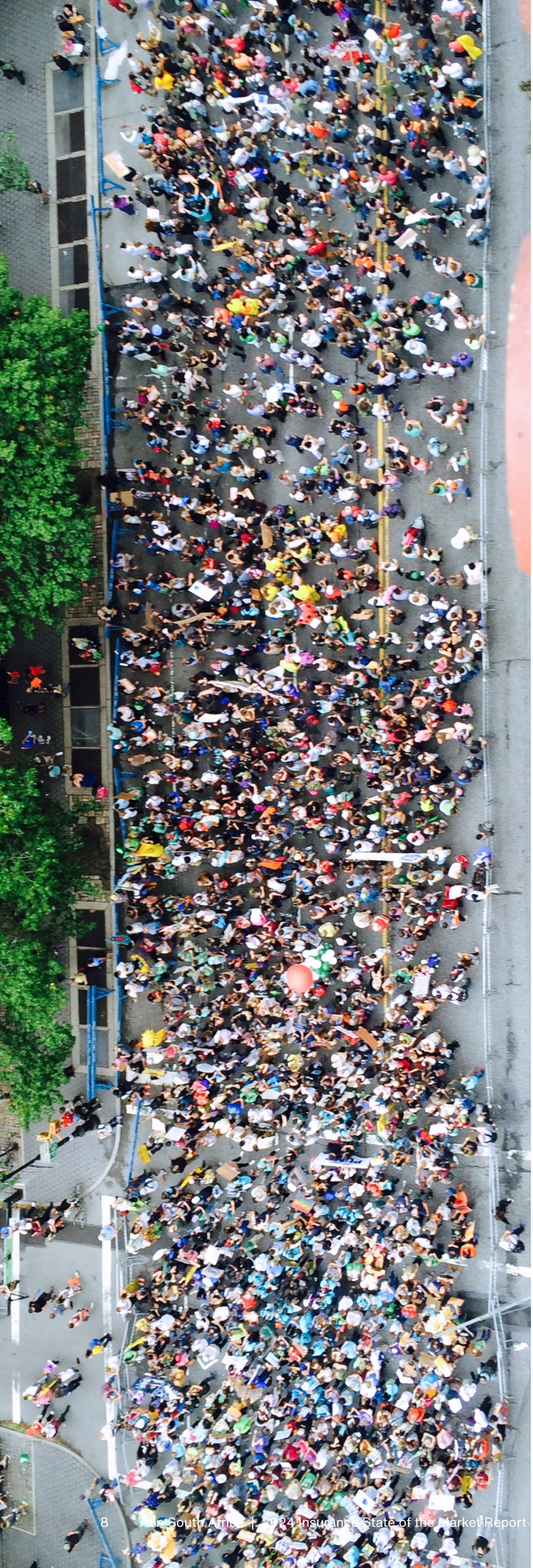
Demand for parametric solutions will increase:
Demand for parametric covers from corporates and public entities will continue to increase to provide quick liquidity after a disruptive event, to address gaps in traditional insurance cover (deductibles, sub-limits, exclusions, etc.) and to cover non-traditional risks (non-damage business interruption, contingent exposures, and many more).

The market will see an influx of capital:
Capacity will continue to flow into the space, both from established players increasing their capabilities and new players arriving on the scene. This will include both traditional capital sources (insurance and reinsurance companies) as well as non-traditional (e.g., insurance-linked securities funds). The result of this capital influx will be not only more competition on programs but also smarter and more effective structures for clients.

Confidence in parametric solutions will grow:
Parametric solutions have now been tested in claims events around the world and are behaving as expected, which will lead to a much higher comfort level in going down the parametric road.

The industry will innovate new solutions:
Innovation across the sector will increase, both within established perils (such as natural catastrophe and weather) and in new perils (e.g., cyber, marine cargo, and a wide variety of other indices).

Now that there is a general understanding of parametric solutions as viable – and often vital – tools in the risk management toolbox, the 2024 discussions with clients will explore at a deeper and more granular level how parametric solutions best fits with other tools to create a more optimal risk management strategy.



Political, Terrorism and Strike Risk Looms Large(r) in an Election Year

The ripple effect of the July 2021 riots in KZN and Gauteng - with over R50 billion in resulting damage and 340 lives lost - has been the hesitancy on the part of both local and international insurance markets to provide cover to this line of business. The international Insurance markets that provided supplementary coverage to SASRIA were also affected.

The premiums now payable for riot cover, either through SASRIA or the International Property Terrorism and Strikes (PTS) Insurance market have increased drastically – Sasria premium prices increased by 47% as reinsurance costs increased by 600%. Furthermore, Sasria reduced its coverage limits from R1,5bn for assets and business interruption to R500m. It's now more challenging to obtain Insurer interest, with many more exclusions and restrictions added to the coverage provided.

However, in the past 12-18 months, we have seen carriers wanting to advance again in providing riot cover solutions for businesses. But as we have seen in other countries across the globe, the political outlook can change quickly. As South Africa prepares for a potentially volatile election period with the election date announced for 29 May 2024, the insurance market could go one of two ways. If the current environment continues and remains steady, with little riot damage up to and beyond the election, we're likely to see the underwriting regime soften. However, if there is a deterioration with riots before or after the election, we're likely to see some insurers withdraw entirely, or certainly seek even more onerous terms.

Underwriters typically become more cautious prior to elections – this is a global trend - with more subjectivities imposed, however for now the market continues to provide solutions for our clients in South Africa. Potentially, we may see a reduction in capacity in the short-term leading up to elections, however if there is minimal to no unrest, then this capacity becomes readily available. We have seen the London Market pay out cumulative claims in excess of USD1.5billion to our clients following the unrest in 2021, making this a tried and tested solution.

Implications for large corporates with Sasria's R500 million limit

Sasria offers cover up to a limit of R500 million for most classes of risk subject to predefined premium rates. For many large corporates, these limits may however be insufficient and will require additional cover in the form of a 'riot wrap' policy.

The riot wrap provides additional coverage for loss of profit, contingent business interruption and material damage in excess of Sasria limits. The riot wrap cover also provides cover for exclusions of war and civil war which are not covered under Sasria. Essentially, where combined material damage and business interruption values exceed Sasria's R500 million limit, the riot wrap policy will provide extended coverage in respect of the claim once the underlying Sasria (or primary limit) is eroded.

Structuring of insurance programmes around riot and political risk needs specialist broking experience of both the local and international insurance markets to structure the best solution around what is an increasingly complex and volatile risk, which has the potential to be financially and operationally devastating if not correctly insured and managed. With levels of unrest rising globally, its essential to consult with specialist brokers to ensure that riot coverage has been extended to cover all perils and close any gaps, that left unchecked in a crisis, could be catastrophic.

Reinsurance Market Update

Macro Factors

Global Insured NatCat Losses - Aggregated losses since 2017 approaching $1trn; almost 60% from 'secondary' perils.

- 2023 was the warmest year on record, with 24 countries recording their highest ever temperatures.
- Estimated economic losses from global natural disasters were above short and long-term averages at $380bn.
- Estimated insured losses were $118bn, making it the 8th most expensive year on record.
- Losses from primary perils were relatively low at $17bn, despite above average tropical storm and hurricane formation.
- 'Secondary' perils generated $101bn of losses, including $58bn of severe convective storm losses in the U.S. alone.
- The year featured a record number of $1bn+ losses (37).

Economic Inflation is coming down, but loss cost inflation remains elevated and social inflation is a major concern.

Subsiding economic inflation does not address investors' two major concerns:

1. **Is today's pricing staying ahead of loss cost trends?** Commentary on the 3Q 2023 earnings calls suggests the answer is broadly "yes", albeit with question-marks over professional liability, workers' compensation and cyber.
2. **Are prior year reserves still adequate?** Most companies still show overall redundancies, but US general liability reserves in the 2015-2019 period are developing adversely.

January 2024 Renewals Overview

Broadly stable after a significant 'reset' a year ago.

- The January 2024 renewals proceeded relatively smoothly, compared to a year earlier.
- The supply of retrocession capacity increased, particularly for excess of loss products. Demand was generally stable, with buyers focused on achieving the broadest possible coverage. Overall, pricing was within target levels.
- Demand for reinsurance capacity was robust, particularly in the U.S., where record severe convective storm losses resulted in many insurers experiencing underwriting volatility, capital erosion and increased rating agency scrutiny.
- Rebounds in profitability and reported capital and more certain availability of retrocession capacity encouraged many reinsurers to display increased risk appetite at the enhanced terms established in 2023.
- Higher primary insurance pricing provided support in most areas, offset by continued uncertainty around the impact of climate change, inflation, litigation funding and geopolitical risk on ultimate loss costs.
- These unknowns are constraining new capital inflows, despite the expectation that most reinsurers will easily cover their cost of capital in 2023.
- Insurers able to clearly articulate positive changes to underwriting portfolios continue to achieve the best outcomes.
- Property: Broadly stable, after significant adjustments in 2023, except in areas that saw further ceded loss activity.
- Casualty: Moved modestly in reinsurers' favour, but not to the extent predicted at the start of the renewals.
- Specialty: A mixed bag, with heightened geopolitical risk continuing to impact war-exposed classes.

Key Considerations for a Successful Renewal

Differentiation is yielding results in a challenging market.

- Consider alternative capital for optimal placement results.
- Access facultative facilities for capacity when risks are removed from treaty programs.
- Leverage strategic consulting and data analytics to refine risk appetite, adjust investment and underwriting strategies, or review business lines.
- Explore structured and legacy reinsurance solutions to manage volatility and free-up capital for growth opportunities.
- Articulate clearly how you underwrite for inflation and its impacts on your risk profile.
- Develop a custom view of risk to reduce exposure hotspots and improve understanding of secondary perils and emerging risks.
- Understand your true cost of capital, including volatility of returns, in order to optimize long-term performance.
- Partner with a true client advocate that can provide advice and analytics to ensure your portfolio is best positioned across capital providers.

Market Dynamics Summary

- Pricing: Overall market pricing was flat but varied widely by risk and product. Natural Catastrophe-exposed and otherwise challenging risk types experienced the most significant price increases while Cyber pricing softened. Inflation was a key topic of pricing discussion.
- Capacity: While capacity was generally sufficient, appetite for middle market and poor performing risks was limited.
- Underwriting: Corporate responsibility concerns continued to gain importance in underwriting, which remained generally disciplined but was more flexible for Cyber and Financial Lines placements. Scrutiny of Property exposures further strengthened amidst ongoing Natural Catastrophe concerns.
- Limits: Expiring limits were achieved on most placements, with increases available on some risks; especially, Cyber and Directors & Officers placements, as insureds reinvested their premium savings in program enhancements.
- Deductibles: Expiring deductibles were achieved on most placements, with decreases available on some risks; especially, Cyber and Directors & Officers placements as insureds reinvested their premium savings in program enhancements.
- Coverages: Most placements renewed with expiring coverage terms and conditions, including exclusions for per-and polyfluoroalkyl substances (PFAS) and war. South Africa risks experienced coverage limitations, especially on Property and Liability placements.

Product Trends

Automobile:

Inflation and rising claims costs continued to drive up pricing and impact insurer risk appetite and capacity deployment. In addition, recent flood and hail events led to a strengthening of underwriting scrutiny and rigor.

Casualty / Liability:

Divergent market conditions were at play, based on risk size, complexity and exposure. Multinational risks with significant US exposures, as well as risks in heavy industries such as life science, chemicals, automotive parts and mining experienced capacity reductions, pricing pressure, and reconsideration of terms and conditions. PFAS also came to the forefront of underwriting discussions as many insurers sought to apply blanket exclusions.

Cyber:

Despite increased ransomware activity, insurer appetite was strong and capacity was abundant. As year-end approached, insurers seeking to utilise remaining capacity competed more aggressively and the market continued to soften across the region. While underwriting remained disciplined, insurers reduced their information requirements; however, evidence of key security controls remained a fundamental requirement to obtain coverage. War and systemic risk remained key underwriting considerations.

Directors and Officers:

Market conditions remained buyer friendly. As the downward pricing trend continued, many insureds sought to reinvest premium savings in deductible decreases, limit increases, and wording enhancements. Such improvements to terms and conditions were key levers in response to rising defence costs and class action settlements. The events of 2023 in the financial institutions sector did not have a materially negative impact on insurance market conditions.

Property:

The Property market transition continued. While insurers remained focused on rating adequacy and Natural Catastrophe capacity management, they also sought profitable portfolio growth through targeted appetite and disciplined underwriting. Rate increases continued, but they were generally moderate for most risks, although heavy industry and Natural Catastrophe-exposed risks experienced a more challenging pricing environment.

Capacity remained generally sufficient; competition strengthened, and some insurers continued to expand their local presence in the region. Detailed underwriting information and early engagement remained key to achieving superior market outcomes, and alternative solutions served as important levers when necessary.

Our Advice to Clients

Challenging and unpredictable market conditions have refocused buyers on the value, structure and overall cost of their insurance programme. The makeup of risk transfer is evolving. In most cases, buyers will be faced with decisions around how to manage an ever-expanding and complex risk transfer need. It has never been more important to focus on Total Cost of Risk (TCOR) rather than risk transfer or premium cost.

The current market dynamics create unique opportunity, incredible uncertainty, and risk – risk that is increasingly connected, and more severe. With this change comes a pressing need for businesses to make important decisions, more often.

At Aon, our industry expertise, powerful insights and risk management strategies enable us to work with organisations to identify the risks they are faced with in order to make better decisions when it comes to addressing traditional exposures and emerging risks.

To help shape better decisions and outcomes for our clients, our advice is to:

- Take time to understand new forms of volatility: start early on the renewal process, explore alternative structures and consider access to new forms of capital.

- Think more aggressively about risk retention: to 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.

- Set your risk tolerance and appetite at a portfolio level rather than per product: rather than assuming large deductibles on part of your programme and small deductibles on other parts, consider consolidating premium and leveraging it to build scale within a captive.

- Consider whether your business model has changed: reflecting your organisation's learnings from COVID-19. As technology improves and ESG starts to dominate boardroom decisions, challenge the point at which you would consider not reinstating an asset, for example. Approach risk management broadly rather than focusing on the renewal of your expiring insurance policies.

- Be proactive and differentiate your risk: the current, selective underwriting environment calls for detailed disclosure and business profiles as well as a description of risk management and mitigation efforts. Be sure to describe any changes to your business models. Leverage analytical tools like risk modelling. Risk differentiation is key and, when combined with sufficient lead time for underwriters to review, generally results in positive outcomes.

- Explore all options: review retentions, scope of coverage and sub-limits. Consider alternative sources of capacity, working with Aon to ensure options are fully explored.

- Utilise Aon's capabilities to review Business interruption values and indemnity periods.

- Report claims proactively and with thorough documentation: 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.

- Try to engage with Insurers who align with your values: 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.

- Maintain ongoing Insurer dialog: 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.

About Aon

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 and sovereignties with advice and solutions that give them the clarity and confidence to make better decisions to protect and grow their business.

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