Resilience in times of change

General Insurance Industry Review 2023

With the top 10 trends impacting the sector

March 2023

KPMG.com.au

The *KPMG General Insurance Insights Dashboard* which accompanies this report contains a range of interactive charts and graphs presenting the key industry metrics for the past five years. The interactive dashboard enables the data to be filtered to view the metrics for a particular year or insurer. It also enables comparison of metrics for an individual insurer to others in the market.

The dashboard can be accessed via our website at: KPMG.com/au/insurancereview

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Foreword

KPMG's General Insurance Industry Review 2023 includes the financial results up to 31 December 2022 of all Australian direct insurers.

The format, content and presentation of the General Insurance Industry Review 2023 comprises three segments:

1. **Results and analysis** – this section contains a concise but insightful analysis of how the general insurance sector performed throughout the year utilising Australian Prudential Regulation Authority (APRA) annual data statistics.
2. **Top 10 emerging trends** – this includes KPMG's views on the top 10 trends that will shape and influence the industry for the remainder of 2023 and beyond. These trends were informed by our 2022 Insurance CEO Outlook that drew on the insights and perspectives of 1,325 global CEOs. In this section we highlight current and emerging trends, which Australian general insurers should consider in order to build resilience in these changing times.
3. **KPMG General Insurance Insights Dashboard** – this interactive dashboard contains a range of interactive charts and graphs presenting the key industry metrics for the past five years. The interactive dashboard enables the data to be filtered to view the metrics for a particular year or insurer. It also enables comparison of metrics for an individual insurer to others in the market.

"KPMG's annual review highlights 10 trends that the firm believes will be important to the sector this year. These trends permeate through all areas of the insurance value chain, and are expected to be 'top of mind' for insurers as they continue their journey throughout 2023. Consistent with our 2022 Insurance CEO Outlook, CEOs globally believe that technology and ESG are amongst their highest priorities and these trends feature heavily within the Top 10 trends of our Australian General Insurance Industry Review for 2023"

DAVID AKERS

"Insurers' profits during the year rose to a five-year high. That being said insurance is by its nature cyclical and only three years ago insurers' profits were minimal, largely due to significant claims from the bushfires and other catastrophic weather events. With the expectation of increasing frequency and severity of natural hazards, rising reinsurance costs, increasing inflation, supply chain issues and labour shortages we envisage there will continue to be upwards pressure on premiums pricing. It is anticipated that on average, premiums will rise by at least 10% throughout 2023."

SCOTT GUSE

Results and analysis

At a glance

		2022	2021	2020	2019	2018
Gross written premium $m	●	59,364	53,781	48,625	46,271	44,111
Net earned premium $m	●	40,286	36,003	33,703	32,967	31,217
Underwriting result $m	●	6,125	3,562	(186)	2,211	3,443
Insurance profit $m	●	4,949	3,483	930	4,070	4,609
Investment income $m	●	(1,257)	509	1,452	2,984	1,912
Loss ratio	●	62%	66%	75%	69%	65%
Expense ratio	●	23%	24%	25%	25%	24%
Combined ratio	●	85%	90%	101%	93%	89%
Insurance margin	●	12%	10%	3%	12%	15%
Capital ratio	●	1.72	1.69	1.68	1.67	1.74

Source: APRA Annual General Insurance Performance Statistics Dec 2022 (Direct Insurers only) and KPMG analysis

Year in review

Insurance results – a five-year high

The 2022 industry insurance profit of $4,949 million was up 42% (2021: $3,483) and is notably the highest result over the past five years. The increase was largely driven by a 10% increase (2021: 11%) in gross written premium to $59,364 million on the back of higher premium prices. The growth in gross written premium was evident across all classes of business (except 'mortgage'), though most profound in the following areas where we saw both an increase in premium rates, and the number of risks underwritten:

- homeowners/householders
- commercial motor vehicle
- employer's liability.

Increased claims costs were largely mitigated by these higher, average written premium prices, with insurers continuing to price products to reflect claims inflation, natural hazards expectations and higher reinsurance costs.

This resulted in an improvement in the 2022 loss ratio of 62% (2021: 66%). The decrease in the loss ratio is due to the growth in net earned premium of 12% exceeding the increase in net incurred claims of 5%. Despite raised levels of natural catastrophes and claims inflation in 2022, reinsurance coverages and releases to COVID-19 business interruption provisions reduced the impact on net claims costs. The underwriting result of $6,125 million was 72% higher than the previous year (2021: $3,562 million).

COVID-19 provision releases

With the High Court of Australia decision on 14 October 2022 in relation to business interruption claims being largely favourable to insurers, most insurers revised their business interruption provisions downwards, thus releasing these previous year provisions to current year profits.

Cost discipline

Cost discipline remained a key focus area for insurers, with the expense ratio improving to 23% (2021: 24%). This is despite continued raised levels of spending on technology, regulatory and compliance costs. Insurers continued to invest in automation in pursuit of customer and operational excellence.

Volatile investments

Investment losses were $1,257 million (2021: $509 million profit) driven by rising bond yields in fixed interest investments (which created significant mark to market losses for many insurers). Volatile equity markets also contributed to this loss, particularly in the first half of 2022.

Capital

The industry's capital coverage at 31 December 2022 for direct insurers increased marginally to 1.72 times the APRA prescribed capital amount (2021: 1.69 times).

Catastrophes

Insurers continued to be impacted by natural perils in 2022, with the overall catastrophe cost for the industry more than doubling from 2021. This was predominantly driven by the February 2022 South East QLD and NSW Floods which is now the costliest catastrophe on record for Australia (based on insured losses).

CATASTROPHES – 2022		CLAIMS COUNT	TOTAL LOSS $M
CAT224	Nov 22 Central West NSW Floods	13,376	196
CAT223	Oct 22 VIC, NSW and TAS Floods	20,920	638
CAT222	Jul 22 NSW Severe Weather	22,656	262
CAT221	Feb 22 South East QLD and NSW Floods	239,538	5,757
			6,853

CATASTROPHES – 2021		CLAIMS COUNT	TOTAL LOSS $M
CAT216	Oct 2021 SA VIC Severe Storms	110,428	892
CAT215	Sep 2021 Mansfield Earthquake	18,465	101
CAT214	Jun 2021 Victorian Storms and Floods	34,372	313
CAT213	Apr 2021 Cyclone Seroja (WA)	10,022	411
CAT212	Mar 2021 East Coast Storms and Floods (NSW, QLD)	58,865	618
CAT211	Feb 2021 Perth Hills Bushfire	1,342	99
			2,434

Source: insurancecouncil.com.au – Historical Catastrophe Data February 2023

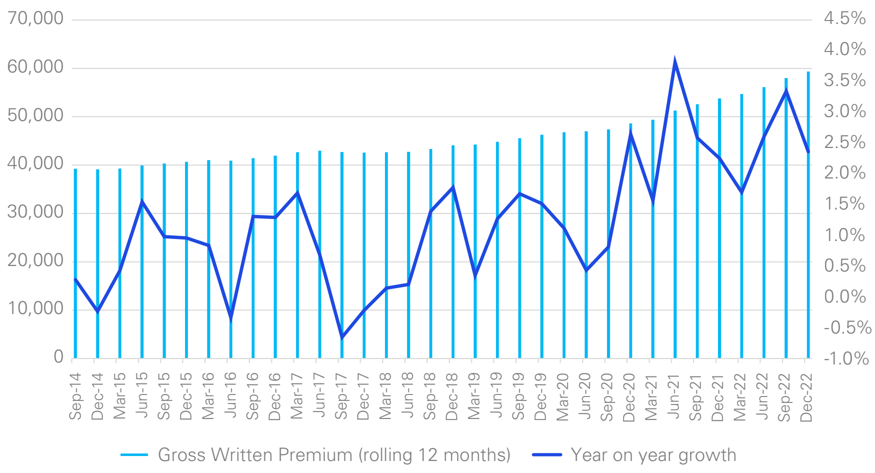
Market outlook

The average gross written premium quarterly increase for 2022 was 2.5%, maintaining 2021's strong momentum (2.6%). This quarterly increase led to an annual increase of circa 10% in gross written premium. Growth was driven by average written premium increases, reflective of higher natural hazards, increased reinsurance costs, and inflationary pressures.

The expectation of increasing frequency and severity of natural hazards, rising reinsurance costs, increasing inflation, supply chain issues and labour shortages will continue to put upwards pressure on premiums pricing. It is anticipated that on average, premiums will rise by at least 10% throughout 2023.

Improving resilience and thereby reducing the impact of extreme weather events on Australian communities is a key focus for the industry. This is seen as a must in ensuring insurance remains affordable to all, especially those that need it.

GROSS WRITTEN PREMIUM (ROLLING 12 MONTHS)



Source: APRA Annual General Insurance Performance Statistics Dec 2022 (Direct Insurers only) and KPMG analysis

To this end, the industry is looking for increased government investment, and to work together to develop a more resilient and affordable future for insurance in Australia. Disaster relief spending is too often an afterthought in Australia, and a more forward-thinking approach to managing catastrophe risk is required. Suggestions for public policy initiatives have included reviewing land use planning arrangements and amending building codes.

On other fronts, ongoing investment in technology modernisation (including cyber defence), ESG, as well as regulatory and compliance transformation initiatives are expected to continue in 2023.

Insurers are also finalising their implementation of the global accounting standard, IFRS 17 Insurance Contracts. Most large insurers are more progressed than the small to medium insurers, and for some, it has been a sprint to the finish.

Share price performance

ASX LISTED INSURANCE COMPANIES' PERFORMANCE

The 'ASX Listed Insurance Companies' Performance' graph depicts the share price performance of the four listed Australian General Insurers – IAG, QBE, Suncorp (SUN) and Helia (HLIA) – against the Australian Stock Exchange (ASX) 200 Index for the period from January 2018 to December 2022.

The overall ASX 200 Index decreased by 7% during 2022, however, the Australian listed insurers had mixed results in relation to their own share price performance. Helia and QBE outperformed the ASX 200 index with increases of 14% and 13% respectively for the 2022 year.

IAG and Suncorp saw an increase in share price of 7% and 4% respectively.

Top 10 GI industry trends

01
Resilience

02
Reinsurance

03
Technology modernisation

04
ESG

05
Simplification and cost optimisation

06
Changing customer expectations

07
Cyber

08
Data

09
IFRS 17

10
Regulatory and compliance transformation

01. Resilience

Insurers continue to face a higher exposure to natural perils, such as floods, bushfires and cyclones.

Natural disasters also have a significant impact on people and communities. To enhance the country's resilience against such events, insurers are encouraging government action to reduce both the risk and exposure. Public policy initiatives such as an increase in commonwealth investment in extreme weather resilience measures; reviewing land use planning arrangements; and amending building codes to include a resilience and future risk standard are among the policy recommendations made by the Insurance Council of Australia (ICA).

Resilience measures are important to keep insurance affordable in Australia. There is a benefit to all Australians if such measures are undertaken and for insurers and governments to work together to build a more resilient Australia.[1]

02. Reinsurance

Reinsurance costs have increased exponentially in the last few years largely due to increased claims from weather-related catastrophes.

For Australian insurers, reinsurance costs have risen much faster and higher than gross written premium has over the same period. As a result, direct insurers are feeling the cost of this impact on profitability.

Insurers have and will continue to pass these increased reinsurance costs on to customers which will contribute to the anticipated 10% increase in average premiums that we expect for 2023.

The Australian Government cyclone reinsurance pool, which came into effect on 1 July 2022, is designed to improve the accessibility and affordability of insurance for households and small businesses in cyclone-prone areas. As the pool has only recently commenced operating, it remains to be seen how effective the structure will be in keeping the end customer's costs reasonable and affordable.

[1] Insurance Council of Australia: Building a more resilient Australia

03. Technology modernisation

Insurers should evaluate whether their current technology platforms and architecture are fit for purpose and make changes to better align for future needs.

Many insurers have a complex technology architecture which makes it difficult to be flexible. This includes legacy systems that are expensive to replace or upgrade and are also expensive to maintain when regulatory change occurs. Insurers have also invested in digitisation to keep up with customer expectations. This may include manual or semi-automated processes to connect legacy systems to the digital customer experience.

Insurers could derive enormous business value from a clear data and technology target state that business decisions can be assessed against to ensure the organisation is continually moving towards more up-to-date technology systems and platforms. Any business decisions should include the potential cost in maintaining legacy systems or upgrading to new technology that aligns to the target state.

Digital investment continues to be strategically important for insurers to remain relevant and be competitive. Insurers are realising that partnerships are critical to staying resilient and delivering on their digital transformation plans.

04. ESG

Australian insurers are ahead of many companies in other sectors in Australia when it comes to ESG but behind the pack globally.

Globally, insurers are increasingly recognising the breadth and depth of ESG within their own businesses and the impact they can have on society.

Companies need to include ESG in all aspects of the organisation and ensure that ESG is embedded into the company's financial ambition and vision. Most insurers in Australia have set ESG targets and are now tackling the difficult task of operationalising and reporting against these targets. It requires the targets to be embedded at every level of the organisation from a decision-making process, system and culture perspective.

The ability to integrate ESG into the DNA of an organisation will be a competitive advantage in the future, both to avoid any suggestion of greenwashing and green fraud, but also to attract investors and employees whose ESG expectations continue to increase. Insurers may need to partner with others to build sustainable solutions that have multi-factor benefits.

With the International Sustainability Standards Board (ISSB) expected to finalise IFRS S1 and IFRS S2[2] in 2023, ESG reporting is moving towards essential rather than optional.

[2] IFRS S1 General Requirements for Disclosure of Sustainability-related Financial Information and IFRS S2 Climate-related Disclosures

05. Simplification and cost optimisation

Similar to 2021, profitability remains a challenge as a result of increased claims and reinsurance costs.

As a result, this is driving a continued focus on simplification and automation across all aspects of the value chain.

Insurers need to continue to focus on digitisation, simplification, productivity, automation and operating model adjustments across all aspects of the value chain to drive efficiency and cost reductions.

Insurers need to continue to be strategic to achieve cost optimisation and this may include working with partners to drive value. Identifying and managing third parties effectively can help reduce costs whilst mitigating risks and supplementing capability gaps.

06. Changing customer expectations

Customers are increasingly looking for personalised, value-driven digital solutions and they want experiences that allow them to be in control of the process as well as having ongoing visibility of their status.

Some insurers have made significant investments in digitising and improving the front-end sales process. The ability to take out a new policy, renew existing policies, make amendments and change excesses all online have reduced insurers' operating costs and enhanced customer interactions.

Some insurers have also made investments and enhancements to the claims management process, such as developing claims tracking apps. However, as the claims management process is a critical interaction with a customer that can really 'make or break' a future customer relationship, a continued focus is warranted to provide more transparency over the claims management cycle.

To improve the customer claims experience, companies should begin with the customer and work backwards, taking an outside-in perspective to reverse-engineer and shape what the experience should be.

07. Cyber

With an exponential increase in cyber attacks, there is heightened awareness of the cyber risks facing insurers (as corporates).

As a consequence, in addition to focusing on their cyber defences, insurers are currently reviewing the data they hold, determining what should be retained, and purging excess data that is being held.

The recent cyber attacks in Australia have left consumer trust low and organisations exposed to more security risk than ever before on how they prepare for and respond to a breach. Building and protecting that sense of trust requires many parts of the organisation to work together to deliver a consistent unified vision.

When it comes to products, cyber protection insurance continues to only be offered by a small number of niche players, and it is becoming increasingly difficult to obtain in the Australian market. Future government action may need to be considered to provide protection in this space.

08. Data

APRA's five-year roadmap for transforming its approach to collecting data from regulated entities creates an opportunity to leverage compliance into a larger business transformation, in order to develop an insights-led organisation.

Enabling data-driven decision-making is one of the core pillars of APRA's Corporate Plan. APRA's five-year timeframe for the detailed data collection is ambitious and the timelines are more aggressive than those implemented by other global regulators. The scope of data to be collected will increase as APRA works with other agencies on holistic data requirements and includes emerging focus areas such as climate change risk.

Organisations should be planning for delivery and capability enhancements to ensure the outcomes delivered over the next five years are sustainable and enabled by strategic data and technology architecture.

09. IFRS 17

Significant investment has been made by insurers to date to comply with IFRS 17, however, further investment will be required to successfully embed strategic solutions.

Many general insurers, especially small to medium insurers, have sprinted to the finish line ultimately needing to rely on tactical rather than strategic solutions. APRA's data collection is equally growing more detailed, and the impending data quality framework will raise further expectations on the quality of the data and executive oversight of the quality. Some insurers may struggle to meet the data quality expectations, especially if IFRS 17 data is not integrated and used for other purposes such as management reporting.

Ideally insurers should look to use IFRS 17 data as an input to management decisions and embed the new standard in their ways of working. It is now time for insurers to find ways to gain efficiencies and value from IFRS 17 data.

10. Regulatory and compliance transformation

The general insurance industry has gone through significant regulatory change in the last few years with many insurers hopeful to move into a phase of embedment and refinement of the regulatory changes.

Unfortunately regulatory change has not slowed down. If anything it continues to accelerate, both in the quantum of changes and the reduced implementation timeframes, leaving insurers struggling to keep up. The pricing promises review, CPS 230, CPS 190 and CPS 511 are among the regulatory changes currently being implemented.

The expectation from the regulator is a customer focused, integrated operation where accountability is clear, material service providers are managed well, promises to customers are monitored, and executive remuneration aligns to prudently managed risks.

Whilst regulatory changes have been necessary, the pendulum may have swung too far. It is hoped that some balance will be attained in the future.

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