Kashmira Naran

Partner
Insurance
Tel: +27 82 710 7629
Email: kashmira.naran@kpmg.co.za

Reinsurance industry results

The 2023 financial results of reinsurers participating in this year's survey reflect a welcome reprieve from the challenges faced over the last few years. From COVID-19 in 2020, the Kwa-Zulu Natal riots in 2021, the Kwa-Zulu Natal floods in 2022 and the ongoing local infrastructural challenges experienced, to name but a few. These were some of the toughest years seen by the South African insurance industry, which tested the resilience and core purpose of the industry beyond limits thought imaginable.

The strict measures reinsurers put in place to restore profitability and balance sheet strength post these events, such as price increases and the implementation of stricter underwriting principles (higher attachment points and underwriting limits), have started to reap the benefits they set out to achieve. While the industry appears to be in a state of calm right now, with fewer natural catastrophe events and load shedding having been suspended for 163 consecutive days at the date of writing this article, the uncertainty around climate change, political actions and the impact of global economic and geopolitical activity require constant vigilance and assessment.

According to the AON 2024 Climate and Catastrophe Insight report[1], the following flooding events occurred in South Africa in 2023:

Date(s)	Deaths	Economic loss (USD)
14 Jun – 19 Jun 2023	2	100 million
23 Sep – 26 Sep 2023	11	Millions
27 December 2023	21	Millions

The 2023 results of reinsurers analysed in this survey have not been materially impacted by these losses, which is most likely attributable to the underwriting limitations put in place, following the spate of loss events that took place over the last few years.

The latest insurance sector data published by the South African Reserve Bank indicates that there are nine professional reinsurers in South Africa as at December 2023[2] (2022: nine professional reinsurers). In this year's survey, we analyse the results of four registered reinsurers, representing approximately 51% of the South African market. These results include three composite reinsurers and one composite branch. The financial results of all reinsurers surveyed in this year's analysis have been prepared under an *IFRS 17 Insurance Contracts* (IFRS 17) basis of accounting.

The financial results of the life and non-life insurance industries are a key contributor to the results of the reinsurance industry. It is, therefore, important that the results of the reinsurance industry are reflected on against what has transpired over the course of 2023 for South African non-life and life insurers.

The life insurance industry continued to generate strong results, with an increase in profits from R27.3 billion in 2022 to R37.4 billion in 2023. Similar to what we reported in 2022, these results are reflective of the recovery and stabilisation experienced by life insurers in respect of normalised mortality levels post the COVID-19 pandemic.

The non-life insurance industry went from a loss of R14.6 billion in 2022 to a profit of R13.7 billion in 2023. While hardened reinsurance rates prevailed over the period, along with a high inflationary and interest rate environment, the turnaround in results is largely due to the benign natural catastrophe weather event exposures over the course of the year and the absence of the 2021 riots in Kwa-Zulu Natal.

[1] https://assets.aon.com/-/media/files/aon/reports/2024/climate-and-catastrophe-insights-report.pdf

[2] https://www.resbank.co.za/content/dam/sarb/publications/prudential-authority/pa-selected-south-african-insurance-sector-data/2023/Selected%20South%20African%20insurance%20sector December_2023.pdf

The gross domestic product (GDP) growth rate for 2023 was 0.6%[3], following an increase of 1.9%[4] in 2022. According to the African Development Bank Group, this deceleration was "due to persistent electricity shortages, transport sector constraints, and lower international prices for gold and platinum group metals."[5] In addition, "Household consumption declined from 2.8% in 2022 to 0.7% in 2023 due to higher interest rates. Inflation declined from 6.9% in 2022 to 6.0% in 2023 reflecting lower international fuel prices. The South African rand weakened by 12.4% against the US dollar in 2023, to 18.40 rand to the dollar, due to declining terms of trade for South Africa's main exports."[6] These factors persisted from 2022 and continue to place pressure on the disposable income of consumers and policyholders with cascading impacts on premium renewals, rate increases and lapse rates.

The African Development Bank Group goes on to further note that "The poverty rate was estimated at 21.6% in 2023, and the Gini coefficient was 0.63. Overall unemployment stood at 32.1% and youth (25–34 years) unemployment at 39%. South Africa is among the top 10 most unequal countries globally."[7] With competition being rife and market saturation at already high levels in the South African insurance industry, these economic indicators shed interesting light on the challenges that the industry may be experiencing in achieving market growth. To increase revenue on existing business, attract new customers, maintain the existing customer base or tap into underserved markets, insurers would need to employ intense levels of innovation, technology investment and collaboration to see top line growth.

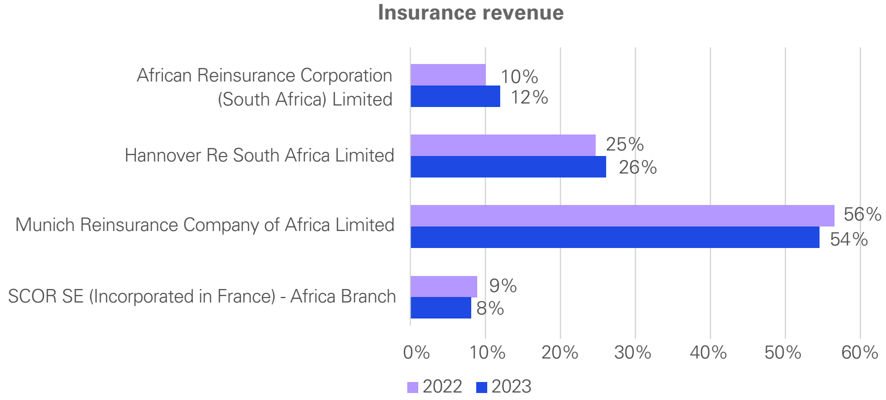
Financial indicators

Growth

Insurance revenue declined slightly by 2% over 2023, with varied results being experienced across all reinsurers surveyed. African Reinsurance Corporation (South Africa) Limited (Africa Re) and Hannover Re South Africa Limited (Hannover Re) both experienced growth in insurance revenue, with Munich Reinsurance Company of Africa Limited (Munich Re) and SCOR SE (Incorporated in France) - Africa Branch (SCOR Africa Branch) experiencing decreasing revenue. These results are influenced by various factors such as hardened reinsurance rates, renewals, repricing, organic growth, new business, cancellations and the implementation of stricter underwriting risk principles.

Based on top line growth (with reference to a combination of insurance revenue and gross written premium measures), the 2023 results of reinsurers surveyed are largely reflective of the growth experienced by life insurers of 10.4% by net premium income measures under *IFRS 4 Insurance Contracts* (IFRS 4) and 3.9% by insurance revenue measures under IFRS 17. Non-life insurers saw growth of 16.6% in IFRS 4 gross written premium and 7.9% growth in IFRS 17 insurance revenue.

Illustrated below is the share of the reinsurance market by insurance revenue based on these four reinsurers' share (51%) of the market, as reported in their audited financial statements.



The market share distribution across reinsurers continues to remain relatively consistent, with marginal movements noted across industry players.

[3] https://www.statssa.gov.za/publications/P0441/P04414thQuarter2023.pdf

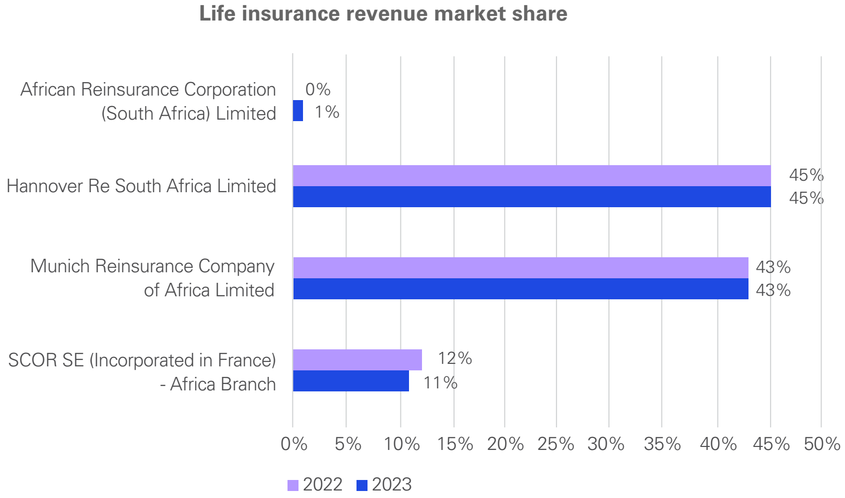
[4] https://www.statssa.gov.za/publications/P0441/P04414thQuarter2023.pdf

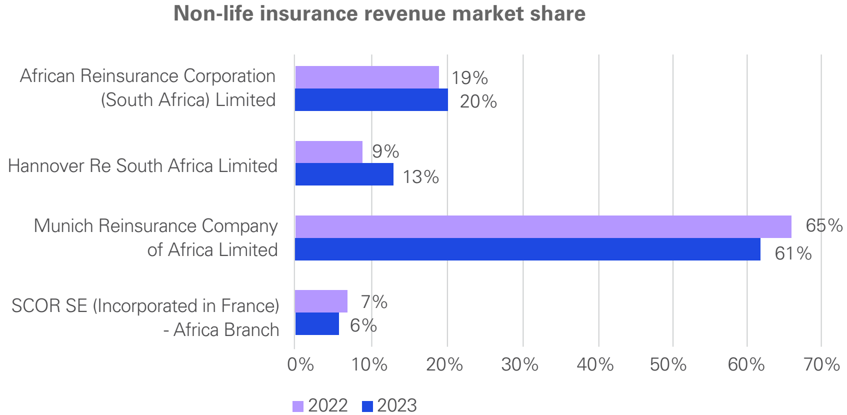
[5] https://www.afdb.org/en/countries/southern-africa/south-africa/south-africa-economic-outlook

[6] https://www.afdb.org/en/countries/southern-africa/south-africa/south-africa-economic-outlook

[7] https://www.afdb.org/en/countries/southern-africa/south-africa/south-africa-economic-outlook

We discuss the detailed movements per reinsurer further on in our analysis.





Other key performance indicators of the four reinsurers surveyed are as follows:

Performance indicator	2023	2022
Reinsurance ratio[8]	81%	618%
Insurance service expenses ratio[9]	84%	101%
Insurance service result ratio[10]	63%	84%
Incurred claims and other expenses ratio[11]	69%	74%
Acquisition costs incurred ratio[12]	4%	5%
Insurance service result	R639 million profit	R877 million profit

The 2023 results largely follow a similar trajectory to that experienced in 2022, reflecting the recovery and stabilisation of the insurance market following muted natural catastrophe incidents, as well as the results of strategic initiatives implemented by reinsurers over the last few years to moderate risk exposures, such as premium rate increases and underwriting limitations.

The decline in the reinsurance ratio from 618% in 2022 to 81% in 2023 is largely due to net **income** earned from reinsurance contracts held by Africa Re and Munich Re in 2022, and this amount being in excess of the insurance contracts result[13].

The improvement in the insurance service expenses ratio is largely characterised by the lower incidence of natural catastrophe events, with all reinsurers surveyed having experienced a reduction in these ratios from 2022 to 2023.

Africa Re is the largest contributor to the acquisition cost ratio with the decrease attributable to better rates secured on renewals during the year.

8 Reinsurance ratio: net expenses/income from reinsurance contracts held/insurance contracts result (insurance revenue less insurance service expenses from insurance contracts issued)

9 Insurance service expenses ratio: insurance service expenses/insurance revenue

10 Insurance service result ratio: insurance service result/profit/(loss) before tax

11 Incurred claims and other expenses ratio: incurred claims and other expenses/insurance revenue

12 Acquisition costs incurred ratio: acquisition costs incurred/insurance revenue

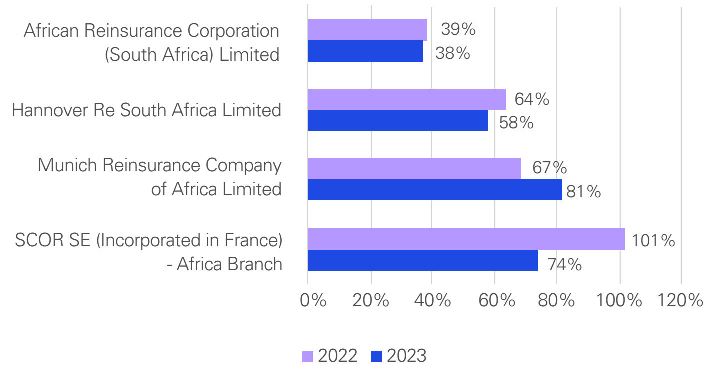
13 Insurance contracts result: insurance revenue less insurance service expenses from insurance contracts issued

The insurance service result ratio reflects the contribution of the insurance service result to profit/(loss) before tax for the year. Hannover Re and Munich Re both experienced positive insurance service results which contributed to overall profit before tax for both 2022 and 2023. While Africa Re experienced an overall profit before tax for the year, it experienced a loss on its insurance service result for both 2022 and 2023. SCOR Africa Branch also experienced a loss in its insurance service result, which flowed down to the loss before tax line.

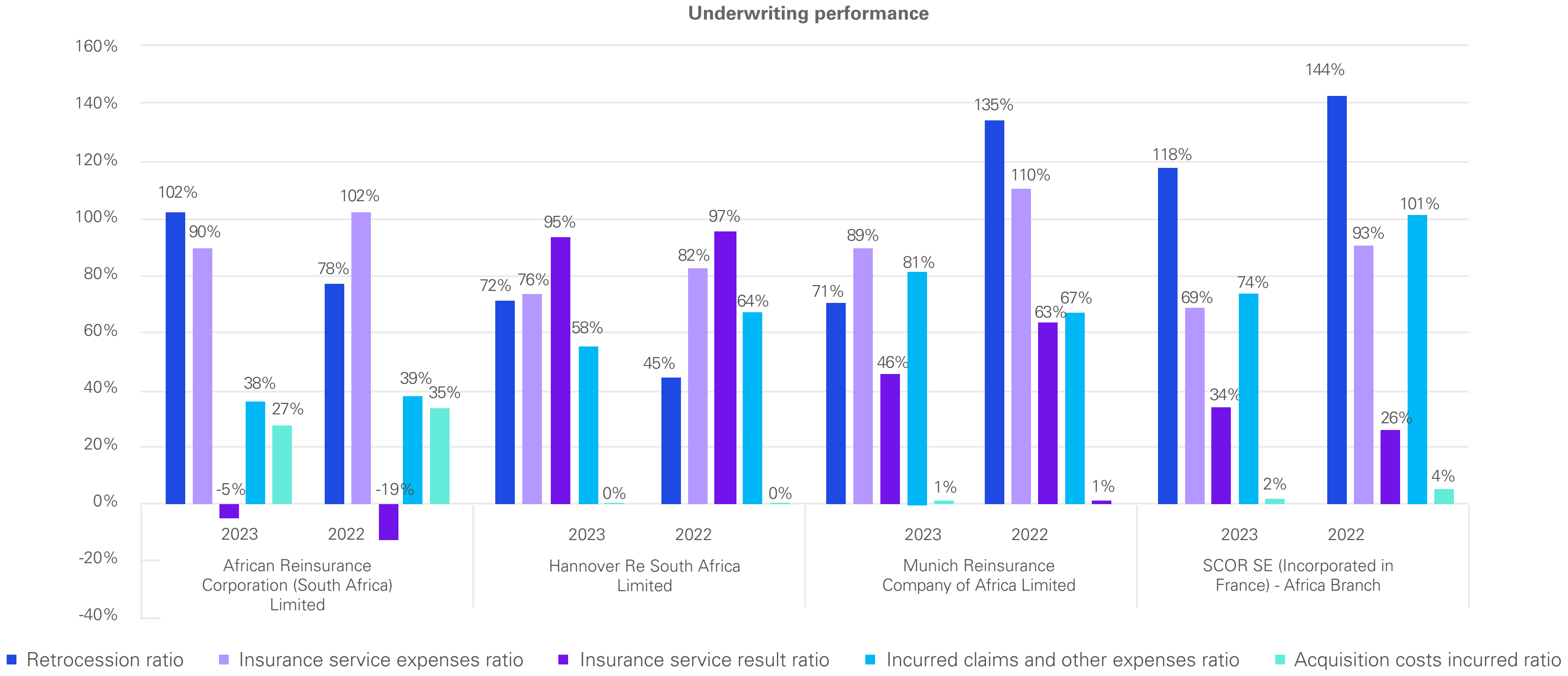
In the previous year we noted that except for Munich Re, no other reinsurer declared dividends during the 2022 financial year, consistent with the financial results of 2021 and 2020. This has largely remained the same apart from Hannover Re that declared a dividend in 2023. It is interesting to note that many reinsurers continued to take a conservative approach, in the context of the strength of their balance sheets. This level of conservatism is understood in the context of the uncertainty around the impact of climate change, the continued recovery of previous losses, as well as local and global market uncertainties.

The graph included below illustrates the incurred claims and other expenses to insurance revenue ratio for each reinsurer. With the exception of Munich Re, reinsurers experienced a healthy improvement in loss ratios over the year, compared to 2022.

Incurred claims and other expenses to insurance revenue



Underwriting performance per reinsurer



Mixed performance results are reflected across all reinsurers surveyed, reflecting the complexity and nuances of market dynamics on each reinsurer's business operations. The next section of our report provides deeper analysis into the results of each reinsurer.

Africa Re

The 2023 financial year was the first full year in which Africa Re operated as a composite reinsurer, after having undergone a relicensing process in 2021 to include the ability to write life reinsurance risks, in addition to its already established non-life insurance business. The financial results for 2023 reflect the results of operations from writing both life and non-life reinsurance business, with only non-life business being written in previous financial years. The non-life insurance operations contributed 96% to insurance revenue for 2023 (2022: 100%) with the remaining insurance revenue of 4% (2022: 0%) attributable to the life insurance business.

Africa Re experienced growth in insurance revenue of 11% from R2 244 million in 2022 to R2 490 million in 2023. This performance result reflects a sustained growth trajectory in line with the objectives the reinsurer set out to achieve in terms of the turnaround strategy which it embarked on in 2018. This strategy aimed to de-risk and enforce better underwriting discipline in the quality of risks assumed. The growth in insurance revenue can also be attributed to premium rate increases secured on renewals during the year.

The insurance service expenses ratio reflects improved performance from 102% in 2022 to 90% in 2023, along with the insurance claims and other expenses ratio from 39% in 2022 to 38% in 2023. This is largely due to the reinsurer not having exposure to catastrophe losses during the year, in line with industry wide observations, and due to the impacts of the strategic underwriting decisions applied. The improved claims experience was offset by an increase in attributable expenses due to inflation and planned investment in human capital and other resources, to support the business growth and regulatory compliance obligations.

The reinsurance ratio increased from 78% in 2022 to 102% in 2023. The reasons for this are complex and need to be unpacked further. During 2022 a loss of R55 million on the insurance contracts result was observed. This loss was offset by net income earned from retrocession contracts of R43 million, as a result of amounts recoverable from the retrocessionaire for incurred claims being in excess of retrocession premiums paid. During 2023, a profit on the insurance contracts result was observed of R239 million, offset by a net expense from retrocession contracts of R245 million.

While the insurance service result and net insurance result reflected losses for 2023, the performance of the investment portfolio was a key driver in delivering an overall profit after tax for the year of R85 million (2022: R48 million).

Hannover Re

Overall insurance revenue growth was muted at 4% from R5 232 million in 2022 to R5 452 million in 2023. However, this result needs to be understood in the context of the contribution of the life and non-life insurance segments to the overall business. Life insurance revenue contributed 70% (2022: 79%) to total insurance revenue with the non-life insurance business contribution coming in at 30% (2022: 21%). While the non-life book of business reflected insurance revenue growth of 47% from 2022, this growth was offset by a 7% decline in life insurance revenue.

The insurance service expense ratio showed improvement from 82% in 2022 to 76% in 2023. Similarly, the incurred claims and other expenses ratio decreased from 64% in 2022 to 58% in 2023. The primary contributing factor is attributable to the lower extent of natural catastrophe and other major losses during the year.

Despite the positive gains experienced from insurance revenue growth and improved performance over the insurance contracts result, the insurance service result ratio declined from 97% in 2022 to 95% in 2023. This can be attributed to the increased net expense from reinsurance contracts ratio from 45% in 2022 to 72% in 2023, largely due to increased retrocession premiums paid as a result of the hardened reinsurance market.

Munich Re

Munich Re experienced a decrease in insurance revenue of 6% from R11 837 million in 2022 to R11 166 million in 2023. The non-life insurance book contributed 67% (2022: 66%) to total insurance revenue with the remaining 33% (2022: 34%) attributable to the life insurance book of business. Insurance revenue from the life insurance business decreased by 8% while insurance revenue from the non-life insurance business decreased by 4%.

The incurred claims and other expenses ratio deteriorated from 67% in 2022 to 81% in 2023. This can be attributed to an increase of 111% in incurred claims and expenses related to the life business (movement in loss ratio from 46% in 2022 to 106% in 2023), offset by a decrease of 16% in the non-life insurance business (movement in loss ratio from 78% in 2022 to 68% in 2023).

In contrast, the insurance service expense ratio improved from 110% in 2022 to 89% in 2023, largely due to the decrease in changes related to past service across both the life and non-life insurance segments.

Similar to Africa Re, the reasons for the decrease in the retrocession ratio from 135% in 2022 to 71% in 2023 is complex and requires further elaboration. During 2022 a loss of R1 221 million on the insurance contracts result was observed. This loss was offset by net income earned from retrocession contracts of R1 646 million, as a result of amounts recoverable from the retrocessionaire for incurred claims being in excess of retrocession premiums paid, largely due to recoveries related to catastrophe events experienced in 2022. During 2023, a profit on the insurance contracts result was observed of R1 218 million, offset by a net expense from retrocession contracts of R861 million.

Consequently, the decline in insurance revenue and increases in incurred claims and other expenses and net expenses from reinsurance contracts resulted in a decrease in the insurance service result ratio from 63% in 2022 to 46% in 2023.

SCOR Africa Branch

Similar to Munich Re, SCOR Africa Branch was the only other reinsurer to experience a decrease in insurance revenue (14% from R1 927 million in 2022 to R1 647 million in 2023). Life insurance revenue decreased by 18% while non-life insurance revenue decreased by 10%. The share of the life and non-life insurance books of business in terms of insurance revenue measures is fairly even with the life business contributing 57% (2022: 59%) to total insurance revenue and the non-life business contributing 43% (2022: 41%).

The decrease in the incurred claims and other expenses ratio from 101% in 2022 to 74% in 2023 can be attributed to there being no exposures to natural catastrophe losses in 2023. The loss ratio for the life insurance book of business improved from 106% in 2022 to 101% in 2023, with the non-life insurance loss ratio improving from 95% in 2022 to 38% in 2023.

Despite the decrease in insurance revenue noted, SCOR Africa Branch was able to achieve an improvement in the insurance service expense, reinsurance and insurance service result ratios. However, an overall loss after tax for the year was experienced, with SCOR Africa Branch being the only reinsurer of those surveyed to have experienced a loss in 2023.

Investment performance

Reinsurers achieved an average return on investments (including cash and cash equivalents) of 7.07% (2022: 6.95%), despite the year-on-year increase in investments and cash and cash equivalents of 14%. This is less than the average prime rate of 11.11%[14] (2022: 8.59%[15]) and the average 10-year government bond yield of 10.30%[16] (2022: 10.10%[17]). The investment performance of reinsurers surveyed relative to market returns is indicative of the conservative investment strategies employed considering the industry's exposure to uncertain market forces.

SCOR Africa Branch was the top performer in terms of investment returns in 2023 at 8.6% (2022: 4.4%), followed closely by Munich Re with 8.0% (2022: 8.7%) and Hannover Re with 7.4% (2022: 8.5%). Africa Re achieved a return of 5.0% (2022: 3.7%).

What the future holds for reinsurance operations

In 2023 Fitch Ratings reported that the reinsurance sector outlook was revised to "improving", citing price and claims costs increases, the continued demand for reinsurance, and underwriting limitations as the key drivers, whilst acknowledging the sector's strengthening financial performance into 2024.[18]

The factors noted by Fitch in 2023 are largely reflected in the 2023 results of reinsurers surveyed.

On 5 September 2024 Fitch Ratings released its most recent outlook for the global reinsurance market for 2025: "Fitch Ratings has revised its global reinsurance sector outlook to 'neutral' from **'improving'** as the pricing cycle has most likely passed its peak", the agency says in a new report. Nevertheless, profitability should remain very strong by historical standards in 2025.

Capital buffers and reserve adequacy have strengthened, helped by record profits in 2023 and 1H24, and reinsurers are well positioned for a decline in prices even as claims costs continue to rise and catastrophe losses become more significant due to climate change.

Given the sector's abundance of capital, we expect a moderately softer and more competitive market in 2025, barring significantly above-average loss activity in 2H24. However, underlying margins are likely to remain close to their 2023-2024 peak as reinsurers maintain their underwriting discipline. Fitch forecasts the sector's calendar-year combined ratio to be 88% for 2024 and expects its near-term return on equity to be very strong, at close to 20%."[19]

14 https://www.fnb.co.za/rates/LendingRates.html?srsltid=AfmBOopb3jdCgu4APYf_669IYek3r6LAwm2685q8UlesCLqZcYD4tDik

15 https://www.fnb.co.za/rates/LendingRates.html?srsltid=AfmBOopb3jdCgu4APYf_669IYek3r6LAwm2685q8UlesCLqZcYD4tDik

16 https://za.investing.com/rates-bonds/south-africa-10-year-bond-yield-historical-data

17 https://za.investing.com/rates-bonds/south-africa-10-year-bond-yield-historical-data

18 https://www.fitchratings.com/research/insurance/global-reinsurance-sector-outlook-revised-to-improving-07-09-2023

19 https://www.fitchratings.com/research/insurance/global-reinsurance-sector-outlook-revised-to-neutral-05-09-2024#:~:text=However%2C%20underlying%20margins%20are%20likely,%2C%20at%20close%20to%2020%25.

KPMG

Earlier this year in June 2024, AM Best revised its outlook for the global reinsurance market from "stable" to **"positive"**, citing "robust profit margins along with higher attachment points and tighter terms and conditions that followed a period of drastic repricing." It went on to further note that "despite reinsurance rate increases decelerating, underwriting discipline is being maintained and profit margins remain healthy enough to absorb higher loss activity than recently experienced."[20]

While hardened reinsurance renewals rates continued into 2024, South African reinsurers can be expected to continue with a cautious approach as they move into the 2025 underwriting cycle. A key common theme coming out of the international rating agency announcements is the maintenance of stringent and conservative underwriting disciplines by reinsurers, regardless of the direction in which premium rates might unfold.

Reflecting on the risk landscape within which reinsurers were operating in over the past year, little has changed; from the instability brought on by local political uncertainty, infrastructure challenges, and a vulnerable and volatile civil sentiment, to geopolitical dynamics and climate change pressures. While the financial results for 2023 reflect a continued recovery from 2022, if we have learnt anything over the last few years it is that risk exposures in unprecedented and unexpected ways and forms are lurking around the corner. In a state of continuous uncertainty, constant vigilance is non-negotiable.

Employing agile operating models, continuous assessment of the risk landscape and innovative product offerings are key imperatives for reinsurers to be able to maintain and gain a competitive edge, whilst at the at same time protecting their balance sheets.

The stability provided by the reinsurance industry to the wider financial eco-system cannot be underestimated. As we have seen time and time again, no matter what the future might hold, reinsurers are seen as the cornerstone in maintaining the resilience of the insurance industry.

[20] https://www.icmif.org/news_story/am-best-revises-outlook-for-global-reinsurance-industry-to-positive-with-publication-of-new-market-segment-outlook/