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INSURANCE SECTOR EDUCATION
AND TRAINING AUTHORITY

LEARNER GUIDE

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Analyse new developments reported in the media that could impact on Short Term Insurance

Introduction

This Module is intended to promote general knowledge and understanding of current affairs in the field of Short Term Insurance in order to ensure knowledgeable and informed workers in the industry. It addresses a broad base of Short Term and risk management related knowledge and requires the analysis of current affairs as they could impact on premiums and risk. It requires learners to make connections between the Short Term insurance sector and current events that could impact on the industry. It provides the opportunity for learners to integrate knowledge learnt in the other Modules and current events as they occur so that they begin to apply their knowledge of the industry in authentic situations. The focus is on prediction and anticipation of events rather than on historical research after the event.

Module 1

Current affairs in Short Term Insurance

This Module deals with:

- Significant or controversial issues related to Short Term insurance and views expressed and substantiated in plain language.
- Articles on Legislation that could change the Short Term insurance sector and suggestions as to the potential impact on the sub sector.
- Current events in the socio political environment interpreted and indication of their possible impact on Short Term insurance.
- International socio political events that could impact on reinsurance analysed to identify the potential effect on the South African Short Term insurance sub sector.

1.1 Insurance and society

As events in the Social Environment occur, the insurance industry is faced with a need to act positively to deal with the outcomes of such events. New underwriting criteria are set, reinsurance needs are more closely realised, risk control becomes more important, and product offerings are amended to provide cover that relies on the principles of insurance in terms of potential exposure.

Faced with events in the Social environment, the insurance industry will be affected as follows:

- The financial requirements of insured losses would need to be met, often at great expense and effort by insurers

- Reinsurance protection would be reassessed, perhaps reduced. Acceptance criteria are tightened, and there is a closer watch on rating, risk assessment and the risk management requirements on the part of the insured.
- More intense statistics collection and investigation is implemented.
- Emergency operational requirements are implemented to perform the additional tasks – e.g. temporary staff, mobile claims settling units, customer service lines.
- Survey activities are more closely scrutinised and more rigorously followed.
- Claims history becomes more important to insurers at the risk offering stage.
- Product offerings may be altered; resulting in reduced cover, or even excluded cover.
- Greater market networking takes place, as unified and effective procedures for dealing with future events are implemented.
- More intensive research results, to plan and prepare for future events, and to lessen their impact wherever possible.

1.2 The environment, society and the economy

The economic cycle has been closely associated with various social phenomena. Marriage and divorce rates and the consumption of luxuries vary more or less closely with the economic cycle at the time. Church activities vary somewhat in reverse order. In other words in a down cycle in the economy, more divorces are reported, but more people attend church.

Crime rates also respond to the cycle, but in several different ways, depending on the nature of the crime. There is a measurable relationship between economic cycles and the cycle's observable in nature, particularly the more severe ones such as weather and sunspots. Weather cycles with alternations stressing favourable and unfavourable crop years, extending over periods ranging from a decade to a generation, have been noted.

•Economic Cycles:

Economic cycles are alternations of business activity from peaks of prosperity or booms, to the low points of depressions. Business activity in booms, measured chiefly by productive activity commonly rises as high as 15% above the general average of current business. Depressions sink to 20% and more below. Economic cycles generally last four an average of five years, but generally vary from one to twelve years. An economic cycle is closely related to the expansion and contraction of money, and its substitute, credit. During the nineteenth century under the leadership of Britain, gold became the sole monetary standard of leading nations. In effect, the dollar, pound, franc and mark were merely comparable weights of gold.

•The Great Depression:

The most outstanding characteristic of the boom that had preceded the depression of 1929 to 1939 had been an intensification of business activity marked by rises in production and prices. The initiative had been taken by heavy industries related to investments, the stimulus being the anticipation of profits. With the outlook favourable, banks extended credit to finance expansion. Companies then increased production, and created surplus jobs, thus increasing costs. The excess of bank credit jeopardised reserves, and high prices caused an outflow of gold, as businesses bought cheaper goods elsewhere. Consequently, banks were forced to

restrict credit. Businesses contracted and failed, and millions of people became unemployed. The effects of this economic depression were felt throughout the world. It had a major impact on all sectors of the insurance industry, as people were out of work and therefore not earning.

They therefore had nothing to spend, and one of the first areas they cut back on was insurance.

• **Inflation:**

Whenever credit is restricted because it has grown to too large a position, inflation ensues. This manifests itself in rising costs associated with manufacturing and production, transportation, wholesale and retail prices and the general costs of living. While South Africa is rich in mineral reserves, it is a net importer in areas of textiles, manufacture, luxury consumer goods, and industrial machinery.

This means that we are influenced by rising costs overseas, and by the devaluation of the Rand against other currencies, as these imports are payable in the currency of the supplier. This affects the financial stability of companies and individuals, and they look to cut costs. The insurance industry is among the first to feel these effects, as there is an ever-increasing trend for consumers to seek cover chiefly based on the price of the product sought. When inflation rates are low, and the Rand is strong against other currencies, the insurance industry benefits as consumers have more ready cash available. Companies seek the fullest cover available to protect their assets, and individuals spend more on investments to maintain their living standards in the event of economic changes occurring in the future.

• **Retrenchment, restructuring and downsizing:**

Statistics show that companies that exercise the option of retrenchment of staff as a result of rising costs and reductions in profit and turnover never achieve the levels of profit and income that they hoped for. This is because retrenchment is merely one option of dealing with symptoms of a worsening economic cycle. Often service levels have dropped, staff is not adequately trained, prices are set too high, the core business has been diluted by and the company is operating on borrowed money. The effects on the insurance industry are that more people are unemployed, and therefore not financially satisfied, and so less money is available. Fewer purchases are made in the retail, wholesale and manufacturing sectors, so less money is flowing into the economy. Then less is spent, as a knock-on effect, on insurance. In addition, more people out of work are then eligible for unemployment benefits, placing a heavier burden on the State. The cost of services provided by the State is recovered by way of additional taxation, which adds to the cost spiral. One possibly positive feature is that more retrenchment-related products become available for sale, offering support to unemployed people. Such products include lump sum payments to the insured for a limited period following their retrenchment.

• **War, Terrorism and Conflict:**

These events impact on all sub-sectors of the insurance industry. When soldiers are away fighting and trying to survive, and civilians are in shelters or refugee camps they have no ability to make payments or purchase insurance. War risks to property are excluded other than under Life, and Personal Accident policies, and have been severely restricted under Marine and Aviation covers since the attack on the World Trade Centre in September 2001. War in itself obviously has a negative influence on the insurance industry, but during and after the event, there is always much

expansion or rebuilding to be done. This releases money back into the economy, where it is spent on factory works, manufacturing and new and important processes needed for the war or reconstruction effort. In many circumstances, governments fund these projects, but often grants are made or private financing used. These activities lead to an upsurge in the need for insurance risk protection, and consequently more is spent on insurance products.

The effects of terrorism are profound on the insurance industry. In the wake of the attack on the World Trade Centre (WTC):

- Insurance covers previously available, such as terrorism, kidnap and ransom cover were restricted, and premium was increased for this limited cover;
- Previously where ambiguity existed in wordings, these have been refined to be more precise;
- Reinsurance capacities have been reduced, and the costs of reinsurance have risen;
- A greater focus has been placed on the risk assessment process, with acceptance limits and retentions more clearly defined;
- Many companies have been made to pay out vast sums of money as claims, across many lines of business – fire, combined, business interruption and office contents for those companies with offices in WTC; Life, Pensions and Personal Accident for those that lost their lives; motor in respect of vehicles damaged; aviation covers for the aircraft and liability;
- Some insurance companies will not have enough funds to pay, and will be forced into liquidation;
- In addition, the attacks have a marked effect on global travel, with fewer people willing to take risks;
- This has caused a crisis within the travel and associated industries, with carriers forced to close or cut back on operations, and individuals not needing to have travel insurance cover. The risks available to insure have reduced – BA have cut back their fleet, Swissair and Sabena have closed, and other airlines remain in financial difficulty, faced with mounting costs and reduced customer levels;
- The Great Depression and World War II stimulated the demands for economic reform. Laws were implemented to stabilise stock markets, and economic leadership openly assumed responsibility the supply of money with a view to stabilising market economies. The laws were also put into effect that governed such industries as insurance and Financial Services.

• **Political Environment:**

Political events are those that affect the State, or its government, and these events have a wide impact on the insurance industry. Often the insurance industry is nationalised by governments, which means that the government acts as the risk carrier, under the name of a national insurer. Countries in Southern Africa that have nationalised the industry include Lesotho and Swaziland. All countries have legislated regulations that govern the insurance industry; such the Short Term and Long Term Insurance Acts in South Africa.

Political disagreements often lead to wars (see above) but in many instances also lead to the imposition of economic sanctions on a nation that is deemed to follow political ideals that conflict with more powerful nations' ideology. In recent years, these sanctions have affected South Africa and Zimbabwe, Cuba, Iraq, Taiwan, China and others to varying degrees. The impact on the economic environment and

particularly insurance, is that trade curtailments reduce the need for insurance cover, particularly for Marine cover and export and import risks. Conversely, insurance *needs are enlarged*, when carriers are refused overly rights and had to make longer journeys to reach destinations.

Sanctions also affect the economy of the country they are imposed on as a whole. Without international trade opportunities being available, gross revenues are reduced, and these impacts again include the knock-on effect to insurance. Mostly, however the people of the nations are the ones who suffer most. Deprivation, poverty and suffering are increased by these factors



Module 2

Insurance and Technology

This Module deals with:

- New developments in technology and an indication of how the technology could impact on Short Term insurance or improve service delivery.
- The pros and cons of the new technology and the possible impact of the innovation on Short Term insurance explained with reference to the effect on risk.
- Innovations that could reduce or prevent loss and current remedies/strategies for dealing with the same problem.
- The positive and negative aspects of new innovations.
- Information relating to current loss events collected and organised to allow for an analysis of trends.
- Information relating to life threatening events analysed to determine whether the events will potentially affect the rating structure of Short Term insurance.

2.1 The Industrial Revolution

The most vital change in work related activities was from the Age of Tools to the age of Machines. The steam engine and the power loom broke the slowly dissolving framework of medieval industrial life. The industrial revolution started around 1750 in Europe, with a series of inventions in the textile industry and by the application of steam to the operation of machines. Until 1871 the focus of the revolution was the consolidation of industrialisation.

The main changes wrought by the Industrial Revolution between 1750 and 1871 were in the areas of:

- Textile inventions for spinning and weaving;
- Developments in coal, iron and steel;
- The steam engine;
- The factory system, with the new accent upon machines called for in production;
- Transportation in new road systems, the development of ports, the invention of the railway, and the development of power driven rather than wind driven ships;
- Communication by the use of electricity, the telephone, batteries, and the telegraph;
- Lighting powered by electricity rather than candles and oil;
- Agriculture, when activities and output were increased by means of powered machinery rather than animal and;
- Human effort.

The impact of the industrial revolution on the Social Environment was that now humans were no longer solely required to work for their labour, but needed to become adept at operating machinery. Training and education achieved a higher focus, and the increased number of people no longer able to be employed because machines now did their jobs led to the formation of the first formalised trade union.

New developments in technology, impacting short term insurance recently includes:

- Access to computerised rating systems;
- Systems supporting the prevention of fraud;
- Systems preventing damage or loss;
- Systems enabling smarter rating.

2.2 New Developments in the industry:

We have seen the changes to the industry resulting from a series of mergers and acquisitions of the last several years. In addition to these, there has been a move away from traditional insurance offerings. The following are examples of developments in the industry:

- **The rise of underwriting managers:**

Many companies, including reinsurers have given underwriting authority to expert underwriters in the short-term market. Companies such as Highlander, Covenant Underwriters, SA Underwriting Managers, Hospitality Industry Underwriters, Schools for Africa and many other now write niche and general business on behalf of the sellers. The benefits to the companies are reduced expenditure in administration, and the use of expertise of independent people to write new business for them.

- **INSETA:**

The training and development functions in the industry are formalised under the umbrella of INSETA, to the benefit of the sellers, buyers and brokers.

- **More direct business offerings:**

In certain product lines, insurers have been able to offer more affordable premium rates by dealing direct with the buyers, rather than by means of the intermediary function. This cut the commission costs from the price setting, and the benefits are passed on to the buyer. The negative impact may be that intrinsic expertise levels of the broker are bypassed to the ultimate detriment of the buyer.

- **Reduced Capacity:**

As a result of the attack on the World Trade Centre, many reinsurers have reduced their capacities to insurers in certain classes of business. Certain covers have been withdrawn, such as Kidnap, Ransom and Terrorism, and premiums have been increased.

- **World-wide Programmes:**

As the South African market offers limited capacities, many insured operating here are being forced by their overseas owners to insure under the world wide programme issued in the home country. This results in a loss of premium income to the local market.

- **The growth of Trade Credit insurance:**

The decline of the Rand against other currencies has seen a growth in Trade Credit insurance, whereby the payments by importers are guaranteed by insurers in exchange for premium.

- **The Shrinking of the Construction and Engineering market:**

As a result of the slowdown in the economy, and the low levels of investment return in the property market, development in Construction has slowed. This means not many new projects are undertaken, and the insurance sub-sector suffers as a result.

- **Outsourcing:**

Many organisations have decided to outsource their non-core functions to specialist organisations. These functions include human resources and training, payroll management, audit functions, underwriting agencies, premium collections, information technology, and others.

- **The Virtual Office:**

Several organisations have closed down full branch operations in smaller areas, and have set up a virtual office for one person at their home. These persons, essentially in the marketing functions, service clients and report back via the telephone and e-mail. Policies are issued remotely on line, cutting process and administration costs substantially.

In the past, surveys undertaken of the industry with regard to service levels, professionalism, integrity, rating levels and general feelings about the industry, have derived their opinions in the main from people and organisations within the industry. This information has been in the form of financial stability and claims paying ability, turnaround times, and claims settling activity and general service levels. Information gained from the public has been scarce and it skewed by recent events in the industry. Recent premium increases, or poor claims service may influence these. In a recent independent survey undertaken of 300 'ordinary people' about the state of the industry in the eyes of non-insurance people, the following outcomes were noted:

34% (102 respondents) had no real thoughts one way or the other. Of the remaining 76%, 13% (10 respondents) felt that they received acceptable service and products for their money, and they were satisfied that they were adequately and cost-effectively covered. The remaining 188 respondents gave negative feedback regarding the industry. This feedback was directed at the following problems:

- Poor service levels in general;
- Confusion caused by technical usage in wordings;
- High commission levels for perceived little work done, especially in the life industry;
- Escalating cost of premiums;
- A perception that short term insurers sought ways not to pay claims, rather than being there to protect client's interests;
- The unavailability of mix and match products – I.E. standard covers for everyone;
- The hidden 'small print' in contracts and wordings, such as item limits, the application of average;
- High costs associated with risk protection, such as the fitting or fire and theft protections and vehicle tracking devices and gear locks;
- Being made to feel 'like a criminal' in proving losses;

- The amount of time taken to process routine claims and policy amendments;
- The lack of knowledge apparent at administrative and clerical levels.

The number of claims submitted to the Insurance Ombudsman tends to bear out this vision of the industry, where thousands of claims have been submitted for investigation, because buyers are not satisfied with the companies' stance on the matter. FAIS legislation caused an upheaval in the short term insurance industry. All financial advisors are now by law required to be licensed and to comply with certain basic "fit and proper" requirements with regards training, ethical behaviour and financial management of businesses. Furthermore, the compliance requirements of the FAIS act has spurred a whole new career opportunity: that of the compliance officer. The cost of implementing FAIS will have a negative spin off for the consumer in that insurers will probably re-coup indirectly from policyholders to help fund overhead administration. The positive result of course is the professionalism and improved service levels for consumers.

2.3 Innovations pertaining to crime prevention

Sociologists recognise that poverty, unemployment, the lack of coherent educational systems and other social events impact very strongly on society.

The results are often an increase in crime levels, destruction of the societal unit, and a general change in the norms previously formed in more prosperous societies. Where previously crime was risk to life and property at potentially manageable levels, escalating crime rates in South Africa now affect a vast proportion of the populace.

Statistics gathered show we now have a crime rate amongst the highest in the world. Crimes such as hijacking of vehicles, sexual attacks on children, the carrying of weapons to learning facilities and accompanying violence, rampant corruption in government and protection agencies, occur with regularity. This is in addition to murder and rape, the committing of fraud, theft and housebreaking, family murders and more.

2.4 Insurance protection for crime-related social events

Insurance protection against these events is available in certain products, both life and short term:

- Hijacking is a motor policy peril, freely available but at increased rates, and with a high deductible. Terms are offered generally subject to the installation of an anti-theft device in vehicles. Cover for goods in transit and marine policies cover the cargo on hijacked carriers (ships and vehicles);
- Murder and assault is covered by personal accident and life policies;
- The effects of Fraud can be covered by fidelity insurance, specifically designed to protect commercial enterprises. Unfortunately, risks arising to individuals from dishonest brokers, agents, and other advisers are not. There is a modicum of recourse available through the courts, but pursuing recoveries is often very expensive and time consuming;

- Healthcare benefits are provided to insured persons in the event of Rape, but most victims are from poorer societies. Here cover is not readily affordable and is thus not purchased. Because of the high levels of unemployment in South Africa, (estimated at 44% of people who are available to work) the support of company provided Healthcare benefits is often not there;
- Theft and Housebreaking are insurable perils under theft, all risks and money commercial covers, and household contents, all risks and house owners' policies;
- Corruption: The only possible opportunity for recourse for the private individual is through the legal process, or by means of the electoral process, in voting perpetrators out of office.

The term social environment applies to the human environment and society, including:

- Language;
- Culture ;
- History of peoples;
- Wars;
- Epidemics and disease;
- The impact of political ideals;
- Colonialism;
- The rise of slavery;
- Expansionism and Diaspora;
- Revolution;
- Rapid change to the social environment.

Added to these are so-called human disasters, arising from accidents, explosions, and other events. Throughout history many events have occurred that can be termed as impacting on the social environment. The Economic Environment is made of events that affect the economies of countries, global, international and regional societies, and the individual. Depression and recession in global or national economies, affecting the population at large, as a result of loss of work opportunities, reduced funding for educational facilities, rising costs, the unavailability of basic products, the fragmenting of the luxury goods industries, the reduced need for banks as a tool for savings and investments, the attendant lack of need for insurance products, and the unaffordability of general services and products. Inflation and depreciation of currencies affecting government and its agencies, the import (negatively as goods must be paid for in the currency of the seller) and export industry (positively as goods are sold in the currency of the buyer). Also affected are general consumers, as price increases are the order of the day. Mergers and acquisition of companies, affecting staff and management at the companies involved, in terms of loss of job opportunities, but new opportunities are also created for some. The consumer suffers a reduced choice of carrier, and service levels drop in the immediate aftermath of the merger.

- **Retrenchment, restructuring and downsizing**

This affects all industries in South Africa. Often the first level staff is moved out in the first instance, perhaps on the basis of Last In, First Out, as their number represents the most visible saving area. Key functions will be the least affected.

- **Changes to the cost and method of doing business**

When business increases their reliance on technology, the upshot is often the replacement of people by machines. In the insurance industry, previously essential services such as switchboard operators and typists have been made redundant by voice-mail and direct dialling and software programmes. Effects have also been seen in the post and mail services areas, where e-mail has taken the place of the previously heavy reliance on the postal services. Also, Companies have begun to outsource their non-core functions, such as Human Resources, Training, Salary Services, Auditing, Surveys and Assessment, Fleet Management and Group Benefits functions to specialist organisations. This results in the loss of jobs. Over the last three years, major acquisitions and mergers in the insurance industry have seen some of the following organisations disappear:

- CGU has been absorbed into the Mutual and Federal;
- Allianz has withdrawn from the country;
- The Guardian has been merged with Santam;
- Fedsure has been acquired by Capital Alliance.

The economic effects of these changes include:

- A more limited choice of market for the consumer (the buyer or insured) and the broker;
- A consolidation of business practices resulting in loss of jobs and retrenchments;
- Fewer opportunities for school-leavers wishing to join the industry;
- The first stages of the formation of an insurance cartel, having a more complete hold over industry practices pricing and product offerings;
- Expensive changes to the costs of operations for the companies in transferring data to a unified system, resulting from additional time and training needed to perform this transfer. This results in increased costs to the consumer;
- Increased opportunities for specialist underwriters and brokers to enter the market and offer their services to the consumer;
- A reduction in service levels owing to the increased bureaucracy within organisations.

The negative aspects of these events on the Economic Environment outweigh the positives at the moment, but positives do exist.

In the longer term:

- (i) Higher levels of service will pertain, as organisations streamline their activities, and staff becomes part of the company culture.
- (ii) Capacities are increased, and potential failures of companies are averted. Some of the organisations that have disappeared may not have been able to sustain their results.
- (iii) Ownership of the organisations now lies within powerful groups with demonstrated financial security.

Module 3

The effect that Innovations in Crime and Accident prevention could have on Short Term Insurance

This Module deals with:

- Innovations that could reduce or prevent loss and current remedies/strategies for dealing with the same problem
- The positive and negative aspects of new innovations
- Information relating to current loss events collected and organised to allow for an analysis of trends
- Information relating to life threatening events analysed to determine whether the events will potentially affect the rating structure of Short Term insurance

3.1 Crime and related problems

Sociologists recognise that poverty, unemployment, the lack of coherent educational systems and other social events impact very strongly on society.

The results are often an increase in crime levels, destruction of the societal unit, and a general change in the norms previously formed in more prosperous societies.

Where previously crime was risk to life and property at potentially manageable levels, escalating crime rates in South Africa now affect a vast proportion of the populace. Statistics gathered show we now have a crime rate amongst the highest in the world.

Crimes such as hijacking of vehicles, sexual attacks on children, the carrying of weapons to learning facilities and accompanying violence, rampant corruption in government and protection agencies, occur with regularity.

This is in addition to murder and rape, the committing of fraud, theft and housebreaking, family murders and more.

- **Insurance Protection for Crime-related Social Events:**

Insurance protection against these events is available in certain products, both life and short term

- Hijacking is a motor policy peril, freely available but at increased rates, and with a high deductible. Terms are offered generally subject to the installation of an anti-theft device in vehicles. Cover for goods in transit and marine policies cover the cargo on hijacked carriers (ships and vehicles).
- Murder and assault is covered by personal accident and life policies.
- The effects of Fraud can be covered by fidelity insurance, specifically designed to protect commercial enterprises. Unfortunately, risks arising to individuals from dishonest brokers, agents, and other advisers are not. There is a modicum of recourse available through the courts, but pursuing recoveries is often very expensive and time consuming.
- Healthcare benefits are provided to insured persons in the event of Rape, but most victims are from poorer societies. Here cover is not readily affordable

and is thus not purchased. Because of the high levels of unemployment in South Africa, (estimated at 44% of people who are available to work) the support of company provided Healthcare benefits is often not there.

- Theft and Housebreaking are insurable perils under theft, all risks and money commercial covers, and household contents, all risks and house owners' policies.
- Corruption: The only possible opportunity for recourse for the private individual is through the legal process, or by means of the electoral process, in voting perpetrators out of office.

The term social environment applies to the human environment and society, including:

- Language
- Culture
- History of peoples
- Wars
- Epidemics and disease
- The impact of political ideals
- Colonialism
- The rise of slavery
- Expansionism and Diaspora
- Revolution
- Rapid change to the social environment

Added to these are so-called human disasters, arising from accidents, explosions, and other events.

Throughout history many events have occurred that can be termed as impacting on the social environment:

The Economic Environment is made of events that affect the economies of countries, global, international and regional societies, and the individual.

Events that have an effect on the Economic Environment include:

Depression and recession in global or national economies, affecting the population at large, as a result of loss of work opportunities, reduced funding for educational facilities, rising costs, the unavailability of basic products, the fragmenting of the luxury goods industries, the reduced need for banks as a tool for savings and investments, the attendant lack of need for insurance products, and the unaffordability of general services and products.

Inflation and depreciation of currencies affecting government and its agencies, the import (negatively as goods must be paid for in the currency of the seller) and export industry (positively as goods are sold in the currency of the buyer). Also affected are general consumers, as price increases are the order of the day.

Mergers and acquisition of companies, affecting staff and management at the companies involved, in terms of loss of job opportunities, but new opportunities are

also created for some. The consumer suffers a reduced choice of carrier, and service levels drop in the immediate aftermath of the merger.

Retrenchment, restructuring and downsizing: This affects all industries in South Africa. Often the first level staff is moved out in the first instance, perhaps on the basis of Last In, First Out, as their number represents the most visible saving area. Key functions will be the least affected.

Changes to the cost and method of doing business: When business increases their reliance on technology, the upshot is often the replacement of people by machines. In the insurance industry, previously essential services such as switchboard operators and typists have been made redundant by voice-mail and direct dialling and software programmes.

Effects have also been seen in the **post and mail services areas**, where e-mail has taken the place of the previously heavy reliance on the postal services. Also, Companies have begun to outsource their non-core functions, such as Human Resources, Training, Salary Services, Auditing, Surveys and Assessment, Fleet Management and Group Benefits functions to specialist organisations. This results in the loss of jobs.

Wars, terrorism and conflict: The impact of these is felt across all groups of people and kinds of work.

Changes to or the maintaining of political systems: These affect people and work in the Social and Economic Environments.

Rampant disease or epidemics

Social revolution, or the occurrence of major social events, such as the Industrial Revolution, or the upsurge of HIV/AIDS

Natural evolution or the occurrence of major natural events such as floods or earthquakes

- **Changes to the Economic Environment by mergers or acquisitions in South Africa Affecting the Insurance Industry**

Over the last three years, major acquisitions and mergers in the insurance industry have seen some of the following organisations disappear:

- CGU has been absorbed into the Mutual and Federal
- Allianz has withdrawn from the country
- The Guardian has been merged with Santam
- Fedsure has been acquired by Capital Alliance

The **economic effects** of these changes include:

- A more limited choice of market for the consumer (the buyer or insured) and the broker
- A consolidation of business practices resulting in loss of jobs and retrenchments

- Fewer opportunities for school-leavers wishing to join the industry
- The first stages of the formation of an insurance cartel, having a more complete hold over industry practices pricing and product offerings
- Expensive changes to the costs of operations for the companies in transferring data to a unified system, resulting from additional time and training needed to perform this transfer. This results in increased costs to the consumer.
- Increased opportunities for specialist underwriters and brokers to enter the market and offer their services to the consumer.
- A reduction in service levels owing to the increased bureaucracy within organisations.

The negative aspects of these events on the Economic Environment outweigh the positives at the moment, but positives do exist.

In the longer term:

- (iv) Higher levels of service will pertain, as organisations streamline their activities, and staff becomes part of the company culture.
- (v) Capacities are increased, and potential failures of companies are averted. Some of the organisations that have disappeared may not have been able to sustain their results.
- (vi) Ownership of the organisations now lies within powerful groups with demonstrated financial security.

3.2 Collection of Information

Information regarding the occurrence of events in the economic environment can be gathered from a variety of sources:

- From the **print and radio media** – news broadcasts and newspaper reports and specialist publications such as Financial Times, Business Day, Financies en Tegniek, Finance Week and Business Times and others.
- From the **television media** in the form of news channels and on regular news bulletins
- From **newsgathering agencies** such as Reuters and Associated Press
- From the **community** itself by way of oral and written reports and eyewitness accounts from survivors or others affected by the occurrence
- By general information gathering from **colleagues and friends**
- By use of the **internet**
- From **historical books**, news archive publications and encyclopaedia.
- From **statistics gathering** agencies such as universities and colleges.
- From **government bureaux** such as the Department of Statistics, the Ministry of Finance and the Bureau for Economic Research.
- **Information must be organised to facilitate easy reference.**

This is done by means of protection of the information into a statistical format, using reference and cross-reference points, e.g. by class of event; type of insurance or class; by region, hemisphere or country; date and time; total costs in damages and insurance value; cost of human losses, and relief and salvage operations and cost.

Economic statistics and indicators are used to determine are generally grouped according to whether they lead, coincide with or lag behind the Economic Cycle:

Leaders:

Economic indicators for a leading organisation or industry will show positive measures in the following:

- The average workweek – number of hours typically worked by employees
- Gross hiring or employment costs per 100 employees in an industry
- Value of new orders
- New housing projects undertaken
- Commercial and industrial building contracts undertaken
- Net change in number of operating businesses
- Business failures and aggregate liabilities of organisations
- Corporate profits after tax
- Consumer price indices
- The value of business inventories

The better and more positive these figures are the less the organisation or nation is affected by the Economic cycle – i.e. they remain ahead of the general influence of the cycle.

Co - incident cycles:

Organisations that roughly coincide with the economic cycle will be measured by:

- Unemployment rate per capita
- Gross national product in Rand
- Bank debts across the industry
- Levels of personal income
- The rate of inflation for the industry
- Sales by retail stores
- The consumer price index

Lagging Societies:

Measures and statistics used to determine the lagging group, in other words to determine whether a society is in a lower than current economic cycle, include:

- Expenditures on new plant and equipment
- Salaries costs per unit of output
- Manufacturers' inventories and book value
- Consumer instalment debts outstanding

Module 4

The impact of climate change, disasters and socio economic developments on Short Term Insurance

This Module deals with:

- The impact of climate change on Short Term insurance with reference to the possible influence of these **trends on underwriting practices in South Africa**
- Reasons for natural and other disasters and suggestions are offered to reduce the risk to insurers
- The five most common causes of losses from reports reported in the media
- Events that arise out of socio economic conditions and that could impact on short term insurance from current media
- Possible/predicted disasters in Africa that could impact on South Africa and how these trends could affect Short Term insurance

Since insurance is the method of transferring risk from the insured to the insured, it is important to be aware of occurrences within the Physical Environment that can impact of the insurance industry.

While these events, otherwise known as Natural occurrences can have a devastating effect on people, wildlife and the environment, without the benefit of correctly formulised insurance protection the effects of these occurrences would be much worse

Events in the Physical environment will impact not only on those stated above but also on economic recovery and expenditure, social needs, spending and reforms.

The following naturally occurring phenomena can impact on societies and insurance:

- Fires to buildings, farmlands and other areas of industry and commerce
- Floods arising from heavy rains, tidal waves, and the collapse of dams
- Hurricanes, cyclones, typhoons and other wind storms
- Earthquakes and volcanic eruptions
- Snow storms and avalanches
- Drought and famine
- Freezing or extremely hot weather patterns
- Hailstorms

The effects of these occurrences, when they occur in greater than normal magnitudes, are that the resultant damage often assumes catastrophic proportions.

4.1 Natural events arising in the physical environment that have assumed catastrophic proportions

The flooding to Limpopo Province, Mpumalanga and Mozambique in early 2000 and on for some month major rivers such as the Limpopo and Crocodile burst their banks

causing devastation of crops and farmlands, losses to industry and commerce from damaged or destroyed structures and buildings; losses to thousands of heads of wildlife and livestock; the loss of the lives of hundreds of people.

The Kobe earthquake of 1995 thousands of people died when an earthquake measuring on the Richter scale devastated a highly populous city in Japan, damaging buildings and bridges, and causing massive fires.

Frequent earthquakes in central Southern Asia and Europe (Turkey and Greece)

A snow slide and avalanche that destroyed the Prince of Wales's villa at Klosters in Switzerland and killed his secretary.

The volcanic eruption in the Democratic Republic of Congo in January 2002, resulting in massive damage and loss of life. The lava destroyed whole villages.

A series of hurricanes that have damaged the east coast of the USA, and parts of South East Asia, where they are known as cyclones. To this day, Hurricane Andrew, which struck the south-eastern USA in 1992, remains the most catastrophic of all natural disasters, in terms of total insured damages.

The recent tsunami in the East that caused shockingly high numbers of people dead and caused billions of rands worth of damage. On 26 December 2004 an earthquake caused a tsunami that left billions of dollars of devastation and the tragic loss of lives in its wake. The United Nations estimates that up to 5 million people have been left without food, water, medical attention or basic sanitation and are facing the imminent threat of cholera and typhoid epidemics.

The potential impact of these occurrences on the insurance industry is immense, as there are a number of factors which could require the provision of insurance cover to return the area and people to previously held positions.

Obviously those who have died cannot be recompensed, other than by means of payments to their families or dependants, but the full effects could impact in the following ways:

- Fires, floods, earthquakes, hurricanes or cyclones and hailstorms are insurable perils in South Africa for commercial short-term risks.
- Losses caused by volcanoes and drought are not.
- Loss of life is covered under life and personal accident policies, in respect of all perils arising from the Physical environment, other than the deliberate placing of oneself in danger, or suicide.

It is important to always remember to apply the principle of proximate cause under these covers, as death or injury must arise from a physical accident.

Death by fire under personal accident covers would result in claims being admitted, whereas smoke inhalations may not be.

4.2 Impact on the Insurance Industry:

Apart from the severity of the losses arising from risk in the physical environment, and the associated costs, the occurrences cause the industry to:

- Refocus its underwriting criteria and risk acceptance rules. Where previously risks were not considered as hazardous, underwriters must be aware of the extent of a catastrophic event. Steps must be taken to manage the risk, and to offer solutions to meet the insurance need.
- Be aware of the effects of changing weather patterns, environmental threats and issues such as global warming and its effects on tides, rainfall, deforestation and other meteorological factors.
- Structure more tightly its statistical information, and seek patterns and impacts on frequency and severity of events.
- Inform the insuring public of the effects on the industry and the risks facing them
- Work closely with other organisations, such as government and police, relief agencies and organisations in physical event management and control.
- Ensure that reinsurance protection (Treaty of Facultative) is obtained at a level necessary to deal with losses.
- Arrange appropriate wordings and clauses that clarify covers available and events excluded.
- Inform their partners in the risk transfer – brokers, marketers and other financial institutions of its amended focus.
- Ensure its systems are capable of dealing quickly with the settlement of claims arising – claims, reporting, statistical and networking with other insurers.
- Balance its staff complements with the immediate needs arising from disasters and catastrophes, to ensure speedy and effective assistance to those affected by the occurrences.

4.3 The Effects of Physical Events on the sub-sectors of the industry

In each of the sub-sectors of the industry (see above *Impact on the insurance industry*), the following would arise:

- The financial requirements of insured losses would need to be met, often at great expense and effort by insurers
- Reinsurance protection would be reassessed, perhaps reduced.
- Acceptance criteria are tightened, and there is a closer watch on rating, risk assessment and the risk management requirements on the part of the insured.
- More intense statistics collection and investigation is implemented.
- Emergency operational requirements are implemented to perform the additional tasks – e.g. temporary staff, mobile claims settling units, customer service lines.
- Survey activities are more closely scrutinised and more rigorously followed.
- Claims history becomes more important to insurers at the risk offering stage.
- Product offerings may be altered, resulting in reduced cover, or even excluded cover.
- Greater market networking takes place, as unified and effective procedures

for dealing with future events are implemented.

- Greater and more intensive research results, to plan and prepare for future events, and to lessen their impact wherever possible.

4.4 Epidemics and pandemics

The Black Death:

In the fourteenth century (the 1300's) most of Europe was affected by an outbreak of bubonic plague, transmitted by air, and arising from fleas living on rats. 15 million people died, most during the worst years of the plague between 1347 and 1350. The poor and unsanitary living conditions prevalent at the time assisted the rapid transmission of the disease.

Influenza:

In 1918, during the last year of the First World War, 25 million people died as a result of an influenza outbreak throughout the world. This is 10 million more people than were killed in the First War.

At the time, medical advancement had not reached levels sufficient to provide medication for influenza sufferers. The children's game 'Ring O' Rosie' is based on this event, with the line 'Atishoo! Atishoo! We all fall down!' referring to the stricken sneezing and falling where they stood. Today although antibiotics and other medication manage the disease, no cure has been found.

HIV/AIDS:

The newest and most far-reaching pandemic, caused by a virus that attacks the immune system of sufferers, and transmitted by sexual contact, contaminated blood and drug use, currently affects 100 million people worldwide, most of them in sub-Saharan Africa.

In some areas of Africa the disease has wiped out entire villages and communities. No cure exists, although some drugs have been found to manage the disease.

4.5 War and Conflict:

Over the past seventy years, history records that on *any* given day; somewhere in the world a war was being fought. From the earliest times wars have been constantly fought, arising from geographical conflicts, religious and political, ethnic or racial reasons.

In 1970 the Honduras and El Salvador fought a war over the result of a soccer match.

- The Hundred Years War: This was fought in Europe for 114 years during the early Middle ages.
- World War 1: Between August 1914 and November 1918 most of Europe and some Commonwealth countries, and America were engulfed in the 'Great War.' The conflict arose for a number of reasons, chiefly from territorial demands, but the final incitement is deemed to be the assassination of Archduke Ferdinand

and his wife by a Serbian partisan, Gavrilo Princip) in Sarajevo in the Balkans. By the end of the conflict 15 million people had died, and Europe's political map was changed forever.

- World War II: after a number of territorial conflicts again in Europe, WW II was fought between the Axis powers, (Germany, Italy and Japan) and the Allies (Britain and the Commonwealth, USA, France, Greece, Poland, Scandinavian Countries and others) between September 1939 and August 1945. This was the first time that civilian populations were targeted, and 6 million Jews were killed, countless Poles and more than a million in bombing raids and attacks on cities. The war ended with the dropping of atom bombs on Nagasaki and Hiroshima in Japan in August 1945. During these two events alone, more than 200 000 people were killed.

The rise of Terrorism:

In the late 1960's and early 1970's an old form of political ideology was given a new name – terrorism – when certain political factions added organised violence to their political agendas. Groups of people organised factions to disrupt the ruling classes at the time, and to achieve their political aims.

Groups such as the Red Brigade and Baader-Meinhoff in Germany, ETA in Spain, Black September in some Arab countries and the Red Army in Japan attacked civilian targets.

This effort focused on displaying to the general populace a disregard for personal safety and life to attain political goals. Attacks, which included kidnapping and ransom demands, bombings and hijacking, began to occur with regularity.

- In 1972 8 Israeli athletes were killed during the Munich Olympics
- The Italian Prime Minister, Aldo Moro, was kidnapped and murdered in Italy
- Lod airport in Tel Aviv was bombed and passengers were killed
- An Indian airlines Boeing 747 was blown up off the coast of Ireland, killing all on board
- In December 1988 a Pan American airlines 747 was blown up over the town of Lockerbie in Scotland, killing all on board and several people in the town itself
- On 11th September 2001 hijacked aircraft were crashed into the World Trade Centre and Pentagon, resulting in the deaths of almost 3 000 people.

Ongoing Conflict:

Millions of people have died as a result of ongoing conflict in the world, especially in the Balkan states, Rwanda and Burundi, the Middle East and Cambodia, Vietnam and Korea. There are many others.

Human Disasters:

On April 15, 1912, the luxury liner Titanic on her maiden voyage from Southampton to New York struck an iceberg and sank. More than 1 500 people were lost.

In 1975, two jet airliners collided on the runway at Tenerife, Canary Islands. Over 500 people were killed. This remains the single largest air disaster in history.

On 11th September 2001 four airliners were hijacked in the in the USA and were deliberately brought down – two into the towers of the World Trade Centre and one into the Pentagon, headquarters of the US Military. The fourth crashed into an open field, but it is believed it may have been heading for the White House, centre for the US government and home of the president.

The Trade Centre towers collapsed, resulting in many deaths and massive financial loss. The effects of this event were felt in the Social Environment, but also in the Economic Environment. (See Specific Outcome 3) As a Social event the immediate impact of the attack was war in Afghanistan, where the planners of the event were believed to be in hiding.

Political Disharmony:

Ethnic cleansing, apartheid, tribalism, racial conflict and ideological discord have resulted in countless deaths, and the breakdown of societies.

Religious differences:

Ireland is but one place where religious and political differences resulting in antagonistic conflict have yet to be resolved.

Bibliography

INSETA & IMFUNDO Learning Materials, 2003/8