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Insurance in Emerging Markets: cases from South Africa

The global emerging markets are typically defined as those countries that are in a process of rapid industrialization with higher than average growth rates. These economies are often characterized as intermediate income (i.e. neither low-income nor high-income), exhibiting relatively higher market volatility and within the process of developing infrastructure. Example countries include China, India, Russia, Brazil, Turkey and Mexico – among others. The insurance market in these countries have also exhibited an average growth of approximately 4% since 2021, whereby China alone exhibited a total premium volume of 698 billion USD in 2022[1].

Insurers play an instrumental part in driving economies within emerging markets by mitigating risks, promoting stability and encouraging financial inclusion. Through their assessment of specific needs of individuals in these markets, insurers have a unique opportunity to innovate and incentivize 'good' behavior. Traditional insurance products may not always be suitable in emerging markets due to the cultural and socio-economic context. While purchase triggers for insurance in mature markets often revolve around financial management, in emerging markets, individuals typically purchase insurance out of fear of illness or income protection. This drives insurers to develop innovative products that are tailored to the (somewhat more significant) local needs of the population. Moreover, in markets where governments provide limited support, whether it be for healthcare or loss of income due to illness, for example, insurers play a vital role in filling the gap. Therefore, emerging markets provide abundant and diverse opportunities for insurers.

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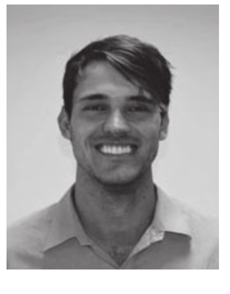

THE SOUTH AFRICAN INSURANCE LANDSCAPE

The South African insurance sector stands as one of the most developed and sophisticated on the African continent. The market encompasses a wide spectrum of offerings, from life and non-life insurance products to a rapidly growing market for low-cost insurance offerings. Insurance penetration (i.e. premiums as a percentage of GDP) is one of the highest in the world – amounting to approximately 14% in 2020[2]. While the large formal insurers dominate the majority of the urban and traditional markets, the complex socio-economic landscape has led to the emergence of micro-insurance solutions tailored towards the inclusion of more individuals into the insured population. Furthermore, the industry has been a breeding ground for innovation, with health incentive programs like Discovery's Vitality reshaping the global discourse around wellness and insurance and the pioneering of critical illness cover. However, the sector is not without challenges. Regulatory complexities relating to the formalization of informal providers serving a growing demand, countering claims fraud, and the need for continuous adaptation to the diverse and evolving South African market requires insurers to remain agile and attuned to the nation's unique socio-economic context and local needs. In this paper, case studies arising from the South African insurance market will be explored.

THE CULTURAL SIGNIFICANCE OF FUNERALS IS AN IMPORTANT DRIVING FACTOR

FUNERAL AND MICRO INSURANCE

Individual funeral expenses cover may not be the main life product in the Netherlands or mature markets in Western Europe, however in South Africa the market has become somewhat of a 'gold mine' in the industry, whereby statistics indicate that in 2021 42% of the total population of 59 million people had funeral cover. In contrast, only 19% of the population is covered by other insurance products[3]. While profit margins range between 3% and 7%, the large volumes of premium underwritten make this a lucrative business[4]. In a nation where a key barrier to the purchase of insurance pertains to affordability, funeral insurance offers an affordable and flexible alternative for much of the low-income population. In addition to affordability, the cultural significance of funerals is an important driving factor behind the popularity of this product as the provision of sophisticated and expensive funerals is fundamental to many South African cultures. A study in a Grahamstown informal settlement found that, for a funeral, the sampled households spent approximately 15 times their average monthly income[5]. Compared globally, funeral costs in South Africa make it the world's fourth most expensive country for dying - after Japan, China and Germany[6]. South Africa is a culturally diverse nation with 11 official languages, and while traditional funeral practices vary across cultures, for many cultures a funeral constitutes a central life-cycle event which is unmatched in importance and costs.

Formal and informal insurance entities (such as Burial Societies) both compete to provide funeral insurance to the public. This is where the introduction of micro-insurance legislation aims to facilitate the formalization of informal providers.

Micro-insurance is a type of insurance mechanism designed to protect low-income individuals and families against specific uncertainties in exchange for regular premium payments proportionate to the likelihood and cost of the risk involved. Various forms of micro-insurance exists internationally and are not limited to funeral insurance. For example, agricultural micro-insurance, which is popular in countries with many small-scale farmers, or credit life cover on consumer goods and micro-loans.

Legislation relating to micro-insurance permits the sale of simplified risk products of limited size targeted at low-income markets. These products create an opportunity for new insurers to enter the market and the development of low-cost risk products. This is achieved by insurers operating under a micro-insurance license as per the Insurance Act. In this way, formal insurers can benefit from lower barriers to entry through less onerous governance and capital requirements compared the intricate regulation imposed on traditional insurers – driven by a dedicated regulatory model tailored to the risk profile of micro-insurers.

An intended outcome of the introduction of micro-insurance products with lower premiums and sums assured is to increase financial inclusion of individuals in the low-income market while providing policyholders with adequate protection in accordance with generally accepted insurance practices.

In addition to licensed insurers, other solutions aim to meet the need for funeral cover in low-income markets like informal Burial Societies. Burial Societies operate under a mutual benefit structure, offering non-guaranteed benefits to its members with limitations regarding the size of benefits payable and membership count.

Beyond formal and informal insurers, banks, telecommunication providers, funeral parlors and even retail outlets have started providing funeral cover. Ultimately making this cover flexible and easy to obtain, with often little to no underwriting. This industry, however, is not without its challenges, including limited underwriting data, fraud and moral hazard. The infamous case of Rosemary Ndlovu highlighted the need for stricter regulation on funeral insurance products, whereby the ex-cop received six life sentences for the murder of her partner and five family members – for whom she each purchased (multiple) funeral and life insurance policies, successfully claiming a total of over R1.4 million (68.4k Euros)[7].

MEDICAL SCHEMES AND CRITICAL ILLNESS

Unlike the Dutch healthcare system, the South African healthcare system is characterized by a large, subsidized and under-resourced public sector (amounting to approximately 400 hospitals and accounting for 48% of expenditures) and a smaller, yet high quality, private sector (amounting to approximately 200 hospitals and accounting for 52% of expenditures). Medical schemes, which vary according to cover, provide access to private healthcare services. While affordability remains a key barrier to this type of insurance, approximately 16% of the population is covered by a medical scheme[8].

Thus far, there has been limited government-intervention for health insurers in South Africa (although the National Health Insurance Bill will ultimately reshape the current healthcare system), providing insurers the opportunity to develop innovative products.

An example of innovation includes that of Discovery Limited's Vitality program, whereby policyholders are rewarded for 'healthy' behaviors such as exercise, healthy eating and seeking preventative care. Vitality members who engaged in the program were found to have up to: 28% lower healthcare costs, 13% lower probabilities of hospitalization and 9% lower mortality rates[9]. This exhibits the role that insurers can play in incentivizing 'good' behaviors through innovation and harnessing behavioral economics.

SUCH INNOVATIONS CAN ALSO BE EXPANDED TO CLAIMS AUTOMATION AND DATA-ORIENTED ARTIFICIAL INTELLIGENCE

Another example pertains to the invention of critical illness cover by Dr Marius Barnard, a cardiac surgeon and brother of Dr Christiaan Barnard who performed the world's first human heart transplant at Groote Schuur Hospital in Cape Town. Dr Marius Barnard saw many of his patients suffer financial hardship following the diagnoses and treatments of critical illnesses. This led to the development of critical illness cover which generally pays out a lump-sum in the case of certain diagnoses or treatments including heart-attack, stroke, cancer and coronary bypass surgery, among an extensive list of others. This product, which is not designed to indemnify the policyholder, can meet a variety of needs e.g. supporting access to medical treatments, funding a change in lifestyle post-treatment or support the change to a lower paying occupation. Since launching in South Africa approximately 40 years ago, critical illness cover has been adopted in markets across the globe from North America to the UK as well as the far east and is widely accepted as the most successful and needed risk product today.

It is evident that where governments may offer limited social benefits such as access to high quality health care (including expensive medical interventions) or income protection, insurers can play a role in filling the gap by developing complex and novel products. Such innovations are not limited to product development and meeting unique local needs, but can also be expanded to other areas of customer-centricity, such as claims automation and data-oriented artificial intelligence.

CONCLUSION

Emerging markets present a wide range of opportunities and challenges for the insurance sector. As illustrated by the intricate landscape of South Africa, the unique socio-economic and cultural dynamics of these countries necessitate tailored solutions that resonate with local realities. The success of specific products, such as funeral insurance in South Africa, exemplifies the broader trend in emerging markets, where understanding and respecting local traditions and norms can reveal considerable potential. Innovations such as health incentive programs and critical illness covers highlight the ability of insurers to not only respond to, but also anticipate the evolving needs of their clientele.

THESE MARKETS ENCOURAGE INSURERS

Actuaries operating in these markets play an influential role in advocating for regulatory governance and consideration of policyholder reasonable expectations when driving the design or marketing of complex products to avoid leaving consumers vulnerable to abuse. The strategic competencies that actuaries bring are also recognized in the high proportion of actuaries occupying commercial and Executive roles with a shared goal of placing customers at the forefront of lifelong wellbeing and financial protection.

While navigating these markets often means confronting challenges like regulatory hurdles, potential fraud, and diverse consumer behaviors, the rewards are evident. Moreover, many of these markets remain untapped. For global insurance providers, the narratives from emerging markets underline the pivotal role of flexibility, innovation, and cultural attunement. These markets encourage insurers with the promise of not only business growth, but also the opportunity to make a significant socio-economic impact, fostering both financial inclusion and resilience. In this perspective, the clear focus on risk management and governance in mature markets, as well as role definitions among first, second and even 3rd line actuaries will also shed lights to the emerging markets. ■

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