49TH AIO CONFERENCE AND ANNUAL GENERAL ASSEMBLY
27 to 31 MAY 2023, HOTEL EL AURASSI – ALGIERS, ALGERIA

THEME: “THE CONTRIBUTION OF INSURANCE TO FOOD SECURITY CHALLENGES IN AFRICA”

Round Table Supervisory Authorities - AIO EXCOM Members Strategies for Increasing Retention Levels in Africa

31st May 2023
Algiers, Algeria
Presented by

Dr. Ben Kajwang , **PhD, ACII(UK), AIRM(UK), FIIU, FIIK, CPT, Chartered Insurer, Risk Mgt. Consultant,**
Chief Executive Officer - College of Insurance, Nairobi, President of the African Insurance Organisation

Agenda

1. Introduction - Facts and Figures About Africa in 2020
2. AIO Study on the Transfer of Premium Offshore (By PwC)
3. Transfer of Premium Offshore
4. Retention and Illicit Financial Flows (IFF)
5. African Premium Retention Frameworks
6. Reasons for Transfer of Premiums
7. Strategic Considerations for Interventions
8. Effects of Externalization
9. Conclusion

African Insurance Organisation Study on the Transfer of Insurance Premiums Offshore

This AIO study was conducted by PwC South Africa in September 2016.

Quote

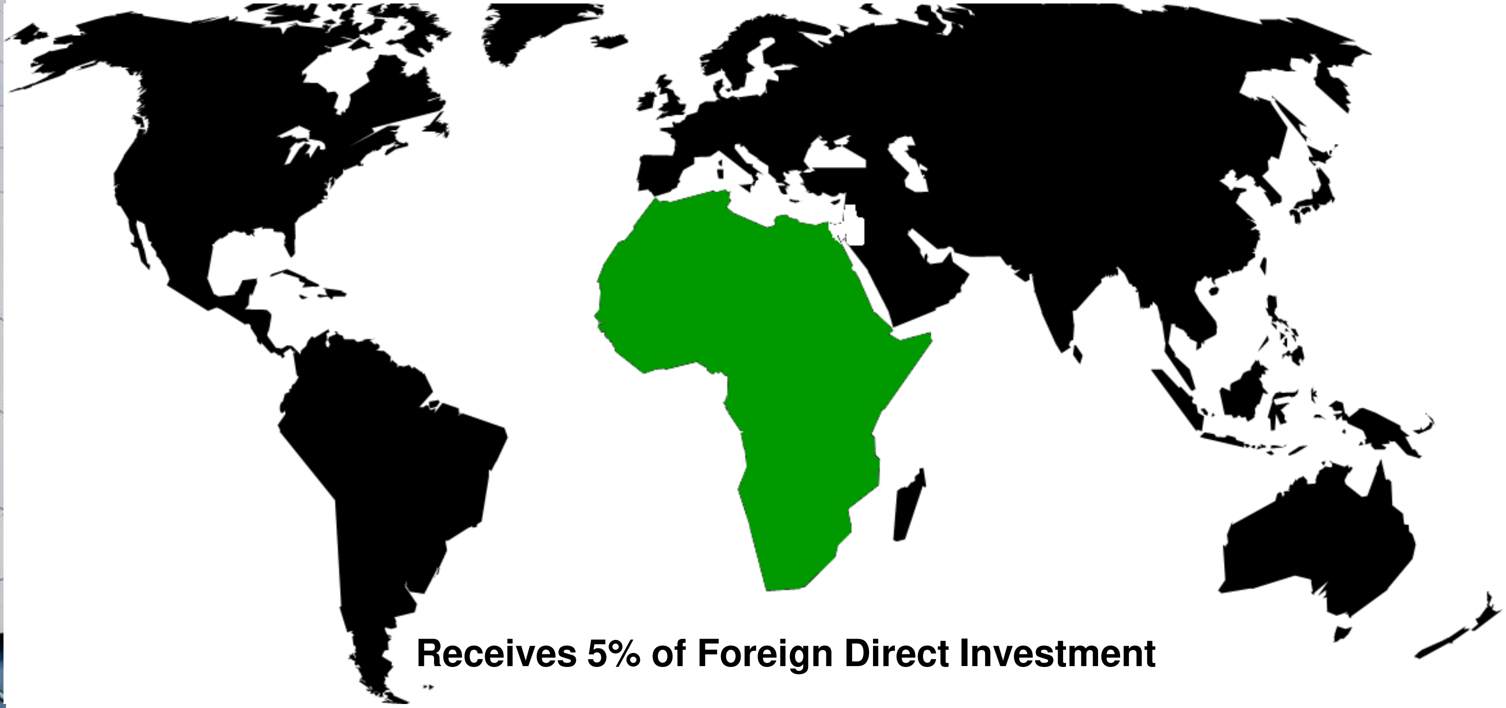
“There are risks and costs to a program of action. But they are far less than the long-range risks and costs of comfortable inaction.”

John Fitzgerald Kennedy

Facts and Figures About Africa in 2020

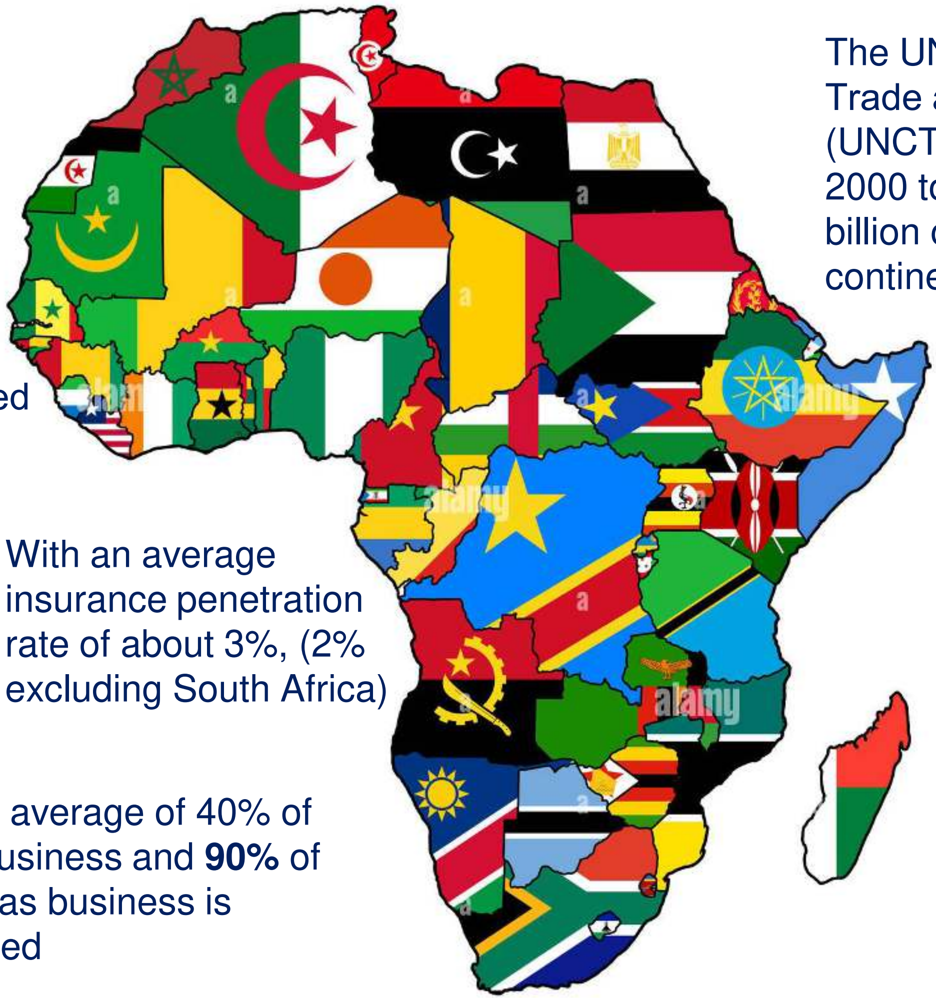
Contributes 3% of world GDP

5% of world trade



Represents 1% of global insurance

Receives 5% of Foreign Direct Investment



The UN Conference on Trade and Development's (UNCTAD) reports that from 2000 to 2015, roughly $836 billion capital left the African continent.

Africa's combined total insurance premium was $81bn.

With an average insurance penetration rate of about 3%, (2% excluding South Africa)

An average of $88.6 billion each year (UN Economic Development in Africa Report 2020).

Of this an average of 40% of general business and **90%** of Oil and Gas business is externalized

FIGURE 1: Total capital flight from 30 African countries by decade (billion, 2018 $)

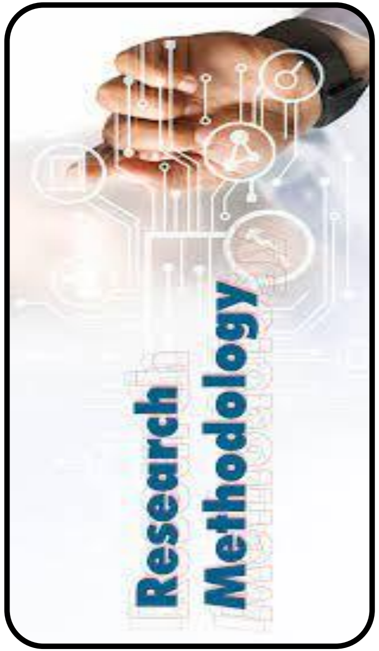
Source: Authors' computations.

AIO Study on the Transfer of Premium Offshore (By PwC) Objectives

- Why transfer of premiums offshore is an issue
- The key reasons put forward for the transfer of premiums offshore
- The key interventions to encourage local retention and reduce offshore transfers
- Strategic considerations for implementing the identified interventions.
- The quantum of insurance premiums transferred outside of Africa, with a focus on Africa’s largest insurance markets and those markets experiencing high levels of Foreign Direct Investment
- The characteristics of African insurance markets that result in the transfer of premiums offshore.

Research Methodology

Investigation Methodology



The structure of the research process necessitated a number of steps before the requisite knowledge and information had been gathered.

- **Desktop research** of current information related to insurance premium flight, and potential legislative attempts at curbing this flight, and the development of a brief literature review on this topic.
- A continental survey developed in consultation with the AIO that was distributed to all the AIO's members.
- **Interviews** were conducted with a broad range of the AIO's members, including insurers, reinsurers, brokers, insurance regulators and industry associations.
- These were conducted in the following eleven countries: **Angola, Egypt, Ghana, Kenya, Mauritius, Morocco, Mozambique, Nigeria, South Africa, Tanzania, Uganda**

Transfer of Premium Offshore

The extent of offshore premium transfer was investigated under two broad categorisations

Type 1:

Offshore premium transfers - after the initial insurance placement in country (where the risk originates) with local insurer through one of the below.

- Cross border reinsurance (i.e. direct offshore transfer of reinsurance premiums);
- Inter-group reinsurance; or,
- Reinsurance with a local reinsurer but subsequent retrocession to a foreign reinsurer.

Type 2:

Offshore premium transfer – due to risks being insured directly offshore through one of the below:

- Direct offshore insurance with a foreign insurance company
- Direct offshore insurance with a foreign reinsurance company
- No formal insurance paid for by the local risk-taking entity, however, profits are paid to (usually through dividends) foreign companies and a portion of the profits are used to provide for insurance with a foreign insurance entity below.

Transfer of Premium Offshore

At the time of the study, estimates from the Swiss Re Sigma report placed the total size of gross written premium (GWP) in Africa at $72bn in 2013 (split into $50bn of life insurance premiums and $22bn of non-life premiums).

Where the Swiss Re Sigma report did not have the required premium figures, the Africa Re Insurance Regulation Directory was used.

Table 2.1 – African Country Insurance Premiums in 2013

Country	Population ('m)	GDP (USD 'bn)	GWP - Life ('m)	GWP - Non-Life ('m)
South Africa	53	366	44,556	9,565
Morocco	32	104	1,023	2,157
Ghana	25	48	168	269
Egypt	79	272	773	1,051
Uganda	35	21	20	140
Tanzania	49	33	30	260
Kenya	44	53	439	1,000
Nigeria	174	522	403	1,406
Angola	22	124	50	948
Mauritius	1	12	463	212
Total	515	1,556	47,925	17,008
Africa Total	**1,111**	**2,390**	**49,939**	**22,485**

Breakdown of premiums across the major African countries

Table 2.2: Life and non-life insurance total gross written premium in 2013

Country	Life insurance		Non-life insurance	
	Gross Premiums Written (USD m)	Net Premiums Written (USD m)	Gross Premiums Written (USD m)	Net Premiums Written (USD m)
Angola	50	17	948	531
Egypt	773	742	1,051	493
Ghana	168	168	269	199
Kenya	439	411	1,000	690
Mauritius	463	359	212	129
South Africa	44,556	34,515	9,565	7,336
Tanzania	30	30	260	130
Zimbabwe	269	264	209	110

Summary of split between life and non-life sectors where appropriate data were available

Swiss Re Sigma report "World insurance in 2013: "steering towards recovery"

Transfer of Premium Offshore

Table 2.3: Life insurance transfers

Country	Life transfer ($m)	Total life premiums ($m)	Proportion of African life market
South Africa	1,146	44,556	89%
Morocco	69	1,023	2%
Egypt	56	773	2%
Nigeria	26	403	1%
Kenya	2	439	1%
Total	**1,299**	**47,194**	**95%**

Table 2.4: Non-life insurance transfers

Country	Non-life transfer ($m)	Total non-life premiums ($m)	Proportion of African non-life market
South Africa	1,800	9,565	43%
Morocco	147	2,157	10%
Egypt	480	1,051	5%
Nigeria	291	1,406	6%
Kenya	275	1,000	4%
Total	**2,993**	**15,179**	**68%**

The tables above are then used in order to estimate the size of the offshore premium transfer for the remainder of the continent.

- The two tables estimate the insurance premiums that remain in the key African countries and, by implication, the level of expatriation. It is important to consider that some level of offshore transfer occurs through direct placements of the risks overseas and is not captured in tables 2.3 and 2.4 but is rather estimated separately thereafter. These tables include figures that were developed by the regulators of these countries, and were confirmed in our discussions with these regulators.
- Tables 2.3 & 2.4 are then used in order to estimate the size of the offshore premium transfer for the remainder of the continent
- Mid-range estimate (type 1)
- Extrapolating the figures to give an Africa-wide premium transfer estimate gives:
  - Total life insurance transfer offshore as $1.37bn, and
  - Total non-life insurance transfer offshore as $4.4bn.
  - The 2013 mid-range estimate of the total premium transfer from Africa is therefore in the region of $5.8bn.
  - The majority of the insurance markets have been included in the above estimation, and it would not be expected that there would be significant changes to the experience for the remainder of the market.

Retention and Illicit Financial Flows (IFF) – A Comparison

Africa loses about US$88.6 billion, 3.7 per cent of its gross domestic product (GDP), annually in illicit financial flows. The High-Level Panel on International Financial Accountability, Transparency and Integrity for Achieving the 2030 Agenda (Financial Accountability, Transparency and Integrity, FACTI Panel) report released in February 2021 cautions that IFFs — from trade mis invoicing, tax abuse, cross-border corruption, and transnational financial crime — drain resources from sustainable development, as well as worsen inequalities, fuel instability, undermine governance, and damage public trust.

UN Conference on Trade and Development (UNCTAD), Economic Development in Africa Report 2020

Overall financial leakage estimate $192b

Ben Ohio - B.Sc. in Artificial Intelligence, Anglia Ruskin University

Retention and Illicit Financial Flows (IFF)

- A 2015 joint United Nations and the African Union report on the value of Illicit Financial Flows (IFF) lost by Africa put the value of the total annual transfer of funds at $60bn.
    - This was updated to a value of between $80bn -$90bn in 2016.
    - This value included numerous sources, of which insurance premiums were not identified separately.
    - These flows included laundering criminal proceeds, corruption, tax abuse and market abuse, and thus are applicable to industries that go beyond only insurance.
    - It was said that two thirds of this total was due to commercial companies, and one third to criminal activities.

Illicit Financial Flows (IFFs) originates mostly from commercial activities as follows:

$ 60 bn

Currently, Africa is estimated to be losing more than $50 billion annually in IFFs.

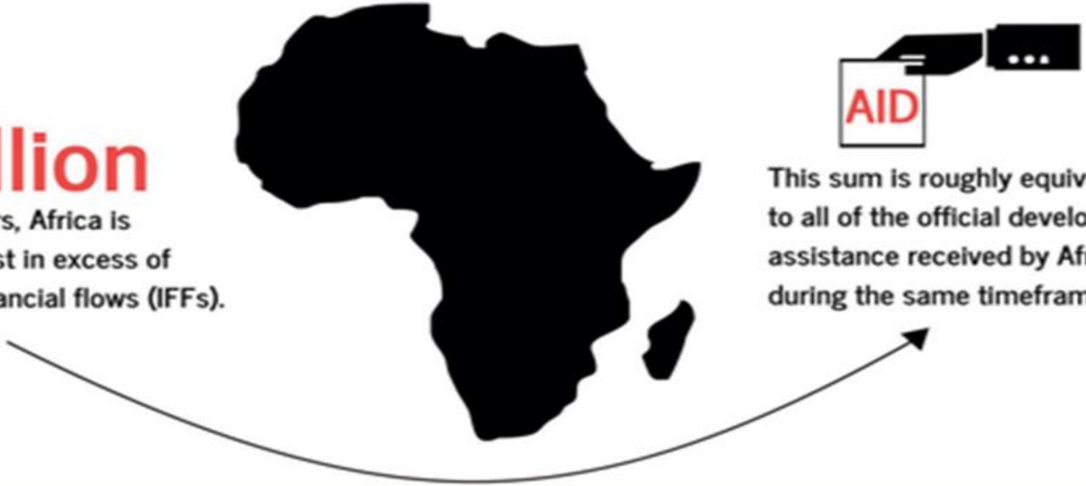
65% Commercial Transaction

30% Organized Criminal Activities

5% Corruption

$1 trillion

Over the last 50 years, Africa is estimated to have lost in excess of $1 trillion in illicit financial flows (IFFs).



This sum is roughly equivalent to all of the official development assistance received by Africa during the same timeframe.

African Premium Retention Frameworks

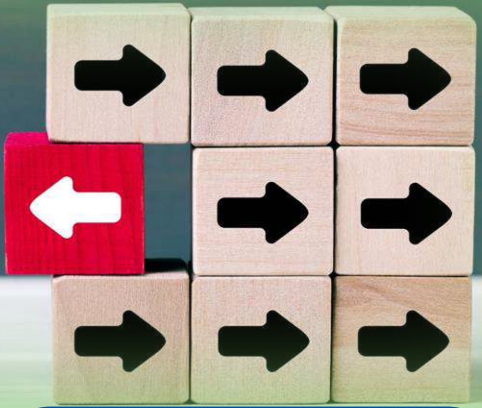
Regulators in most African countries have indicated their awareness of the risk of unnecessary transfer of premiums offshore. African countries have adopted premium retention frameworks that aim to ensure that only necessary offshore premium transfer occurs.

Typical frameworks aim to cover the following at a minimum:

- The requirement that all domestic insurance business be conducted with locally licensed insurers;
- The requirement that reinsurance arrangements and plans be approved by the regulator;
- The exhaustion of local capacity before any insurance or reinsurance can be placed offshore;
- Compulsory cessions to insurance pools, national reinsurers or a regional reinsurer where it exists; and,
- 5% cessions on all treaty business to Africa Re are also applied where a country is a signatory to this accord.

Importance of Retaining Premiums

The AIO has identified the expatriation of premiums as a potential cause inhibiting the growth of African insurance markets.



There is recognition that some transfer of premiums offshore is necessary in the conduct of insurance business.

Insurance relies on the concept of spreading risks. Global placements of insurance and reinsurance can achieve the spreading of risks across various geographies thereby reducing concentration of risk on the African continent

Reasons for Transfer of Premiums

Lack of local capacity amongst local underwriters

Lack of adequate security from local underwriters

The role of global programmes

Role of intra-group operations

Lack of technical skill

Lack of suitable products in local markets

Role of relationships

Price considerations

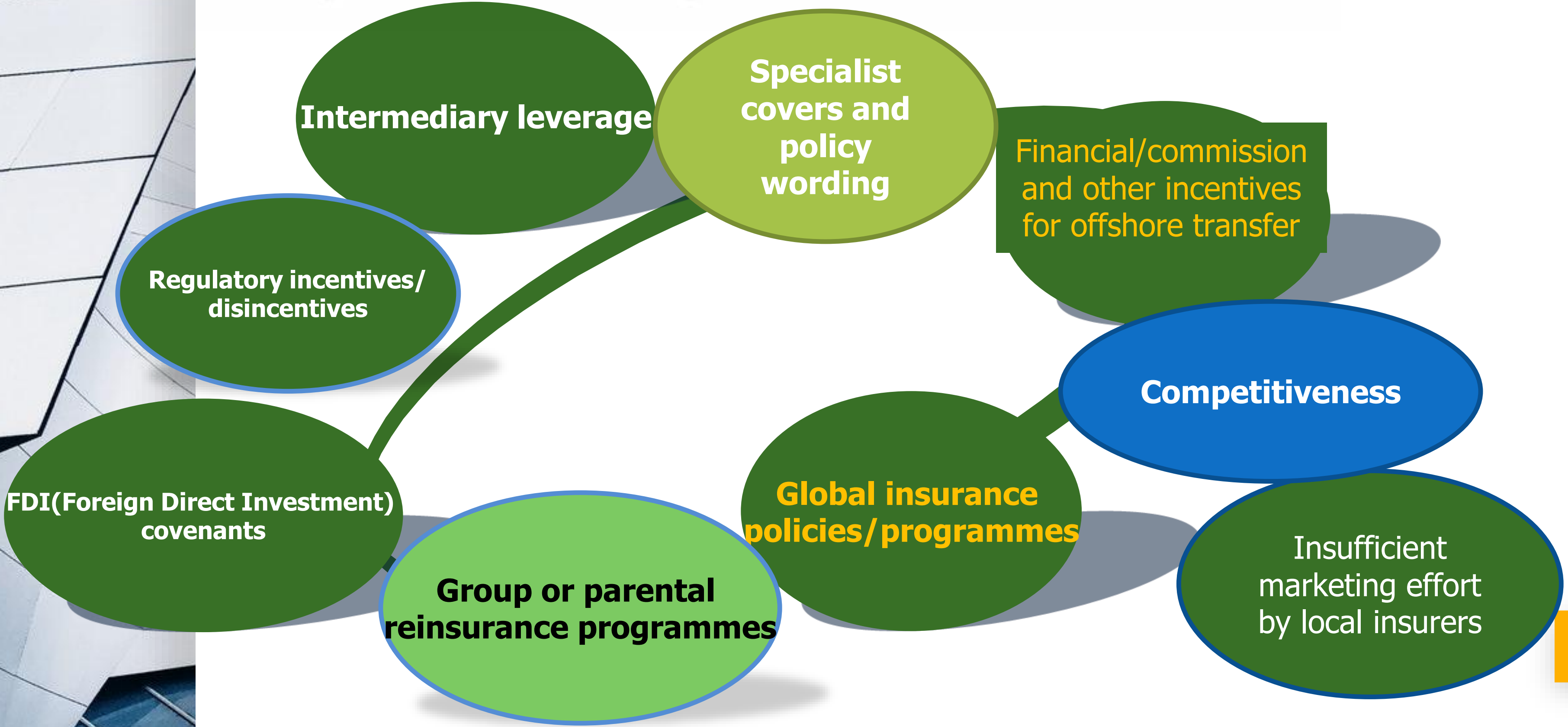
Lack of awareness of the existence of some of the above factors

The influences of the above generic insurance/economic factors are amplified by the capitalist/free market approach generally adopted by market participants in Africa.

These factors vary in different countries.

Reasons for Transfer of Premiums (Cont'd)

Examples of sub-themes put forward include the effects of:



Offshore Transfer of Premium – Pros & Cons

African Insurance Organisation

Necessary Transfer of Premium Offshore

The necessary transfer of premiums offshore occurs where the local market is restricted and when:

- there is limited capacity to underwrite the risks locally;
- certain risks fall outside risk appetite parameters of local underwriters; or,
- there is a need to diversify in order to prevent the concentration of risks in local markets.

Other considerations for the transfer of premiums offshore may include:

- better premiums or pricing;
- improved security and a willingness and ability to pay claims by foreign underwriters; or,
- improved service and customer experience.

Unnecessary Transfer of Premium Offshore

Transfer of premiums offshore is unnecessary if the risks could have been underwritten locally but are not written, due to reasons unrelated to insurance. Examples include:

- profit transfer arrangements in multi-national groups where 'expenses' are described as insurance;
- pure fronting arrangements where local companies are set up solely as a channel for premiums to foreign countries;
- instructions or policy under a global programme of a foreign direct investor;
- premium subsidisation under global arrangements;
- instruction or policy of sponsor including Government, cell captive, foreign direct investor or contractor; and,
- where there is no desire to promote the local insurance industry by the insured.

APART FROM THE AIO STUDY ON THE TRANSFER OF PREMIUM OFFSHORE, NO OTHER STUDY HAS BEEN DEVOTED TO THIS TOPIC WITH A FOCUS ON THE INSURANCE SECTOR

Strategic Considerations for Interventions

African Insurance Organisation

key considerations for each intervention type

Table 6.1 Types of market intervention

Intervention	Relative direct/ implementation cost	Relative benefit	Relative financial stability risk	Timeline for implementation
Market conduct	Low	Low	Medium	Short
Market development	Medium	High	Low	Long
Prudential supervision	Medium	High	Low	Medium
Supervisory restriction	High	High	High	Long

Swiss Re Sigma report "World insurance in 2013: "steering towards recovery"

The impact of any interventions should be assessed with consideration to the following four key factors:

- the risks to financial system stability;
- the cost of insurance to society, including the impact on the local competitive landscape;
- the benefits of insurance to society; and,
- the time needed to achieve anticipated benefits.

Intervention Types

The intervention types have been grouped according to four key themes

African Insurance Organisation

The market conduct required to reduce the unnecessary transfer of premiums offshore

- reciprocal inter and intra-African exchange of business;
- AIO partnerships;
- standard policy wordings;
- Consolidation of reinsurance purchases;
- reinsurance optimisation;
- international partnerships;
- industry intervention through associations;
- enhancing management capacity; and,
- efficient capital allocation.

1

The market development measures that can be implemented

- promotion of fewer but stronger insurance companies;
- affirmative action leading to localisation requirements;
- policy of government insurances;
- government led strategies to grow the insurance sector;
- market disclosure of reinsurance arrangements;
- building of regional capacity; and,
- education and skills enhancement.

2

The prudential supervisory measures that can be implemented

- risk-based capital structures.
- evaluation of the application of ratings.
- strengthening of the structural insurance framework.
- analysis of earnings.
- analysis of asset quality.
- analysis of capital adequacy.
- analysis of actuarial reserves; and,
- tightening of licence renewal process.

3

Intervention Types (Cont'd.)

African Insurance Organisation

Supervisory Restrictions and Incentives.

- -directives to insure locally;
- -exhaustion of local capacity' legislation;
- -promotion of mechanisms for co-insurance;
- -allowance of direct inward reinsurance by insurers;
- -prohibition of reinsurance outside the local market;
- -compulsory reinsurance cessions;
- -injunction of subsidiaries in global programmes;
- -localisation requirements for management and shareholding; and,
- -Regulatory capital and/or tax advantages to local retention.

4

From boxes 1,2,3 & 4…

Country in conjunction with local/regional market players to develop…

A. Strengthen their local market;
B. Remove loopholes in existing regulation;
C. Promote and incentivise local market retention
D. Manage the appropriate outcomes through regulation

Four strategic pillars to be addressed

A. Market development
B. Market conduct
C. Prudential supervision
D. Supervisory restrictions

Strategies to Increase Retention

Supervisory	Underwriters	Policyholders
Supervisory, being through the International Association of Insurance Supervisors (IAIS), Association of African Insurance Supervisory Authorities (AAISA) and the various National Insurance Supervisors who are able to implement intervention mainly via policy formulation, implementation and monitoring.	Underwriters, both applicable to insurance and reinsurance, including their national, regional and continental associations and forums. Intervention will be mainly via capacity building and increases in risk appetite	Policyholders, including intermediaries who often act in the interest of the policyholder. Intervention will mainly involve increasing the will from multinationals, captives, financiers and government who are all key potential buyers of insurance to improve local, African retention

The AIO will need to balance the advantages, disadvantages and risks involved in considering the various strategies for intervention. The degree of control and influence by the AIO and its members diminishes as the interventions move from supervisory to policyholder. It is therefore difficult to prescribe behaviour at a policyholder level.

African Insurance Organisation

Effects of Externalisation

Be it premium flight or capital flight on the broader scale, these leakages come at a heavy cost in terms of poverty reduction and public investment in health care, education, water and sanitation. It undermines domestic resource mobilization by eroding the tax base. *(Boyce, J. K. and Ndikumana, L. On the Trail of Capital Flight from Africa: The Takers and the Enablers, (2015).*

Capital flight exceeds capital inflows reducing African’s net worth.

Wealth from capital flight from 1970 to 2018 for thirty countries was $2.4 trillion. More than their external debt of $720 billion. A‘net credit’ of $1.6 tn. Political Economic Research institute (PERI, 2021)

The figures indicate that if Africa retains its resources it will not need aid, and the rest of the world would be owing Africa, not the other way round

“Countries with high levels of capital flight have historically devoted less to health care and education on a per capita basis” (PERI, 2021)

Nigeria, South Africa and Angola are Africa’s first, second and third countries with the biggest outflows of capital flight in sub-Saharan Africa. *(Boyce, J. K. and Ndikumana, L., Magnitude and Mechanisms of Capital Flight from Angola, Cote d’Ivoire and South Africa, University of Massachusetts-Amherst 2019).*

Effects of Externalisation

- Reduced income tax base for local countries;
- Reduced investment or developmental funds from insurance savings;
- Pressure on limited foreign exchange reserves and depreciation of the local currency;
- Reduced jobs and enterprise creation;
- Reduced opportunity to create local insurance skills;
- Reduced ability to grow local economies; and,
- Reduced ability to protect African policyholders if insurance outside of the approved regulatory framework prevails.

Effects of Externalisation (Cont'd.)

African Insurance Organisation

Be it Premium Flight or Externalization…

Capital flight exceeds capital inflows reducing companies net worth	Business does not replace what they loss to international market and therefore stagnating their growth	Africa remains dependent on international insurance products and do not provide real insurance solutions to our markets	Externalization takes away from the industry hard currency funds Africa lacks	The continent is left without support and or pay for risk that not from our markets as shown by the example of COVID and Sept 11

GOVERNMENTS' RESPONSE

- Set up local Insurance and Reinsurance companies, Sub-regional Reinsurance Companies and African Reinsurance Corporation.
- Strengthen regulatory requirements of the industry
- Increase the capital requirements of (Re)insurance companies to retain more. Example; CIMA $5.5M, Nigeria $13.5m.

Conclusion

Retention of insurance premiums in Africa should be viewed in the context of Africa's development story and strategy.

The end goal of any intervention would be to strengthen the local insurance industry and create an industry that is viable in the long run.

An approach which sets Africa on the development path to achieving insurers that can insure Africa's risks in a financially independent manner should be promoted.

The primary aim of the intervention must be the long term creation of strong insurance markets underpinned by resilient and efficient domestic insurance and reinsurance institutions.

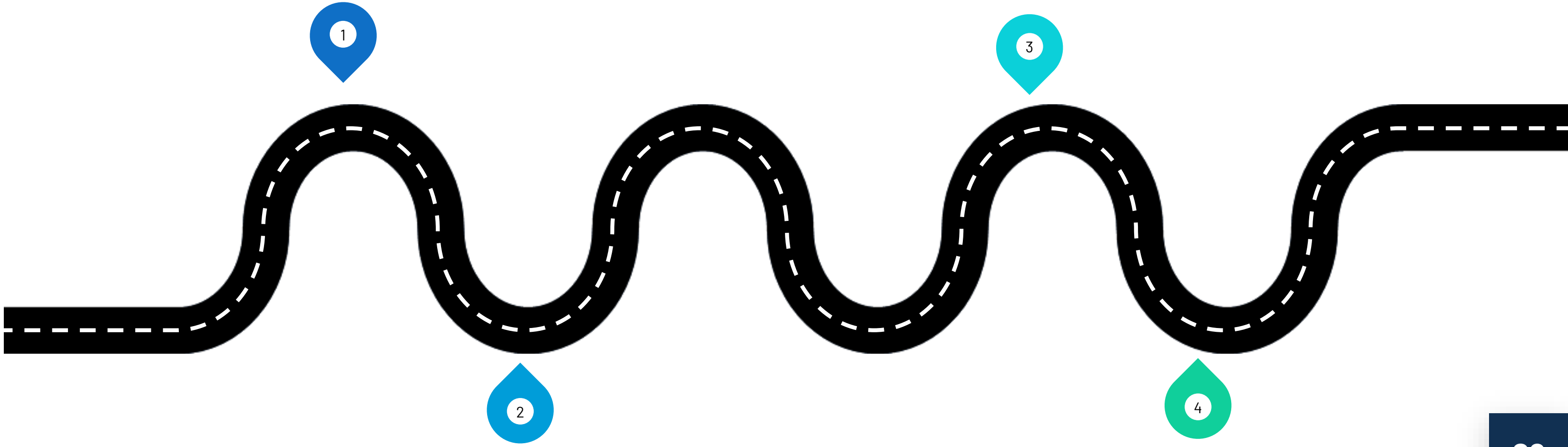
It is only strong African underwriters that can capitalise on the rapidly growing demand for insurance services in Africa and reduce the transfer of insurance premiums offshore.

Conclusion .. Cont

We recommend that each country, based on the assessment of necessary and unnecessary offshore transfers, develops a programme in conjunction with local and regional market players to:

Strengthen their local market;

Promote and incentivize local market retention;

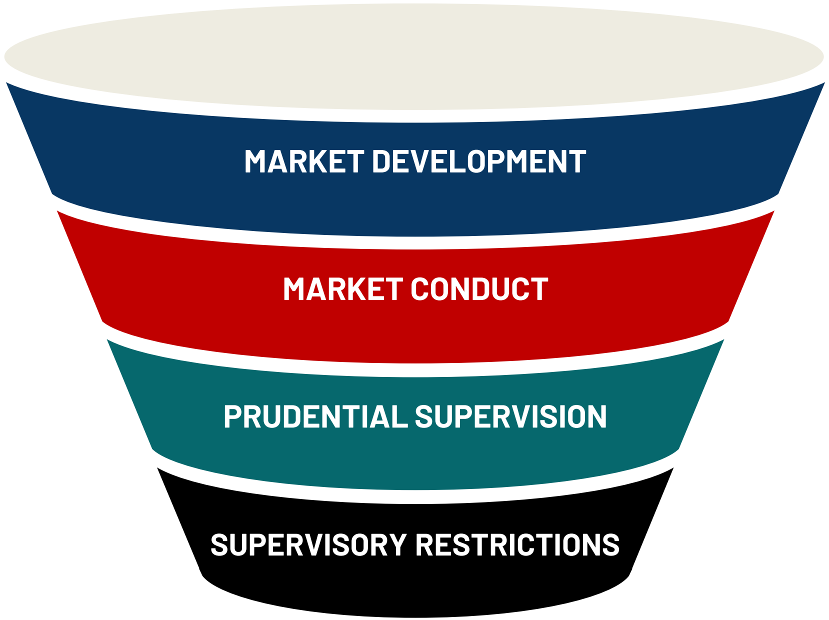


Remove loopholes in existing regulation;

Manage the appropriate outcomes through regulation.

Conclusion .. Cont

- The above can be achieved by adopting a programme that simultaneously addresses the following four strategic pillars:



"The greatest challenges humans face through out their lives are two:

1. ***the challenge of where to start***
2. ***the challenge of when to stop."***

Sameh Elsayed

Thank you/Merci !

African Insurance Organisation