Brighton NEWSLETTER
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Editor's Note

Necessity is the mother of all invention and innovation. The last 3 years have shown that the insurance industry can innovate and evolve when called upon.

From a global pandemic to the economic fallout from the Russia-Ukraine conflict and highest inflation in 40 years; the industry has shown remarkable flexibility and resilience in overcoming them.

But as we approach year-end, 2023 is set to be yet another year of uncertainty and macroeconomic turbulence. In our feature article on the insurance outlook, we present 5 key trends to watch out for in the coming year.

Whilst the common denominator in 2022 has been uncertainty, resilience will be the overarching theme for 2023. The article on global recession describes 2022 as a permacrisis year, which is a term that defines "an extended period of instability and uncertainty".

With the threat of a global recession hangs over the world, the insurance industry is poised for a revolution of rapid innovation and lead the way on climate change resiliency.

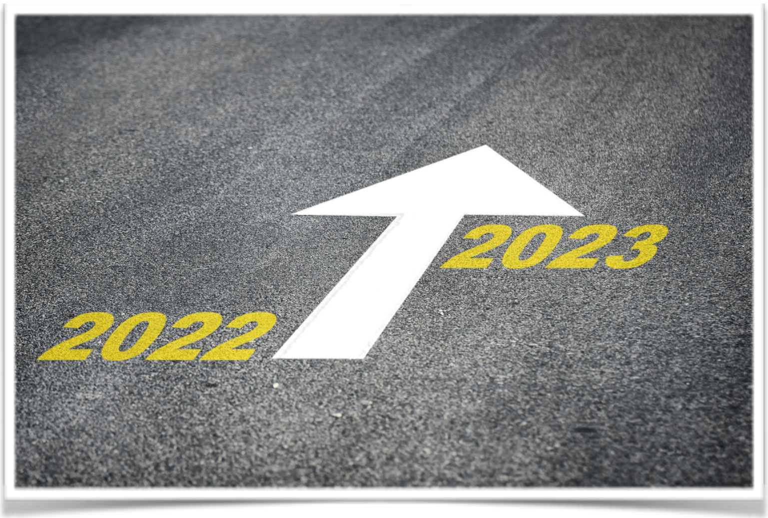
As I write this editorial note, I am reminded of the old Persian adage, 'this too shall pass…', and the industry must be prepared to take advantage of opportunities as they arise.

Annie Undikai,
Managing Director

Insurance Outlook 2023: The Year Ahead

The global insurance industry's development in 2022 has been marked by the massive economic fallout from Russia's invasion of Ukraine, rising inflation, natural catastrophe losses and market turmoils. Although the industry fared relatively well in 2022, some risks still lie ahead.

With global recession looming in the horizon, economic conditions could become more challenging heading into 2023. According to the Global Economic & Insurance Market Outlook 2023/24 by Swiss Re Institute, macroeconomic turbulence will continue to present hurdles for the industry, with inflation remains as the number one macro risk.[1] The report highlighted that although GDP growth has been resilient this year, inflationary recession is on the cards in a number of advanced economies.



1 https://www.swissre.com/institute/research/sigma-research/sigma-2022-06.html

Global inflation is forecasted to rise to 7.5% by year end; driven by food, fuel, energy, and supply chain disruption.[2] With rising inflation expected to persist over 2023, insurers face rising costs for claims payouts and increased operating costs.

However, a silver lining to the inflation crisis is higher interest rates by central banks to curb accelerating inflation. After years of ultra-low interest rates and slashed to near-zero to support the economy through the pandemic; an era of rising interest rates bodes well for the insurance industry. High interest rates boost investment returns that will help offset the higher claims they are liable for.

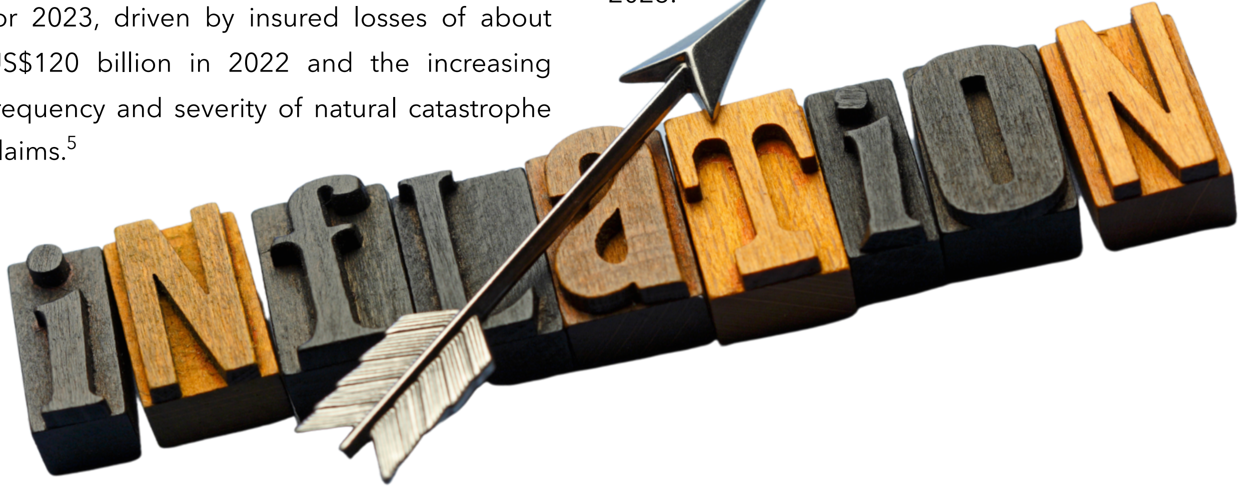
In the face of rising inflation, surging insurance claims and looming global recession; further rate hardening is expected in 2023.[3] According to Moody's Investor Service, the year 2023 will also see rapid price increases within the reinsurance market, primarily in the property and casualty (P&C) lines.[4]

In terms of property catastrophe cover, Fitch expects double-digit premium rate increase for 2023, driven by insured losses of about US$120 billion in 2022 and the increasing frequency and severity of natural catastrophe claims.[5]

Mergers and acquisitions (M&A) in the global insurance industry reached the highest growth rate for 10 years in the first half of 2022,[6] but recorded a decline in both deal value and volume in the third quarter of the year by 85% and 6%, respectively.[7] However, continued geopolitical instability and economic uncertainties are expected to further slow down M&A activities in 2023.

Climate change and cyber risks are once again listed as the most pressing threats for insurers in the coming year. Cyber insurance costs increased by 102% in the first quarter of 2022 and this momentum is expected to continue in 2023 as demand for cyber insurance remains high.

The effects of climate change will continue to play out as the frequency and severity of natural catastrophe intensifies. Insured losses from natural catastrophes have increased 250% in the last 30 years. In the first half of 2022, floods and storms drove global insured catastrophe losses of US$38 billion and this trend towards more frequent and costlier natural disasters is expected to continue in 2023.



2 https://www.globaldata.com/media/business-fundamentals/global-inflation-forecast-rise-7-5-end-2022-driven-food-fuel-energy-supply-chain-disruption-observes-globaldata/

3 https://www.swissre.com/institute/research/sigma-research/sigma-2022-06.html

4 https://www.artemis.bm/news/reinsurance-buyers-expect-rapid-price-rises-in-2023-moodys/

5 https://www.insurancejournal.com/news/international/2022/11/23/696447.htm

6 https://www.actuarialpost.co.uk/downloads/cat_1/CLYDE%20&%20CO%20-%20Insurance%20Mid%20Year%20Growth%20Report%202022%20FINAL.pdf

7 https://www.globaldata.com/store/report/insurance-industry-m-and-a-deals-by-theme-quarterly-analysis/

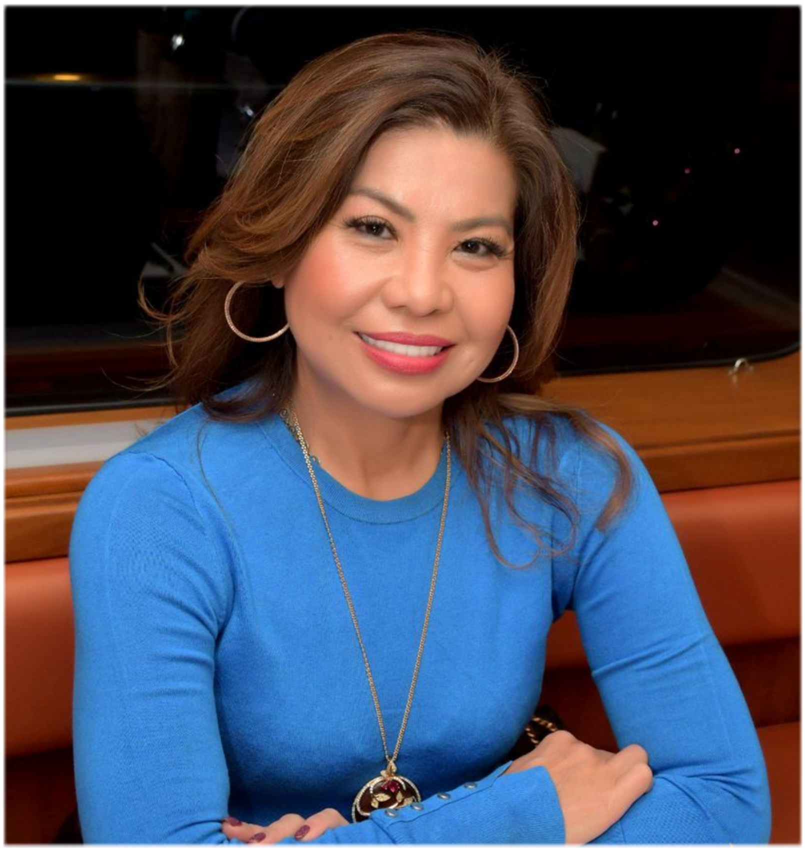
A conversation with...

Annie Undikai

Founder & Group Managing Director, Brighton International Group

Unlocking The Power Of Captives In Asia

What is your assessment of the captive insurance landscape in Asia Pacific over the last few years, amid the pandemic and the current global economy?



While the Asia Pacific captive market accounts for only 3% of captives globally, it is seeing considerable growth and interest, particularly post-pandemic. In the face of geopolitical instability and adverse macroeconomic conditions, businesses in the region are taking on a more critical look at their approach to risk management. In fact, we are seeing a rise in the level of enquiries we have received in the last two years or so.

In the past, captives were most common in large companies and industries such as financial services, healthcare, and manufacturing. Under the current economic situation of rising inflation and interest rates as well as the looming global recession, many other companies and industries are considering captive structures as a viable option as they discover how captives can provide innovative ways to assert better control over their costs of doing business. A captive can offer more premium stability, an improved risk management strategy, access to reinsurance, as well as cost savings. Within the last two years, the captive markets in the region have seen significant increases not only in the numbers of captives being formed; but also the broadening range of covers that existing captives provides as well as an increase in the use of cells within the protected cell captives (PCC) structure.

What do you see as the new and emerging risk trends in Asia? What roles can captives play in covering these risks?

Emerging risks are continuously evolving at a pace never seen before. The new emerging risks landscape that has emerged means that organisations need to be agile and innovative in the way they approach risk. Top emerging risks to look out for are climate change, cyber risks, geopolitical risks and global supply chain.

The captive market has a leading role to play in propelling the shift in the risk landscape and ensuring stability in a hard market. We expect to see more companies expanding their use of captive insurance beyond providing cover for traditional property and liability risks, to include coverage of non-traditional classes of risk, such as cyber risk and climate change risk.

What examples of innovation are you seeing in the use of captives to cover emerging risks?

Emerging risks such as climate change and cyber threats will continue to play a significant role in the formation and expansion of captives because captives are by default, designed to provide cover for such hard-to-place risks.

This momentum will continue in 2023 in tandem with the hardening of the insurance and reinsurance markets, with business owners looking for alternative risk transfer solutions that could provide better cost efficiencies, as well as flexible solutions in managing their risks.

With heightened emerging risks from cyber attacks, we have also seen captives are being utilised as a strategic tool to provide cyber coverage. Cyber risk modelling is naturally improving as more data becomes available.

With cyber risks being ranked as the top 3 emerging risks to the global economy by the World Economic Forum, we can expect demand for captive cyber insurance to grow and become a critical element of a company's risk management strategy.

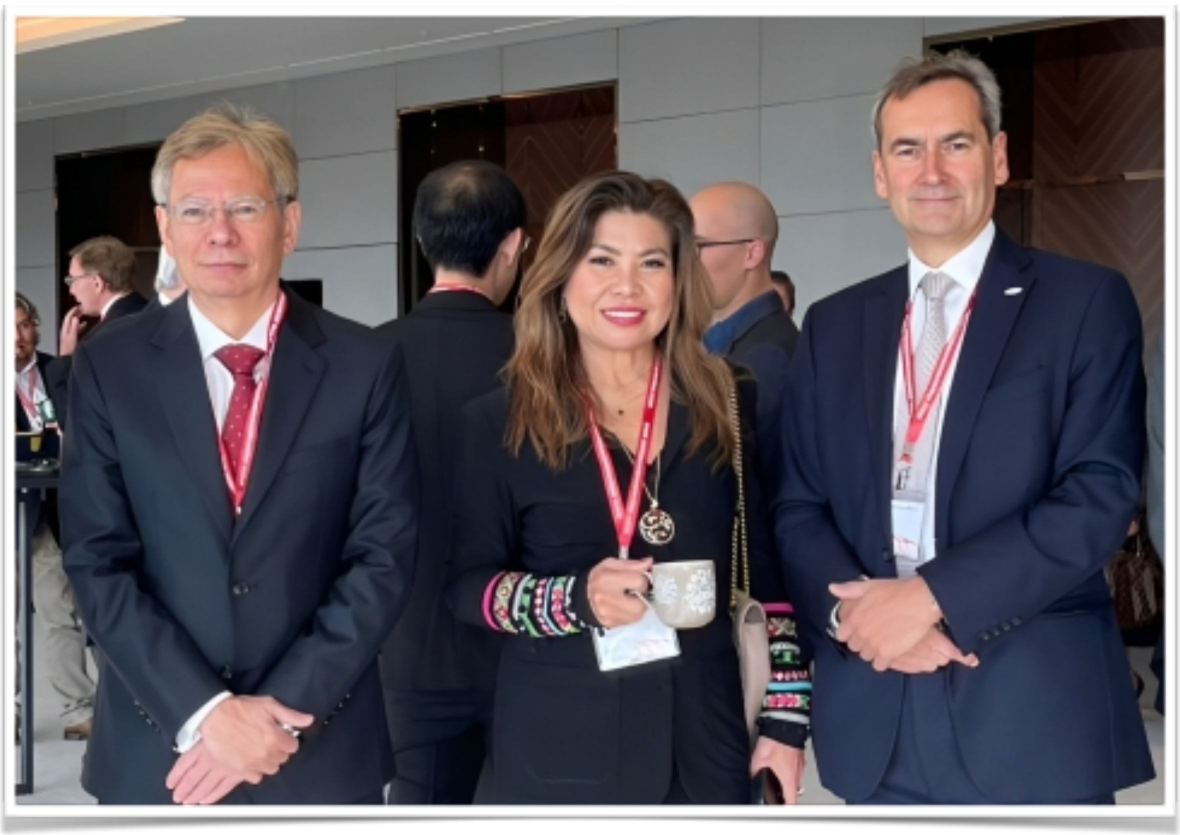
It is also likely that the captive industry will see ESG themes and principles integrated further into the captive strategy, especially concerning the assessment of retained risk and investment strategy. For example, captives surpluses can also be used to fund environmental projects or invest in green bonds, which are financial instruments that support projects that have a positive effect on the environment.

Earlier you mentioned that there is growing interest in cell captives in recent years. What is driving this growth?

Interest in cell captives has been mainly attributed to the hardening market, which continued to gain momentum post-pandemic. What makes cell captives appealing from a cost-efficient perspective is the ease of implementation and lower operating costs compared to a pure or standalone captive. This feature has attracted the interest of companies seeking an alternative risk management solution, but without the costs or commitment associated with a standalone captive. In fact, in a survey conducted by Labuan IBFC and Captive Review, 76% of respondents said that cell companies could be a suitable solution for Asian risk.

A popular cell captive structure is the Protected Cell Company or PCC. Under this structure, assets and liabilities of each cell are segregated and ring-fenced from each other. The flexibility inherent in a PCC facilitates the delivery of tailor-made risk programmes to suit the cell owner's specific needs. In Labuan IBFC, the creation of a PCC has been made relatively easy as it does not require the approval of the regulator (Labuan FSA), merely a notification within 14 days after the establishment of the cell is required.

Growth in cell captives is also driven by the increasing need to re/insure against new and emerging risks; ranging from cyber risks, climate change, and supply chain risks. Cell captives are well suited for emerging risks that are categorised as high severity but low frequency. Given the many benefits and increase awareness of cell captives, the growing interest in cell captives is expected to continue in the years ahead.



Is The Economic Headwinds Blowing Towards A Global Recession?

The year 2022 can at best be described as a permacrisis year, as economic recovery post-pandemic is being gravely shaken. The global economic growth is predicted to slow further in 2023 as the war in Ukraine rages on with no end in sight coupled with rising inflation fuelled by global supply chain disruptions cloud economic growth outlook. The International Monetary Fund (IMF) predicts global growth will slow down from 3.2% this year to 2.7% in 2023;[1] whilst the World Bank has lowered its 2023 global growth forecast from 3% to 1.9%.[2]

However, the World Bank warns that as central banks across the world simultaneously hike interest rates to curb inflation, the risk of a global recession is on the rise. This is due mainly to three major reasons: the big global economies are slowing down, inflation is speeding up, and the world's global order is fragmenting.[2]

Economic growth in the US, China, and Europe – the three major engines of global growth, is slowing down simultaneously. This is going to dampen the demand for exports from emerging markets and consequently will have a trickle down effect on Asia's growth.

Soaring food and energy costs have fuelled the highest rates of inflation since the 1980s, and this is set to continue in 2023 according to the head of the European Central Bank (ECB), Christine Lagarde. She warns that inflation in Europe is set to increase further, as the ECB is likely to raise interest rate further in order to tame inflation.[3]

However, according to The Conference Board Global Economic Outlook 2023, a global recession may be avoided, but the world will probably experience notably below-trend growth of 2.1% in the coming year.[4] Looking beyond 2023, the report further highlighted that the global economy is expected return to a trend of slow growth relative to the pre-pandemic pace.

[1] https://www.imf.org/en/Blogs/Articles/2022/11/13/slowing-global-economic-growth-is-increasingly-evident-high-frequency-data-show

[2] https://www.worldbank.org/en/news/press-release/2022/06/07/stagflation-risk-rises-amid-sharp-slowdown-in-growth-energy-markets

[3] https://www.pbs.org/newshour/economy/inflation-in-europe-likely-to-increase-more-interest-rate-hikes-likely-warns-central-bank-president

[4] https://www.conference-board.org/topics/global-economic-outlook/2023-global-recession-fears-resurface-risks-mount