SUBMISSION TO THE JOINT HEARING OF THE STANDING AND SELECT COMMITTEES ON FINANCE ON THE FISCAL FRAMEWORK AND REVENUE PROPOSALS

Date of submission:	**26 February 2019**
Contact person:	**Pamela Ramagaga** **Executive Manager**
Contact details:	**E-mail: pamela@saia.co.za** **Tel: (011) 726 5381** **PO Box 5098, Weltevreden Park, 1715**
Type of stakeholder:	**A Non-life Insurance Industry representative body**
Submitted to:	**Mr A Wicomb: awicomb@parliament.gov.za** **Mr Z Rento: zrento@parliament.gov.za**

Contents

1. Introduction

The South African Insurance Association (SAIA) welcomes the opportunity to make this submission to the Standing and Select Committees of Parliament on the fiscal framework and revenue proposals put forward by the Minister of Finance, the Hon Mr Tito Mboweni, in his budget speech of 20 February 2019.

2. About SAIA

The SAIA is the industry association for the non-life insurance industry (NLII). In the NLII, there are 74 insurance companies (there are a greater number of insurance licenses, as 1 company may have more than 1 license). The make-up of the NLII is:

- 6 state owned insurance companies.
- 14 captive insurers, they only insure assets of their holding companies.
- 31 companies offer products in only 1 or 2 segments of insurance.
- 36 companies offer products in 3 or more segments of insurance.
- 7 companies offer products across all segments.

The market share of the largest six (6) NLII companies is 56% and the largest ten (10) companies is 66%.

Because of the nature of non-life insurance policies, insurers are required to hold most of their assets in liquid investments. The industry had domestic assets of R135 billion as at 31/12/2015, of which 37% was held in cash and deposits (Financial Services Board, 2015) and provides insurance cover of trillions of Rands

3. The Role of the Non-Life Insurance Industry in the Economy

The non-life insurance industry provides policies of insurance against losses covering a wide range of items including building and related content, motor cars, personal effects, liability etc, impacting the entire economy.

The NLII allows those who participate in the economy to produce goods and services without fear that adverse incidents may leave them destitute or unable to recover. The absence of insurance in an economy would make investment difficult. For instance, it becomes challenging to attract investment without the surety of an insurance policy behind the transaction. Therefore, the NLII enables access to credit from financial institutions, therefore should for instance motor insurance not be provided for in South Africa, the culminating effect would be felt in both the financial institutions and the motor trade sector. This could have a catastrophic effect to the number of people dependent on these sectors for jobs, given the numbers employed in both sectors.

The NLII is therefore the grease which ensures that the economy functions successfully, as it enables businesses and individuals to manage their risks and insure their risks by transferring them to the NLII who manages, diversifies and absorbs respective insurable risks.

4. SAIA Comments on the Fiscal and Revenue Proposals and Request to the Standing and Select Committees of Finance

In relation to the fiscal and revenue proposals contained in the Budget Speech and associated documents, the SAIA wishes to draw attention to the Minister of Finance, the Hon Mr Tito Mboweni's announcement in relation to the agricultural sector, in which he stated:

> *We are supporting private sector investments in agriculture by emerging farmers. R1.8 billion is allocated for the implementation of 262 priority land-reform projects over the next three years. R3.7 billion is set aside to assist emerging farmers seeking to acquire land to farm.*

The SAIA welcomes the priority given to promoting investment in the agriculture sector. However, we believe that maximising the potential of the agricultural sector to contribute to the growth of the economy cannot only rely solely on essential support for emerging farmers, but also needs to nurture commercial farming, which has seen great challenges in recent years. We crucially believe that essential support to investment by both emerging farmers and commercial agriculture could be significantly enhanced if access to Multiperil Crop Insurance (MPCI) could be improved, especially considering the tremendous challenges faced by the agricultural sector as a whole because of climatic factors and specifically because of drought.

Mindful of its direct employment and broader growth multipliers to the economy, the SAIA has more than a decade ago already started work on a proposal for a public-private project to provide subsidised MPCI to farmers in South Africa to support investment in both emerging and commercial agriculture despite rising climatic and other crop risks. **Considering government's renewed focus on supporting agriculture, both as expressed by his Excellency, the President of the Republic of South Africa Mr Cyril Ramaphosa, as well as by the Minister of Finance in the Budget speech, we wish to again raise the proposal for the provision of subsidised MPCI to primary agriculture as well as subsidised index insurance premiums for emerging farmers. Index Insurance is a more affordable form of insurance.We therefore humbly request that the Standing and Select Committees of Finance recommend to National Treasury to engage with the NLII as represented by SAIA, to consider allocation for it in future iterations of South Africa's National Budget.**

Subsidised insurance makes it also possible for commercial and emerging farmers to access finance and thereby growing their own businesses. Therefore contributing to growth and jobs.

5. Brief Background on the Agriculture Insurance Discussion with Government

More than ten (10) years ago, the South African Insurance Association (SAIA) approached the National Treasury (NT) and Department of Agriculture, Forestry and Fisheries (DAFF) for premium subsidy for the Multiperil Crop Insurance (MPCI), currently offered to commercial farmers in South Africa, specifically for drought insurance.

The primary reason for the premium subsidy is to make MPCI more affordable for

commercial farmers and allow for more commercial farmers to take up the necessary insurance therefore ensure their future sustainability.

Another reason for approaching the government for the premium subsidy for MPCI, is because it is becoming difficult to insure as some reinsurers are not willing to insure it due to the high risk, and if insuring it, it is very expensive. And, because the cost of insuring it is high, too few commercial farmers are using the MPCI for protection.

The government agreed to look at the requested premium subsidy or financial contribution towards reinsuring MPCI (drought only) for commercial farmers but requested a crop and livestock insurance product offering for emerging farmers (drought and hail only), for which a premium subsidy would also be considered. To drive this two-pronged initiative, the SAIA Agricultural Insurance Project was created in collaboration with NT and DAFF to further both product offerings for premium subsidies.

Given that the emerging farmer index insurance product offering does not currently exist in South Africa, the first step was to create it. Therefore, the current focus, even though both product offerings are equally important, is to create the new product as both must exist for the government to consider the premium subsidies.

6. Status update on the two-pronged initiative

The project continues to gain momentum at an increased pace in the last two to three years. Tasks and responsibilities are such that, the Agriculture Steering Committee (ASC) has requested SAIA to explore the prospect of appointing a project manager to oversee the project. The current ASC is made up of participating SAIA members, NT, DAFF, SASRIA, Land Bank Insurance Company (LBIC), World Bank, Prudential Authority (PA) and the Financial Services Conduct Authority (FSCA). The ASC has recently authorised for further stakeholders to be included, given the progress made on the project.

<u>Milestones achieved thus far are:</u>

- Memorandum of Understanding from our participating insurance and reinsurance members, who have spent time and money to create the opportunity in creating this insurance solution.
- Research scope has been done providing for the two economic scenarios, with and without the premium subsidies on the South African economy.

For the MPCI:

- Research scope has been done to investigate the commercial farmer insurance gaps, to feed into the submission to be made to NT for the MPCI premium subsidy.

For the new product type:

- Research has been completed in terms of understanding the emerging farmer profile and where they are and what they farm as primary information to create a product offering for them.

- The new insurance product offering for emerging farmers, has been found, it is an Index Insurance Product (IIP). This product type allows it to operate at a lower cost base than MPCI, which is envisioned will make it more affordable for emerging farmers.
- Research work and training in creating an industry regulatory framework necessary for this specific product type, given the product type does not exist in South Africa.
- Attorneys have been appointed to look at the business legalities, in creating a new insurance structure with government, which will incubate the new product type.
- An insurance underwriting system tool, from respective service providers, has been found to pilot the new product type.
- A distribution methodology has been initiated, to allow for effective distribution of the new product type, of which methodology will be tested once the pilot mandate has been received from the ASC.

SAIA is in the process of updating their previous submission to the NT. It is envisioned, with the necessary work that still needs to be fulfilled, that the submission will be made by June 2019. It is therefore anticipated that the insurance premium subsidies and/or reinsurance support for commercial and emerging farmers will only be included in the 2020 budget.

The previous submission was made to NT in 2016, of which was successful and was included in the Minister of Finance's, 2016 Medium-Term Budget Policy Statement but unfortunately was not followed through.

SAIA is very hopeful that it will succeed in their second submission to the NT, and is working tirelessly with its members and respective government representatives, to fulfil the project objectives, which are to make MPCI more affordable and to create an insurance product solution for the emerging farmers.

7. The Need to Expand Access to Multiperil Crop Insurance to Primary Agriculture in South Africa

The need to expand access to MPCI to primary agriculture in South Africa is underscored both by the lack of access to such insurance at present, as well as by the importance of primary agriculture to the economy.

In respect to access to MPCI, **it is important to note that only three non-life insurers are still offering MPCI and that international reinsurers are starting to not offer reinsurance for MPCI products in SA due to the drought risk in SA.** Because of the risk factor involved, the cost of MPCI has escalated, reducing annual consistency in demand for such products – farmers tend to only procure MPCI during seasons in which they anticipate increased risk, rather than procuring it on an annual basis, thus further increasing the associated risk and cost barriers to non-life insurers in providing broader access to such products on a more cost-effective and sustainable basis.

In this regard it is important to note that in its presentation to the Public-Private Growth Initiative currently under way under the auspices of the Department of Planning Monitoring and Evaluation in the Presidency at the BUSA Economic Indaba of 29 January of this year, the agri sector noted the following (see

presentation attached):

- Despite significant climatic and policy barriers, primary agriculture has been growing its direct contribution to the gross domestic product (GDP) of the country from around 2.4% per annum over the period 2013/14 to 2015/16, it has been able to improve its performance to a contribution of 2.6% of GDP for 2016/17.
- It has also been able to improve its direct contribution to job creation from around 700 000 jobs in the earlier part of the decade to the 850 000 – 900 000 mark since 2015
- Agricultural exports are a significant contributor of export revenue, averaging a contribution in the order of 34% of export revenue over the period 2014/15 to 2016/17 and have also maintained a positive trade balance of around US$2bn since 2014
- Amongst the key trends the agri sector noted in the industry, it raised the immense pressure domestic policy and climatic factors have placed on the profitability and competitiveness of the sector, but noted that this could be improved with, amongst other, a common vision towards food security and food safety and the adoption of critical sustainable agricultural initiatives.
- In terms of the key focus areas of the agri sector's strategy it prioritised feasible financing opportunities for new farmers (inclusive of development and commercial finance) and improved climate change and disaster management.
- To improve the investment environment, it committed to advocate for an enabling policy environment that would, amongst other, facilitate various private sector initiatives.
- As a key part of the required policy changes to improve access to finance for new entrant farmers, it prioritised a focus on greater access to insurance, which would relate to MPCI.

8. Developing a Successful Public-Private Partnership model for increasing access to Multiperil Crop Insurance and Index Insurance for emerging farmers

- A Public Private Partnership (PPP) is a long-term contract between a private party and a government entity, for providing a public asset or service, in which the private party bears significant risk and management responsibility, and remuneration is linked to performance.
- Market penetration of MPCI for smallholder (including emerging) farmers is less than 1% and provides an opportunity for improving the livelihood of smallholder farmers as well as increasing the insurance industry's understanding of this audience.
- SAIA is proposing an independent host structure, where for instance SASRIA could be the insurance administrator for the PPP, given their already existing infrastructures to manage costs.
- All parties in the PPP provide funding, direction, resources & expertise for which the terms and conditions are set in a partnering agreement.
- It is advised that the PPP includes multiple private companies, not only insurers but also technology and distribution partners.

9. Towards a Feasible Distribution Model for Index Insurance for emerging farmers

- Multiple distribution channels have been reviewed, including multinational organisations, banks, multilateral financial institutions, retailers, agribusinesses, technology, CBO's, non-governmental organisations and the Post Office.
- To improve efficiency within the agriculture index insurance value chain, it is recommended to combine delivery channels.
- Technology, MNO's and agribusiness are recommended distribution channels as they offer benefits on cost, scalability, brand power, existing relationships and trust to a wide range of farmer profiles.

10. Leading Practices: Key Lessons from across Africa and India for a Successful Product Launch

- The Financial Services Conduct Authority and the Prudential Authority need to develop a clear regulatory framework, for insurance support for emerging farmers.
- An insurance product that covers a variety of appropriate and relevant risks (including income) must be developed.
- Technology and the use of mobile network operator services must be considered as a low-cost option for distributing insurance policies to and making payments.
- Technology and data must be considered to lower costs and support the administration of insurance products.

11. Demand for Agricultural Insurance amongst Smallholder and emerging Farmers

- The need to cover agricultural risks faced by smallholder farmers is clear from changing weather patterns and resulting high losses from drought and hail
- 85% of smallholder's farmers are somewhat willing to purchase index insurance
- The main reasons for unwillingness to purchase index-based agriculture insurance relates to income and farm productivity
- We estimate the demand for pasture drought index and or livestock mortality insurance to be 112,625 emerging farmers
- We estimate the demand for area yield and crop weather index insurance to be 44,625 emerging farmers

12. Conclusion

We hope to have conveyed in this proposal that the SAIA, and the NLII which it represents, has invested significant effort and resources (including money) to identify a real need in the economy and to develop a proposal in how to address and promote inclusive growth in terms of its proposal around a PPP to increase access to Multiperil Crop Insurance for primary agriculture and Index Insurance for emerging farmers.

It is our hope that the Standing and Select Committees of Finance will recognise this effort with a recommendation to National Treasury that it will engage with us urgently in working towards future budgetary allocations for this project.

We also stand ready to provide any further information required by the Standing and

Select Committees, and in future engagement with government, inclusive of further information on key next steps, strategic implementation plans, monitoring and evaluation for the proposed PPP.