Africa Insurance Outlook 2022

Risk-based capital developments across Africa

MAKING AN IMPACT THAT MATTERS since 1845

Risk-based capital developments across Africa

Insurers across Africa are placing significant attention on the implementation of IFRS 17 and IFRS 9. At the same time, regulators in a number of African countries are upgrading their risk and capital regimes and introducing new or enhancing existing risk-based capital (RBC) regimes.
We have explored the application of RBC in several African countries using the following approach:

- We investigated the kind of RBC regimes that are being considered and the impact they could have on the insurance market.
- We also looked at the progress made by the various countries in adopting an RBC approach.
- We have interviewed a number of regulators and insurance practitioners in order to understand their reasonings for transitioning to an RBC regime.

RBC in Africa

One of the primary roles of insurance regulators is to ensure that insurance companies are able to meet the promised benefits to their policyholders.

Most African countries have announced that they are transitioning to an RBC regime. Kenya, Ghana and Nigeria have started by increasing the minimum capital requirements (MCR) for insurers.
The MCR has been increased to ensure a smooth transition to an RBC regime. Weakly capitalised insurers are given time to recapitalise or to restructure their businesses. One regulator indicated that a criterion they are applying to implement an RBC regime is that capital is commensurate with the nature, size and complexity of the risks borne by the regulated entities.

African insurers employ a range and sometimes a mix of solvency and capital practices including:

- rules-based regime which with stress scenarios that vary by risk;
- rules-based regime with stress scenarios that vary by product type; and
- a principles-based regime, covering all known risks with room for market calibrations.

West Africa: Nigeria and Ghana

Ghana: Plans to adopt RBC supervision in Ghana gained momentum in 2014, when the National Insurance Commission (NIC) released draft technical specifications [1].

The NIC revised the minimum capital requirements of all insurance entities in Ghana, effective from the 31st of December 2021. The minimum capital requirement for insurers in Ghana has increased

1 https://nicgh.org/wp-content/uploads/2018/02/NIC_Annual-Report_2015.pdf

from GHC15m (USD2.4m as at 31 December 2021 exchange rates) to GHC50m (USD8m as at 31 December 2021 exchange rates). The minimum amount for reinsurers was raised from GHC40m (USD6m as at 31 December 2021 exchange rates) to GHC125m (USD20m as at 31 December 2021 exchange rates) [2].

Nigeria: The National Insurance Commission ("NAICOM") announced in August 2018 that they are adopting an RBC measure. NAICOM issued a circular requesting all insurance companies to recapitalise, based on a 3-level tier-based minimum solvency capital requirements which was in line with a Risk Based Supervision ("RBS"). The circular was later withdrawn in November 2018.

In 2019, as part of a phased approach to RBC, Nigeria increased the minimum capital requirements for insurers. The minimum capital requirements have been increased from N2bn (USD6m as at 31 December 2019 exchange rates) to N8bn (USD22m as at 31 December 2021 exchange rates) for life insurers, from N3bn (USD8m as at 31 December 2019 exchange rates) to N10bn (USD28m as at 31 December 2019 exchange rates) for general insurers, and from N5bn (USD14m as at 31 December 2019 exchange rates) to N18bn (USD50m as at 31 December 2019 exchange rates) for composite insurers. Reinsurers have also seen an increase in their minimum capital requirement from N10bn (USD28m as at 31 December 2019 exchange rates) to N20bn (USD52m as at 31 December 2019 exchange rates) [3]. Insurers were requested to hold at least 50% of these minimum capital requirements by the 31st of December 2020, after which all insurers were required to be fully compliant with the minimum capital requirements by no later than the 30th of September 2021 [4]. At the time of writing this paper, NAICOM has not yet enforced the second phase because of industry pushback via the courts.

East Africa: Kenya and Uganda

Kenya: The RBC implementation journey in Kenya started in 2011. The regulator embarked on internal and industry-wide capacity building exercise and issued guidelines to support the implementation of an RBC regime. The regulator also updated its reporting systems to automate collection of industry data to aid supervision. In 2017, RBC regulations were published and insurers were given a transition window period, with the adoption date set to July 2020. However, but in the course of 2020, this was extended to December 2020 due to the COVID-19 pandemic. The regulations set minimum solvency capital requirements based on three measures:

- a minimum capital of KES 400m (USD1m as at 31 December 2020 exchange rates);
- a volume-based measure of 5% of best estimate liabilities (carried over from the previous regime); and
- an RBC measure based on stresses applied to assets and liabilities.

The regulator planned a gradual increase of capital requirements to 200% of the minimum solvency capital under the different measures. This has paused this given the impact of the COVID-19 pandemic.

Uganda: The Ugandan RBC regime commenced in February 2018. The regulator applied a structure similar to the Kenyan RBC regime. The Insurance Capital adequacy and prudential regulations were gazetted in the year 2020 and came into effect immediately [5].

The RBC regime in Uganda requires that insurers compute their Capital Adequacy Ratio (Available Capital/Required Capital) which should be at a level above 200% at all times. In a circular released in October 2021, the Insurance Regulatory Authority of Uganda (IRA) directed all insurers, reinsurers and health management organisations (HMOs) to meet the CAR of 200% by 31st December 2021 [6].

North Africa: Morocco

Morocco: As part of the ongoing insurance sector reforms, the Moroccan lawmakers have set up a new independent regulatory authority for insurers, the Autorité de Contrôle des Assurances et de la Prévoyance Sociale (ACAPS) in 2016. The ACAPS is in the process of implementing a RBC regime similar to Solvency II of Europe but adapted to the Moroccan insurance market. A three-pillar structure has been adopted as a regulatory framework: Quantitative requirements (Pillar I), a qualitative pillar focusing on governance of the undertaking and supervisory activity (Pillar II) and a disclosure pillar focusing on supervisory reporting (Pillar III). At the time of writing, the ACAPS had made the following progress:

- Pillar I: quantitative impact assessment exercises have been performed with insurance companies. However, finalised regulatory standards have not yet been issued. These stress tests have been performed to calibrate the final regulatory standards.
- Pillar II: Regulations have been issued with the end of December 2022 as the target date for the implementation by insurance companies.
- Pillar III: The ACAPS has not yet issued any updates relating to this pillar.

Southern Africa: South Africa, Zimbabwe and Zambia

South Africa: In July 2018, South Africa implemented Solvency and Asset Management (SAM), an RBC regime which shares many similarities (a three-pillar regime) with Solvency II of Europe.

Zimbabwe: The Insurance and Pension Commission (IPEC) first announced plans to transition to an RBC regime in 2015. In June 2021, the IPEC launched a new RBC regime commonly referred to as the Integrated Capital and Risk Programme (ZICARP) [7]. ZICARP has three pillars: Pillar 1 - quantitative requirements, Pillar 2 - qualitative requirements and Pillar 3 - disclosure requirements. It is very similar to SAM of South Africa.

2 https://nicgh.org/wp-content/uploads/2019/06/Press-Release-New-Minimum-Capital-Requirements-for-Insurance-Entities.pdf
3 https://www.naicom.gov.ng/publications/ NAICOM_Circular_on_Minimum_Paid_Up_Share_Capital_20_May_2019%20(1).pdf
4 https://www.naicom.gov.ng/publications/Segmentation_of_Minimum_Paid_Up_Share_Capital_Requirement_for_Insurance_Companies_in_Nigeria_1.pdf
5 https://ira.go.ug/cp/uploads/Capital%20Adequacy%20&%20Prudential%20Requirements,%20Reg%202020.pdf
6 https://ira.go.ug/download/circular-complinace-with-capital- adequacy/?wpdmdl=2520&refresh=6294ca3aa68e41653918266
7 https://ipec.co.zw/ipec-launches-a-capital-solvency-framework-for-insurers

The IPEC has held a number of industry workshops since 2018, conducted qualitative risk & capital management surveys and quantitative impact studies in 2019. In 2021, the IPEC released several circulars documenting the requirements for all three pillars of ZICARP. The IPEC has been conducting dry runs scheduled to end in December 2022.

Zambia: The process of transition to an RBC regime gained significant traction when the Parliament passed the Insurance Act in 2021. In addition to the provisions for the enhancement of consumer protection, the Act also allows for the creation of a new solvency/capital adequacy framework that will respond to the level of risks that insurers and reinsurers are allowed to take on? as they provide cover.

The Pension and Insurance Industry Authority (PIA) has issued a draft RBC regulation which is very similar to the old SAP 104 approach that was used in South Africa before the introduction of the SAM regime.

General remarks

Capital implications: As regulators adopt RBC regimes, the required solvency capital may be higher than the stipulated minimum for some companies, depending on the risks they face. The increase in capital requirements may result in some companies failing to meet their solvency capital requirements which in turn may prompt an increase in merger and acquisition activities.

Company standards: In the absence of risk-based regulatory solvency measures, some insurance companies have adopted principles from SAM (and SAP104) and Solvency II from South Africa and Europe when calibrating their economic capital. This is mostly the case for large insurers and those that are in the same stable as South African and European insurers and need to report on SAM or Solvency II numbers to their parent company.

Skills levels: Some insurers and regulators have engaged external experts for assistance as they transition to RBC regimes. One regulator indicated that, as expected, insurance industry players do not currently have the technical expertise in-house and will require external assistance where applicable, although the regulator will be providing training to support the transitioning to RBC regime. Regulators are engaging with the insurance players to ensure that they achieve a smooth transition to RBC. One regulator indicated that they believe that "the ultimate benefits for industry as a whole will outweigh the initial costs of implementation".

COVID-19: Most regulators and insurers also agree that there is a need to upgrade their solvency and capital regimes following the learnings from the COVID-19 pandemic. This will ensure that the sector is well prepared for future shocks.

Looking ahead

There are many benefits of a solid RBC regime for both regulators and insurance companies. On the one side RBC regime will assist the regulators in understanding the risks companies are facing and how to monitor these risks. On the other side RBC regimes will assist the insurance industry to understand economic capital underlying the insurance business and their solvency position. It will also help those companies that have already calibrated their economic capital models to compare with the standard formula (if available) from the regulator.

The learnings from South Africa and other African countries that have implemented a Solvency II-type RBC regime suggest that the insurance industry will need significant time to implement and to develop internal expertise. Different companies are likely to have different target operating models. Small to medium size companies are likely to focus on ensuring compliance with regulations, while larger companies will focus on the overall transformation of their risk and capital management functions, developing economic capital models and ensuring efficient utilisation of capital. Insurers will be able to leverage learnings gained during the implementation of IFRS 17.

Likewise, regulators can leverage the learnings from the IFRS 17 implementation when developing the RBC regime. There are similarities between RBC regime and IFRS 17 including data granularity (although IFRS 17 requires more data), and new features such as risk margin/risk adjustment, contract boundaries and the use of best estimate valuation assumptions without margins.

Given the potential lack of internal capabilities and experience, insurers and regulators will need support in areas such as RBC training, statutory actuarial support, quantitative and qualitative impact assessment and model development, model validation and general assistance in embedding the new regime.

Authors

Giles Waugh
Associate Director, Actuarial & Insurance Solutions
Deloitte Africa
gwaugh@deloitte.co.za

Takalani Sikhavhakhavha
Senior Manager, Actuarial & Insurance Solutions
Deloitte Africa
tsikhavhakhavha@deloitte.co.za