

COVID-19: IMPACT ON THE INSURANCE INDUSTRY

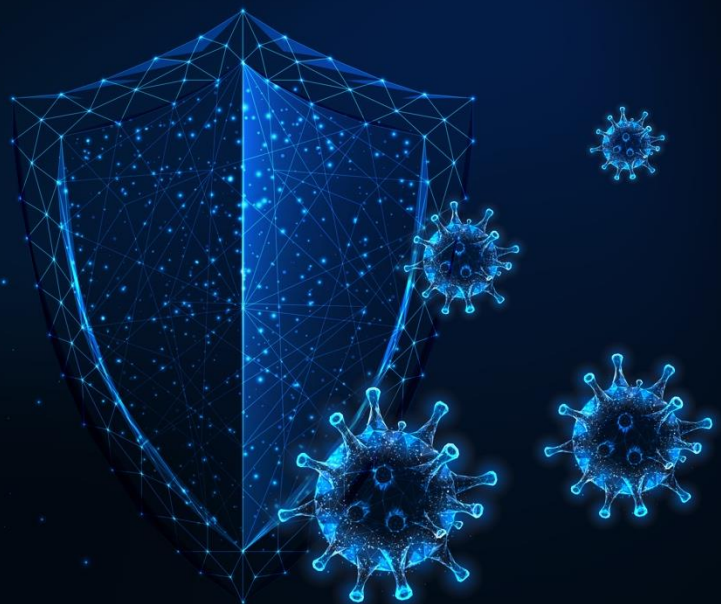
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OVERVIEW

With over two million confirmed cases, COVID-19 is no doubt the biggest challenge facing humanity today and it continues to transform the way we live and do business. Beyond the health crisis, its impact has been felt across all sectors of the global economy, including the insurance sector. It continues to impact this sector in many different ways, and it is clear that all key stakeholders have to brace themselves for some very difficult months ahead.

In this paper, we examine the overall impact of this pandemic on the insurance industry in Nigeria, especially how it impacts diverse interests of players in the insurance business including insurance companies and insured persons. We also examine the regulatory response by the National Insurance Commission (NAICOM) and how the pandemic potentially impacts on the recapitalization efforts by insurance companies in Nigeria, in view of directives previously issued by NAICOM.

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INSURANCE COMPANIES

In the financial services sector, insurance companies, given the risk nature of their business, are likely to be hard hit owing to the impact of the pandemic on policies. For now, like most businesses, the immediate concern is ensuring the health and safety of employees, implementing alternative work arrangements and ensuring business continuity despite the seemingly difficult circumstances; but in the coming weeks and months, we expect to see significant operational adjustments with many insurance companies and policy changes in the administration of the industry.

Whilst insurance companies are generally more resilient to economic shockwaves given the tougher capital adequacy and prudential standards imposed on insurance business operators, many will be forced to reposition and adjust their business strategy, implementation plans, cash flow expectations and investment portfolios to cushion the potential effects of the COVID-19 pandemic (the Pandemic). As custodians of risk, insurance companies occupy a unique position and play a crucial role during times of economic stress. Companies and individuals will rely on insurance companies to manage risks and mitigate losses that may potentially arise during the pandemic and the period following the pandemic. In effect, we envisage that potentially, and this depends significantly on the terms of the policy and risk insured, claims on insurance policies, performance bonds and advance payment guarantees may rise during and in the immediate aftermath of the Pandemic thus resulting in substantial strain on insurance. These concerns may be exacerbated where a substantial part of the investment asset of an insurer or reinsurer is liquid or liquidate-able portfolio. In essence, as one of the largest groups of institutional investors, insurance companies therefore may be vulnerable to volatility in financial markets and will be at the receiving end in this regard.



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The position and potential exposure of insurance companies may become more entrenched when examined against the backdrop of the unsettling reality that, even prior to the disaster heralded by Covid-19, capital adequacy of actors in the industry has been a major concern. In particular, a large number of insurance companies in Nigeria may not be well capitalized and may not be able to withstand an onrush of insurance claims, if the need arises. Although we note that there have been efforts by insurance companies and NAICOM in this regard and we will address how the Pandemic potentially impacts on those efforts later.

Broadly, we expect that the Pandemic will likely cause a strain on the investment portfolios maintained by insurance companies giving the global economic crunch, decreased premium volume generally, including delayed premium payments by insured persons and companies. We also expect to see an increase in insurance coverage disputes.

Without doubt, given that premiums form the major source of revenue for insurance companies, business failure, bankruptcy or insolvency and loss of revenue by policy holders will certainly impact premium payments, if not outright cancellation of the policy. As a corollary, a significant decrease in the volume of premium payments will no doubt impact the revenue pool of insurance companies and business sustainability.

Businesses are increasingly failing globally, especially in the most affected sectors such as tourism and leisure, aviation and, maritime, automotive, construction and real estate, financial services and education. Although most business owners and corporates will typically take out general insurance policies not specifically providing pandemic covers, a significant number of companies and firms in these sectors are likely to have comprehensive insurance covers to include pandemics. There is the recent example of Wimbledon tennis tournament¹, which after the 2003 SARS outbreak took out a pandemic insurance policy of USD\$1.9 million annual premium and now receiving an insurance payout of about USD\$142 million for cancellation of the 2020 tournament

1. <https://www.insurancejournal.com/news/international/2020/04/13/564598.htm>

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Whilst an uncommon policy, we envisage that the trend of making similar claims will increase with insurers potentially having to pay out on multiple such policies all at once further adding to the burdens faced by the industry. In a similar vein, travel insurance is a big revenue driver for many insurance companies and with the aviation industry effectively at a halt now, insurance companies are likely to lose significant revenue from that sector. The volumes of pay-outs on existing travel insurance policies are likely to skyrocket. In the UK for example, around £275 million is expected to be paid out in COVID-19 related claims, the majority of which will be for cancellation cover.

Fitch has already warned that life insurance companies could be particularly hard hit by the combination of falling stock markets and increasing mortality. Paying out on policies will be a huge hit to insurers, and for reinsurers when added to their other exposure, and that could put them in serious jeopardy².

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2. See <https://www.insurancejournal.com/news/national/2020/03/18/561473.htm>

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INSURED PERSONS

For the insured, the expectation is that (depending on the sector in which they operate and how it impacts on daily life and their business), there is likely to be a rise in the insurance claims. Specifically, for commodity price insurance, which is the go-to risk management measure for traders in oil futures and derivatives, with the global slump in prices, the focus will be on insurance companies and other financial institutions providing these products to plug the gaping hole. Similar trend is also expected from actual operators in the oil and gas sectors.

For frontline health workers and persons that are most exposed to the pandemic, we anticipate is that there will be a rise in life insurance and health insurance policies and claims (where such policies are already in place). In recent weeks we have seen private and public sector interventions in this regard, and we expect to see more of these efforts in the coming weeks.



Very recently, Prudential Zenith Life Insurance, one of the leading insurance companies in Nigeria announced a series of initiatives which it has put in place to protect its customers and staff during this Pandemic.

As part of these initiatives, Prudential Zenith will provide additional COVID-19 insurance cover for its customers, staff and sales personnel, waive pandemic exclusions written into policy language, reduce waiting periods for new cover, simplify claims procedures, enabling claims to be made even via WhatsApp and deliver additional training and incentives to its personnel to continue to provide advice and access to insurance during the Pandemic and lockdown period. Speaking on Prudential's response to the Pandemic, Andrew Greenwood, the Chief Operating Officer of Prudential noted that the Pandemic presents a unique opportunity for Prudential to offer support for its existing clients at this crucial time of need and has thus designed a bouquet of benefits and initiatives in this regard.

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Businesses that will be significantly affected by the Pandemic may struggle to pay insurance premiums and may also be forced to restructure their insurance arrangements. For loans where some form of insurance policy has been taken to mitigate the risk of default, there is also the likelihood that claims may be made to the insurance companies in the event that they are in some form of default in the payment obligations under the loan agreement.

In sum, we may begin to see defaults by insured persons and companies, reduced premium remittance and there is a strong chance that a significant number of insured persons will begin to deprioritize a lot of their insurance policies and restructure them as they focus on survival in the midst of the harsh economic conditions that is likely to follow after the Pandemic passes. Also, businesses whose supply chain falls within the countries of restricted access may suffer business discontinuity arising from denial of access, failure to deliver parts or materials essential for production or absence of staff crucial in the supply chain. All of this may eventually lead to a rise in insurance claims for business continuity.

RECAPITALIZATION EFFORTS BY INSURANCE COMPANIES

Over the past couple of years, there has been significant public sector efforts not just to drive growth in the insurance industry in terms of policy holders, the enforcement of compulsory insurance, job creation but also to reinforce the capacity of insurers to withstand shock. Very recently, the National Insurance Commission (NAICOM) introduced a deadline for insurance companies to recapitalize and reposition themselves for growth. At the start of the year, the expectation was that significant activity will be seen in the insurance industry over the course of the year in terms of investments, mergers and acquisitions, given the deadlines set by NAICOM for insurance companies to recapitalize.

Already there has been activity in this regard with a number of deals already in the pipeline. With the Pandemic still in full swing and lockdown measures already in place across the country, we have already seen commercial activity and transactions slow down, with some even grinding to a halt. The restrictions on movement will no doubt impact on the due diligence process and the process of sourcing for investors. Further, with the global economy likely to slide into a recession post-COVID 19, investor appetite is also likely to reduce due to liquidity constraints, foreign currency fluctuations and volatilities in many sectors of the economy. The insurance sector is likely to be negatively impacted by the Pandemic and investors may thus turn away from investing in the insurance sector pending when the economy eventually stabilizes. The economic fallout from the Pandemic will also likely impact on the valuation of insurance companies and possibly extend the timelines for any recapitalization or consolidation efforts.

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NAICOM'S RESPONSE

In recent weeks, NAICOM has issued two circulars to insurance operators to reaffirm its commitment to cushion the effects of the Pandemic on the economy. In its circular dated 27 March 2020 titled "Palliatives as a Result of the Impact of Coronavirus (COVID -19) on insurance operators", NAICOM announced a number of measures including an extension of the deadline for insurance companies to submit Q1 returns, a waiver granted with respect to delayed submission of renewal documents by insurance brokers, loss adjusters and insurance agents. In another circular dated 1 April 2020, NAICOM reaffirmed its commitment to business continuity measures to address the effect of COVID 19 on insurance operations in Nigeria³.

Although no formal announcements were made in relation to possible extension of the recapitalization deadlines previously set by NAICOM for insurance companies, NAICOM did encourage insurance operators to meet their commitments on the recapitalisation process and guaranteed that mitigating measures will be communicated to the public in due course.



3. See <https://guardian.ng/business-services/covid-19-naicom-extends-insurers-deadline-submission-of-q1-returns/>

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CONCLUSION

Nearly every sector of the global economy will be impacted by the Pandemic in one way or the other, and the insurance sector will not be any different. The slowdown in economic activity will eventually undermine the growth of insurance companies and possibly even contract insurable exposures. Notwithstanding this reality, it is imperative that insurance companies stay informed, remain proactive, and seek advice will be better positioned to respond to the compilation of challenges and uncertainty. In the months following the Pandemic, we expect that the exposure to risk many businesses are currently facing will lead to an increased demand for more comprehensive business insurance/business interruption cover. Customers will expect such insurance policies to address the many gaps revealed during the crisis. Insurers will thus need to capitalise on the opportunities and up their investments in innovative products and services.

In the meantime, you can keep up to date with the ongoing COVID 19 related developments and their legal implications on our dedicated [COVID 19 Resource Centre](#).

For further information, please contact:

Yimika Phillips

Partner
+234-1-2702551 Ext 2700
yphillips@olaniwunajayi.net

Jonathan Aluju

Partner
+234-1-2702551 Ext 2720
jaluju@olaniwunajayi.net

Olaniran Osotuyi

Senior Associate
+234-1-2702551 Ext 2626
oosotuyi@olaniwunajayi.net

Comfort Agboola

Senior Associate
+234-1-2702551 Ext 2612
cagboola@olaniwunajayi.net

Rilwan Shittu

Associate
+234-1-2702551 Ext 2649
rshittu@olaniwunajayi.net