2.2 Insurance Sector

The insurance sector is classified into two broad categories - general insurance business and long-term insurance business. As of December 2021, there were 56 insurance companies, 5 reinsurance companies, 220 insurance brokers and 11, 828 insurance agents (including 27 bancassurance agents). The general insurance business accounted for 55.2 percent of total insurance premiums in 2021 and overall insurance sector grew by 18.5 percent in premiums, to reach KSh 276.1 billion. Penetration of insurance services in the economy as measured by the ratio of insurance premium to GDP remained at 2.2 percent in 2021same as in 2020. The ratio is still way below the global average of 7.2 percent. The performance of the insurance industry in the period 2015 – 2021 **(Table 6).**

The insurance industry asset base grew by 10.4 percent to KSh 845.8 billion as at December 2021 from KSh 765.9 billion in December 2020. Long-term and general businesses invested KSh 524.4 billion (78.5 percent) and KSh 143.9 billion (21.5 per cent) in earning assets, respectively. Top three investement assets classes were government securities (71.7 percent), investment property (10.7 percent) and bank deposits (6.9 percent). Investment income increased by 34.4 percent to KSh 68.2 billion in 2021 compared to KSh 50.6 billion in 2020, which may be attributed to the recovery of the capital markets. Exposure to government securities introduces market risk in the event of steep rise in interest rates.

The growth in gross premium and assets increased return on assets and return on equity by 0.3 per cent and 1.2 per cent respectively. The increase in profitability of the insurance sector may be due to the recovery of the economy in 2021 from the impact of COVID-19 and adoption of digital methods in the payment of premiums and verification insurance covers.

Table 6: Key Performance Indicators for Insurers

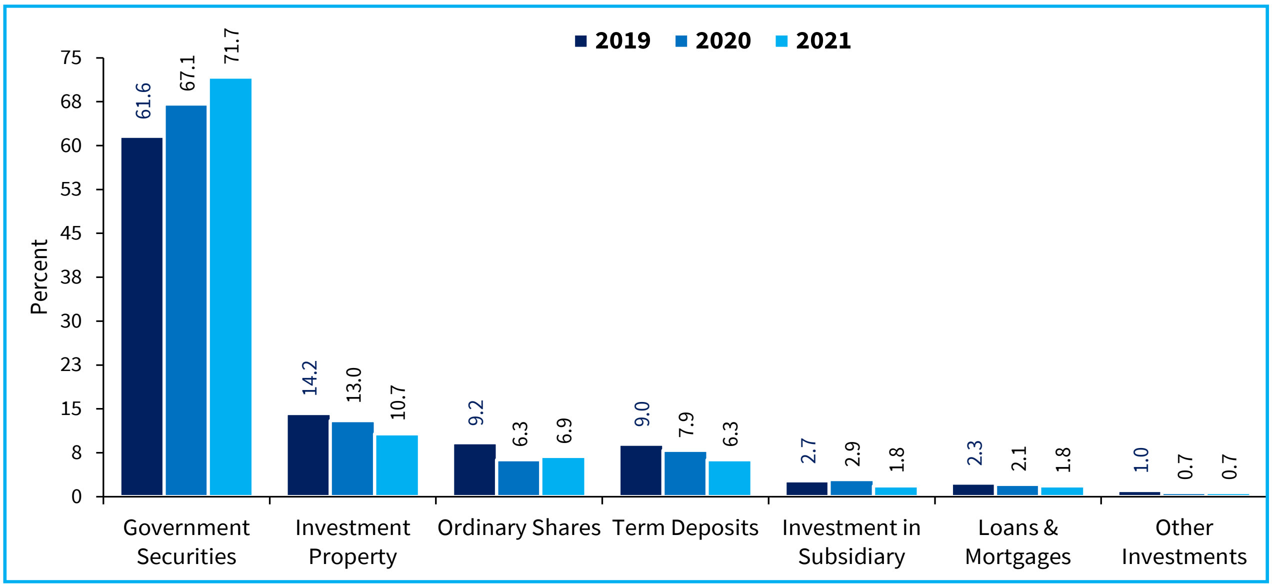
Insurers Performance Indicators								
Measurement Indicator	2015 KSh '000'	2016 KSh '000'	2017 KSh '000'	2018 KSh '000'	2019 KSh '000'	2020 KSh '000'	2021 KSh '000'	Annual Change (%)
Gross Premium Income	174,064,645	196,635,836	209,001,289	216,261,729	229,499,718	234,775,753	276,064,126	17.6
Net Premium Written	140,003,552	158,362,431	165,852,034	172,322,202	182,658,282	187,853,004	221,470,562	17.9
Claims Incurred (Gen. Business)	49,051,411	54,857,495	56,151,961	56,928,003	58,961,581	58,311,459	70,139,114	20.3
Commissions	10,895,759	12,578,735	12,495,181	11,487,628	10,957,562	11,157,093	13,502,337	21.0
Management Expenses	36,272,444	39,982,771	41,197,262	44,072,857	45,702,207	44,173,611	46,786,664	5.9
Investment Income	34,576,984	37,135,382	51,675,571	44,514,367	66,982,398	50,608,392	68,151,650	34.7
Profit/Loss After Taxation	13,635,098	12,832,644	13,642,971	7,269,263	15,119,928	6,388,955	5,726,359	-10.4
Investments	390,225,346	425,304,138	483,799,656	524,237,249	594,028,115	656,460,833	731,490,222	11.4
Assets	478,752,453	528,748,193	590,953,337	635,035,110	709,045,429	765,932,477	845,834,750	10.4
Shareholders' Funds	125,830,029	134,455,222	147,255,007	149,134,602	161,635,278	166,069,303	173,102,044	4.2
Key Performance Ratios for Insurers (Per cent)								
ROA	3.8	3.6	3.2	1.8	3.0	1.3	1.6	0.3
ROE	11.4	9.9	9.7	4.9	9.9	3.9	5.1	1.2
Combined ratio Gen Business)	102.7	102.4	101.1	102.8	103.4	102.0	106.2	4.2
Insurance Penetration Ratio	2.7	2.7	2.7	2.4	2.3	2.2	2.2	0.0

**Unaudited data*
Source: IRA

The growth in gross premium and assets increased return on assets and return on equity by 0.3 per cent and 1.2 per cent respectively. The increase in profitability of the insurance sector may be due to the recovery of the economy in 2021 from the impact of COVID-19 and adoption of digital methods to in the payment of premiums and verification insurance covers.

Increased share of government securities to 71.7 percent in 2021 from 67.1 percent of income generating assets in 2020 may indicate flight to quality and safety by insurers but raises sovereign exposure risk (Figure 23). There was also a decrease in investment in subsidiaries by 34.9 percent. The 2.3 percent decline in the share of investment property, may reflect COVID–19 pandemic aftershocks on the real estate and construction sectors. The value of ordinary shares held grew by 10.3 percent in 2021, reflecting elevated market risk exposure at NSE.

Figure 23: Investment Channels by Insuarance Sector



Source: IRA

Risks Assessment and Outlook

The sector is faced with both/or either increasing risks in magnitude and/or new ones are emerging: These include, but not limited to:

- ***The insurance risk –*** The very nature of insurance contracts is to offer protection against loss. The main factors affecting insurance risk include insurance product design, pricing, underwriting, reinsurance arrangements, reserving, and claims management. The insurance risk affects combined ratio which is a combination of claims ratio, commission ratio, and management expense ratio. The industry combined ratio was 106.2 percent as at December 2021 compared to 101.3 percent as at December 2020, indicating increased insurance risk for general insurance business.
- ***Market risk*** This is the risk of adverse fluctuations in market interest rates or asset prices resulting in overstating of assets /or understating of liabilities. Insurance companies are exposed to the risk of price movements for equities as they invested in the securities market. The sector held securities valued KSh 35.9 billion on the NSE as of December 2021, a 15.3 percent increase from 2020. The growth in the value of equities was mainly attributed to the increase in equity prices as economic prospects improved on diminishing COVID-19 pandemic effects.
- ***Credit risk*** Arises from the fact that a counterparty is unable to repay loans when due, including; amounts due from reinsurers in respect of claims already paid, amounts due from insurance intermediaries, amounts due from corporate bond issuers, cash, and deposits held in banks, reinsurer's share of insurance liabilities and reserves, retrocession assets for reinsurers and loans and mortgages advanced to varies counterparties. The credit exposure from outstanding premiums and reinsurance recoveries increased by 5.2 percent to KSh 40.1 billion in 2021. Insurers and reinsurers are required to constantly monitor risk profile of their creditors and make sufficient provisions and write-offs to ensure adequate valuation of debtors.

- ***Cybersecurity threats and insurance frauds have increased***. Cyber threats are evolving rapidly due to the growing digital transformation of society and the widespread use of internet-enabled devices, systems, and processes. Working away from office (a mitigation measure against the spread of COVID-19) raised exposure to cyber risk due to limited security in home set-ups
- ***Ukraine War.*** The recent Russia-Ukrainian conflict is set to have an impact as seen from the already substantial change in the energy market, for example, the increase in fuel prices. As a result, the conflict is a risk to the insurance market given increase in commodity prices which will in turn impact the cost of insurance across the board. The conflict is also expected to have an adverse impact on the marine cargo class of business and on companies that have an exposure to Russian or Ukrainian companies.
- ***Political Risk.*** This being an election year, political risk is an emerging risk to the insurance industry due to the possibility of riots and/or civil unrest which could cause a disruption in business. Companies could choose to scale down operations as a mitigation to the risk. Investment returns for the industry are also expected to be subdued during the electioneering period.
- ***Climate Change Risk.*** Climate change such as severe drought or floods will likely lead to higher claim pay-outs from insurers participating in underwriting those risks and will in turn reduce underwriting performance. As a mitigation affected insurers should reprice their portfolios to factor long-term exposure to climate changes.

The sector outlook remains positive in terms of growth, stability, and resilience. The IRA has enhanced surveillance and taken measures to address existing challenges to improve the sector's performance. This is complimented by rapid adoption of technology and digital platforms, and innovative distribution channels as well as raising risk awareness. As the economy recovers, insurers see opportunities to innovate and come up with value-based products meeting consumer needs.

2.3 Capital Markets

The Nairobi Securities Exchange performance was resilient to COVID-19 pandemic as investors deployed hedging strategies to mitigate market risk in 2021 (Figure 24). The NASI, NSE 20 and market capitalisation increased by 9.4 percent, 1.8 percent, and 11.0 percent, respectively. Equity turnover and total shares traded, declined by 8.1 percent and 21.4 percent, respectively in 2021. The liquidity of the equities declined in 2021 from 6.9 percent in 2020 to 5.9 percent in 2021, despite adoption of securities lending reforms enabling market participants to buy and sell securities, thereby enhancing liquidity.