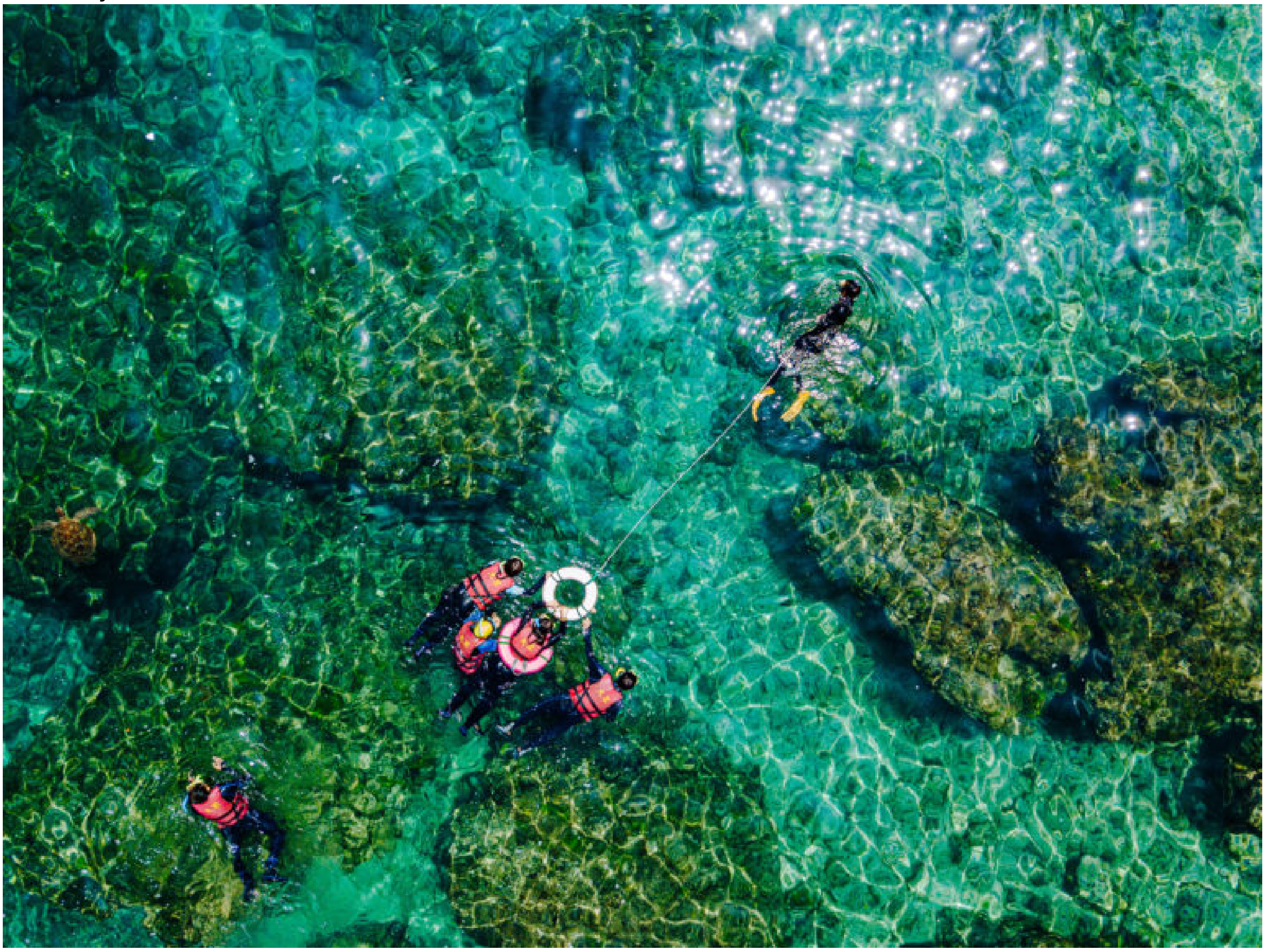
Funeral Insurance in South Africa: Market Review

February 7, 2022



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Market Sizing

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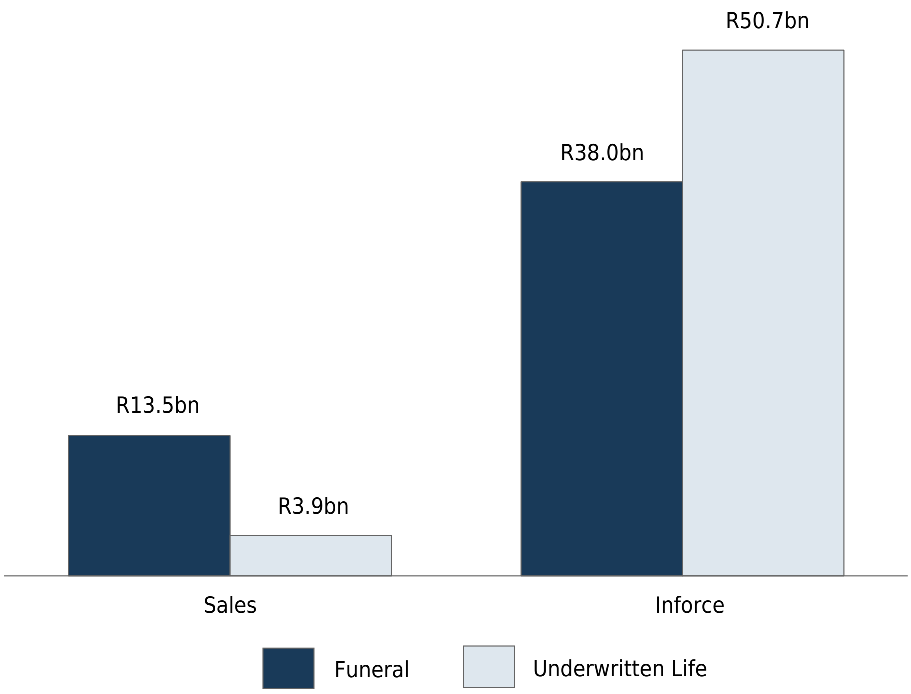
Exhibit 1: Sales and Inforce, Annualised Premium Equivalent as at Q2 2021



Source: NMG Funeral Distribution Monitor, NMG Risk Distribution Monitor

The funeral and underwritten life markets are both very large, and of great importance to the South African insurance industry. They differ in some key areas.

In the 12 months to June 2021, the value of sales of new funeral insurance products was almost four times that of the underwritten life market, at R13.5bn against R3.9bn.

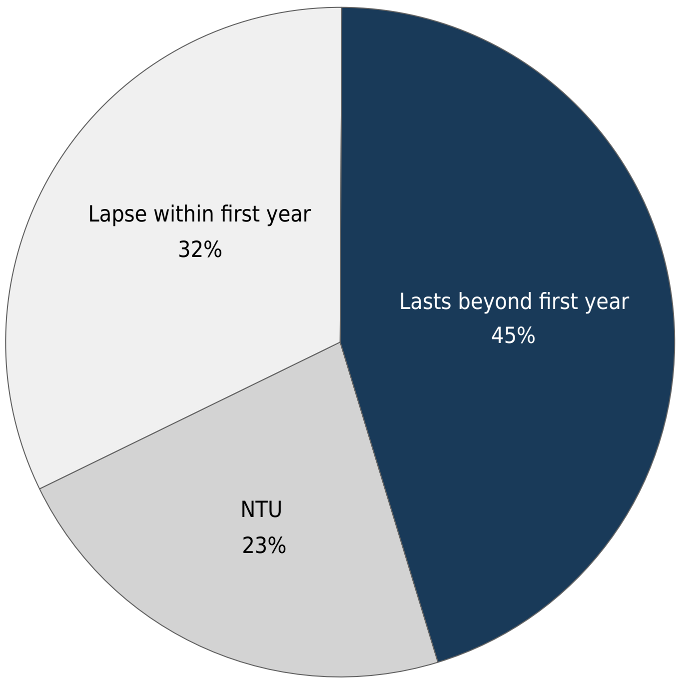
However, inforce premiums for underwritten life are R12.7bn, one-third greater than those in funeral insurance.

The primary reason for this is much lower persistency of funeral insurance products, as explored below.

Persistency and Payment Dynamics

The funeral and underwritten life markets are both very large, and of great importance to the South African insurance industry. They differ in some key areas.

Exhibit 2: Funeral Insurance Persistency, Q2 2021



Source: NMG Funeral Distribution Monitor

As exhibit 2 illustrates, the majority of funeral policies sold will not persist beyond their first year, with nearly a quarter of them lapsing before the first premium is received (hence classified as “not taken up” or NTU).

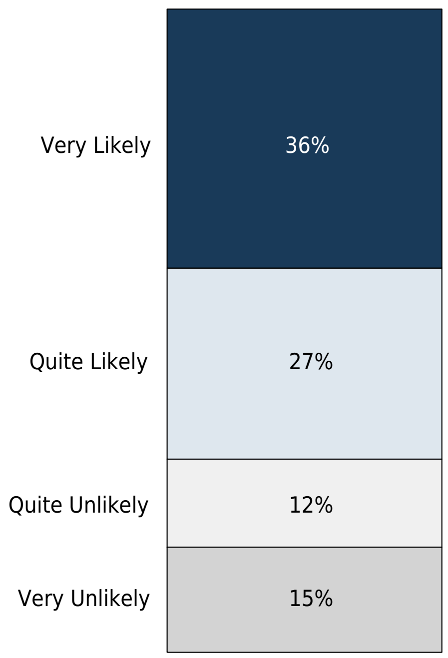
Compare this to underwritten life, where 1st-year lapse rates average 13% and subsequent year lapsation is around 9% – both substantially below their funeral counterparts.

This results in a higher degree of customer turnover for funeral insurance and much greater acquisition costs. The wastage is substantial, and to no party’s benefit.

There are some interesting avenues to explore to improve customer persistency.

One approach appears to be around payment flexibility – e.g. despite affordability challenges, a majority of consumers (63%) expressed an interest in paying for multiple months of cover up front, even with no discount offered.

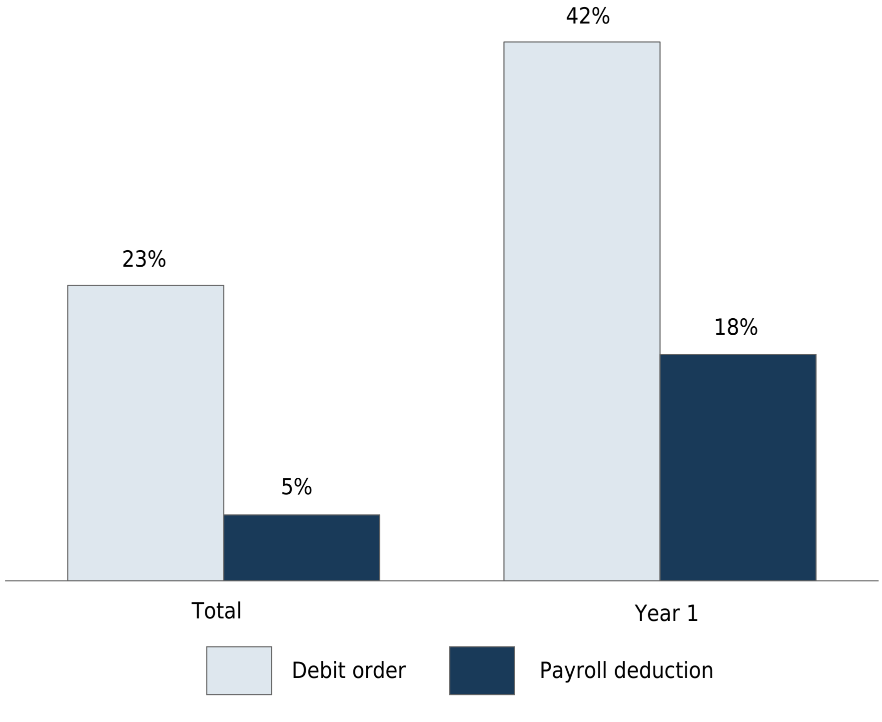
Exhibit 3: Likelihood of Paying Multiple Premiums Up Front



Source: NMG Funeral Consumer Study

Furthermore, we know that the payment method through which policies are sold plays a huge role in persistency, with payroll deduction reducing lapse rates four-fold (and halving first-year lapses), as compared against debit-order and cash payments.

Exhibit 4: Funeral Insurance Lapse Rates by Payment Method, Q2 2021



Source: NMG Funeral Distribution Monitor

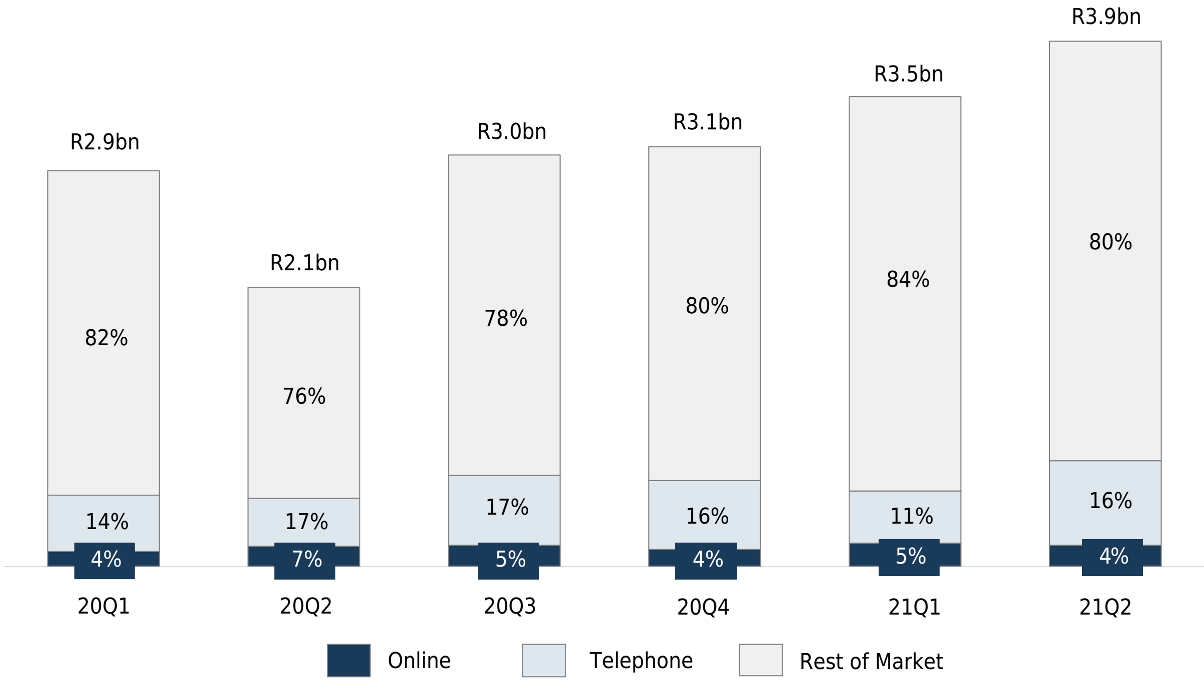
Of course, a payroll deduction system is not always viable. Development often comes with high set-up costs and requires entrenched relationships, not to mention employer facilitation and support.

It is therefore only seen to work effectively within some distribution channels, such as through workplace tied agents.

Direct Channels and Barriers

Turning to distribution channels, the 'direct' channels (online and telephone direct-to-consumer, with limited intermediation) experienced substantial shifts throughout the last 18 months.

Exhibit 5: Funeral Insurance Sales, Q1 2020 to Q2 2021



Source: NMG Funeral Distribution Monitor

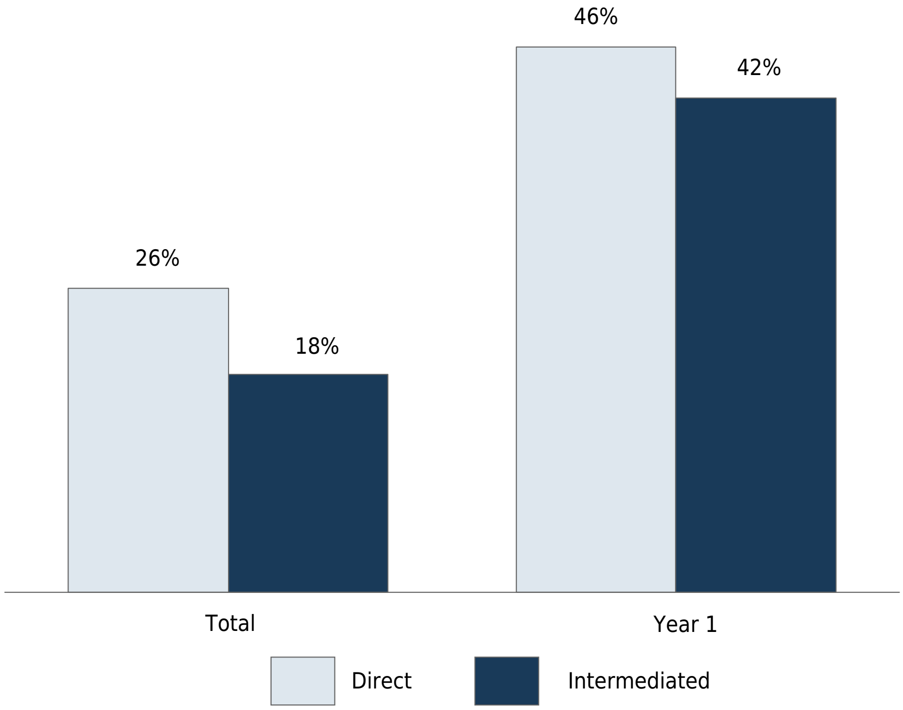
Direct channels experienced their sales peak (relative to other channels) in 2020 Q2 as lockdown measures came into full force.

Accompanied by a severe drop in overall sales – primarily in face-to-face (or intermediated) channels – direct channels accounted for 24% of all sales.

This was a temporary blip, and the recovery of intermediated channels as a result of easing lockdown measures saw a return to normal distribution which continued into Q2 of 2021.

While direct sales seem to be on an upward trajectory, lockdowns do not appear to have been a key catalyst for largescale adoption or permanent rotation into these channels.

Exhibit 6: Average Lapse Rates by Channel, Q3 2020 to Q2 2021



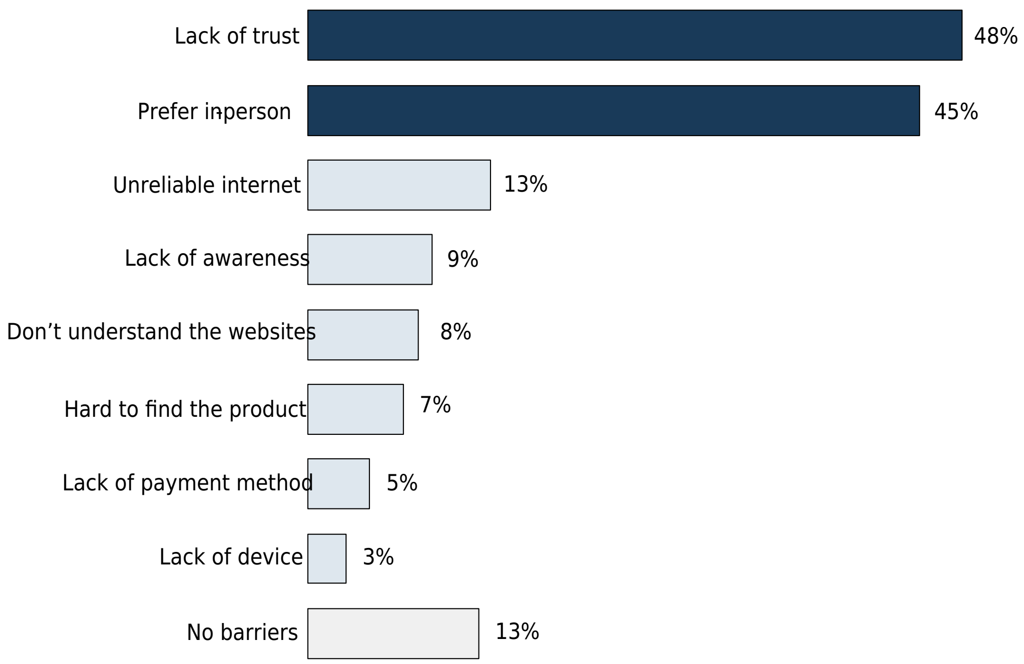
Source: NMG Funeral Distribution Monitor

Furthermore, as evidenced in exhibit 6, direct channels experience even worse persistency than the rest of the market (regardless of Covid).

The majority of consumers prefer engaging with providers and administrating policies through digital means.

However, as seen in exhibit 7, the lack of trust in purchasing through a 'faceless' digital proposition remains a stiff barrier to sales growth and translates into poor ongoing engagement and thus poor persistency.

Exhibit 7: Barriers to Digital Purchase



Source: NMG Funeral Consumer Study
(Note that graph does not sum to 100% as question was multiple choice)

The digital channel faces the challenge of improving consumer belief and trust, and the model is currently quite low-engagement; developing a human-digital omnichannel proposition within an online ‘ecosystem’ could go a long way to solving this, and certain providers are starting to see some success here.

Furthermore, it stands to reason that a well-designed digital ecosystem would increase customer engagement and improve persistency.

There should be a huge opportunity for a funeral insurance provider that can fully establish this financial ecosystem, where funeral plays a role as one piece of a holistic suite of financial products, and the provider has access to customers with a pre-existing relationship and engrained trust in the brand.

The aforementioned preference for online administration already lends credence to such a strategy.

Covid: Reasons for Optimism

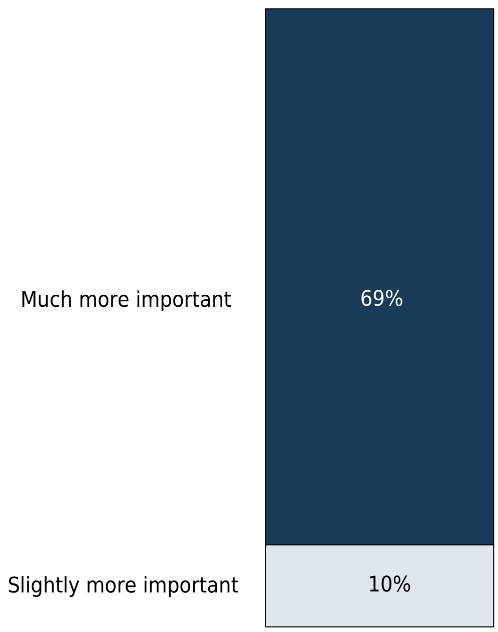
Of course, the biggest factor impacting the funeral insurance market over the last two years (as indeed has been the case for all life insurance products) has been the Coronavirus pandemic.

Sales clearly suffered during the pandemic, with the falls in intermediated channel sales and rotation into (and out of) direct channels discussed previously occurring across the market.

However, despite an initial sharp spike in NTUs (26% to 40% in Q2 and Q3 of 2020, respectively), lapses slowly improved, from a high of 23% in 2020 Q1 to a 2-year low of 20% in 2021 Q2.

This improved persistency could be due to an increased appreciation of the importance of cover, and this is corroborated by consumer responses – 79% of consumers stated that funeral insurance has become more important as a result of Covid.

Exhibit 8: Change in Perceived Importance of Funeral Insurance after Covid



Source: NMG Funeral Consumer Study

Opportunities

One consistent theme is the need to resolve the glaring issue of persistency. Various strategies are already playing out as outlined earlier in this article.

Despite an initial drop in sales, Covid has lifted consumer awareness and demand for cover.

There also appears to be a gap in the market between funeral and underwritten insurance, where we're starting to see the emergence of 'semi-underwritten' or non-underwritten life products. The topic deserves its own article, but there will be key questions such as:

1. Which group of providers are best placed for this? Those already in funeral or mass market, or those already in the underwritten space?
2. Which dynamics (e.g. sales channels) will be similar to the funeral market and which will look more like the underwritten market?

We believe funeral insurance will continue to be an exciting and dynamic sector going forward, and opportunities such as those we've outlined will result in improvements for customers and insurers alike.

By Evan Baars

By Guy Mitchell