ANDREW HALL
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THE PROTECTION GAP AND WHAT IT MEANS FOR AUSTRALIA

Thank you Maurice.

It's a pleasure and honour to be here in Canberra this afternoon.

I acknowledge we meet on the land of the Ngunnawal people and pay my respects to elders past, present and emerging.

Canberra is a city nestled between Red Hill, Mount Ainslie and Black Mountain – a place that it is said to have provided protection for the Ngunnawal people from the worst of the natural elements for thousands of years.

Over recent years however it has proven to be a national capital that has endured its fair share of natural disasters with its state counterparts.

From bushfires to destructive hailstorms, modern Canberra in this sense is no different to the rest of the country it serves.

There is also great significance for me in talking to you, the members of the Press Club, about the impact of natural disasters on our country.

I actually started my career in the mid-90s as a journalist at the Grafton Daily Examiner, and one of the first big stories I covered, alongside a throng of big-name journos flown into town, was a major flood in the Clarence Valley.

I doubt there's a journalist here today that didn't cut their teeth covering a natural disaster of some kind.

Many of you as members of the Parliamentary Press Gallery have followed a Prime Minister to a flood, cyclone or bushfire recovery operation.

Like election campaigns, they are the rare moments when politicians engage directly with a community in unscripted raw and emotional scenes.

Whether we have experienced them directly, or covered them as reporters, we all have some experience of natural disasters.

In Australia it’s inescapable.

Because the extraordinary story of this continent is that it is a place of incredible beauty as well as terrible harshness.

It is a land of risks that demands respect – and in return it draws out from us a determined resilience.

As a country, and as individuals, we all grapple with questions about risk and safety:

What risk in our daily lives is essential if we are to achieve our hopes and aspirations?

What risks can we remove, reduce or mitigate by diversifying or offsetting them?

And what risks must we avoid at all costs because the outcomes would be catastrophic?

Risk in our times

Across history, peoples have faced risk.

We are living in a time now though when risk is being reassessed.

The certainties about how we see the world are changing.

Risk isn’t receding, it’s accelerating.

We have seen it for ourselves.

The Black Summer of bushfires.

East Coast flooding that became the most costly natural disaster in Australian history – and the second most costly natural disaster in the world last year.

The growing weather volatility – if it’s not La Nina it’s El Nino.

Inflation and the risk of ongoing and entrenched price hikes.

A worsening geopolitical environment, with democracies under threat.

The pandemic and wars that have undermined the reliability of international supply chains.

Increasing cyber threats to all sections of our digitally-based and run economy.

These phenomena are global megatrends.

And there's another megatrend we excel at.

Urbanisation and growing wealth in the very places most likely to be hit by extreme weather – towns and cities by the water and where the climate is warm.

All of these pressures have come together to create a perfect storm in insurance markets.

Risk is being repriced.

The pressures and costs are increasing. The trend lines are all going one way.

Because of these pressures, insurers' input costs are going up and up.

One of those costs is capital.

For the last two decades, Australians have benefitted from the global capital markets, who are partners in underwriting Australian risk.

One way this happens is through the global reinsurance market.

This is where Australian insurers buy their own insurance.

They do so to offset the risk inherent in having a relatively small customer base exposed to the same risks potentially happening at the same time.

Reinsurance is our way of accessing a wider pool of protection when disasters strike.

Year to year the financial performance of the insurance sector can be volatile, as we've seen in the years since the 2019 Black Summer fires.

Reinsurance allows insurers to smooth their losses, protecting themselves and the Australian financial system from the impact of significant loss – usually as the result of a large event.

And reinsurance is how global capital helps underwrite Australian risk.

Australia used to be seen by reinsurers as a good hedge against events in the northern hemisphere such as Japanese earthquakes, or Florida hurricanes.

Not anymore.

Because of the trends I've just outlined – which are happening across the globe – Australia is being re-assessed by reinsurers.

After wearing losses over several years in the Australian market they are having to put through significant increases in the cost of their cover.

This, along with other costs, is ultimately reflected in the price of premiums – from Parramatta to Perth, from Townsville to Tasmania.

Some of the biggest price adjustments in nearly two decades have gone through the insurance system.

All of this is occurring at a time when homeowners have experienced 13 successive interest rate rises over 18 months.

Amid a cost-of-living crisis, with interest rates and energy costs increasing, families and households are making difficult choices about their budgets.

The Protection Gap

What this is creating is a growing protection gap.

A protection gap is the extent to which potential economic losses are not covered by private insurance.

It's the gap between the cost of recovering from an unexpected event and the insurance that's in place to cover that event.

It's the difference between what should or needs to be insured and what isn't insured.

It can exist in a household when the sum insured doesn't cover the cost of a rebuild.

And it can exist across regions and states, when governments are called on to fund more of the community recovery costs because there is insufficient private insurance in place.

As one of the great home owning nations, Australians know how important insurance is.

Despite the recent increases in premium costs, we can see that Australians have tried to maintain their cover.

But with households and businesses being squeezed, more and more are looking at reducing or foregoing their insurance coverage.

We are seeing a rise in people who are not insured or are underinsured – particularly in those areas where the threat of high natural peril risk is driving the biggest increases in premiums.

Recent modelling by the Actuaries Institute estimated that more than a million Australian households face home insurance affordability stress – and that this is most pronounced in areas with high cyclone and flood risk.

This is also being felt in the strata insurance market, particularly in our cyclone-prone north, where anecdotally brokers are reporting significant increases.

Since 2017 the level of car insurance amongst car owners has fallen from 75 to 73 per cent, widening the protection gap.

This coincided with an increase in premiums of 39 per cent while car repair claims costs for insurers rose 43 per cent, double the rate of inflation for the same period.

This is because a small ding that might have once sent you to the panel beaters for a straight-forward repair, now requires fixing and testing the complex sensors that are used for car navigation and safety systems.

In home and contents, as well as car insurance, the protection gap is widening.

More and more people are crossing their fingers and hoping that luck will hold their way.

As the protection gap widens there will be serious implications.

The first is the additional vulnerability that households and families, particularly middle- and lower-income earners, will face if the worst happens.

It means that when disasters and accidents occur, they disproportionately upend the lives of people particularly in vulnerable lower socio-economic groups.

It will also mean pressure on banks and our financial system overall.

Extreme weather events in areas of growing population mean banks are increasingly exposed to the protection gap risks.

It will also place greater pressure on governments to bear recovery costs.

A greater reliance on government and not the private sector will mean that taxpayers will carry much more additional risk, putting even more pressure on government budgets.

So the challenge before the industry and all levels of government is, how can we manage this widening protection gap?

What can we do in partnership with all levels of government, other stakeholders like banks, and customers, to alleviate the pressure on premiums, and not let the gap turn into a chasm?

For the industry this is the key problem to solve in this time of dramatic change.

Insurance Council of Australia

We must reflect on our recent experiences as an industry as well as identifying the trends before us.

I want to make observations of what we have identified so far.

Recent Experiences

Since the Black Summer bushfires in 2019 Australia experienced 18 insurance catastrophes, including the record-breaking east coast floods of February and March last year.

These generated almost one million catastrophe claims totaling almost 17 billion dollars.

Last year alone, the insurance industry in Australia paid 302,000 disaster related claims, which caused more than seven and a quarter billion dollars in insured losses.

Six billion dollars of this was from one event – the February/March east coast floods.

After this event, 60,000 insurance professionals worked tirelessly, day and night, to address unprecedented challenges.

Claims jumped from 2,000 a day to 10,000 a day.

An additional 2,200 claims staff were brought on board to help with that influx of claims.

On the ground, insurers helped people start the long and often slow process of rebuilding their lives.

For the vast majority of impacted customers their insurer responded in the way they expected.

Their claim was assessed and completed, and they were able to move on with their life.

However we know that the extreme volume of claims last year did put unprecedented strain on the people, systems and processes, which impacted the experience of too many customers.

The industry has apologised where we didn't meet customer and community expectations.

Given the scale of the floods it's not surprising that insurers were challenged.

The sector is committed to improving and making sure we can adequately and appropriately respond to future extreme weather events.

That's why we commissioned Deloitte to undertake a review of how insurers responded to the east coast floods.

We take our obligations to customers and the community extremely seriously.

I think it's a sign of maturity that the industry was prepared to hold a mirror up to itself and ask, how do we become the global leaders in managing extreme weather events, and make sure we don't fall short in meeting our obligations?

What can we do to make sure this doesn't happen again?

Because rest assured, this type of event will happen again.

Our changing cities

Globally we are seeing an upward trend in catastrophe costs.

In 2022, disasters worldwide caused 275 billion US dollars in damage, of which 125 billion dollars – or less than half – was covered by insurance.

Worldwide, losses from catastrophes have exceeded 100 billion US dollars just five times since 1970, but three of these were in the last six years.

This is due not just to the increased frequency of extreme weather events, but the worldwide increase in urbanisation.

We are seeing an increasing concentration of people and assets in locations that are exposed to extreme weather risk.

To give a local example, adjusted for inflation Cyclone Tracy cost the insurance industry 1.8 billion dollars at Christmas time in 1974.

Today – because of the number and value of buildings and other property in Darwin – that same storm would result in 7.4 billion dollars in losses.

Likewise, the 1999 Sydney Hailstorm which caused 3.3 billion dollars in inflation adjusted losses would cost nearly nine billion dollars if it occurred today.

And it's not just the growth in the number and value of buildings, it's how we build our cities.

Our cities are covered in concrete.

This causes 'soil sealing', which exacerbates flooding because concrete and bitumen stops water going into the ground – but as everyone knows water needs to go somewhere.

Over the last 20 years, the increase in soil sealing in Australia's five biggest cities has been the main contributor to a seven per cent increase in annual expected losses from floods.

Climate Change

Insurers and reinsurers know from the data that the catastrophes of recent years represent an evolution of weather patterns that are profoundly different from what we have experienced in the past.

The expectation of insurers is that climate change will also impact the scope and nature of weather-related catastrophes in coming years.

What does this all mean for Australia?

According to the Royal Commission into Natural Disaster Arrangements, we will likely see an increase in category 4 and 5 cyclone frequency, and a further southern extension of tropical cyclones – and as we do there will be more people living in their paths.

As well, we will witness an increase in intense rainfall, an increase in coastal and flash flooding, and an increase in extreme fire weather.

These will put pressures on all parts of the economy, not just for those communities and households in the direct line of a flood, fire or cyclone.

To give an example of what I mean, following last year's extreme rains across New South Wales, the NRMA received 90,000 calls for wheel and tyre damage caused by potholes.

New South Wales taxpayers picked up a 2.5 billion dollar bill to fix 128,000 potholes over 13,000 kilometers of road.

That's just for repairing roads, not building new ones.

The costs of more extreme weather will play out across the economy.

Direct costs of extreme weather events to Australians are going to rise 5.1 per cent per year – before inflation – until 2050, with a yearly cost to Australia by that time of 35 billion dollars.

These costs aren't here yet but they are coming, which means mitigation of risk is crucial.

As an industry, we are determined to keep driving the debate around mitigation because it is the only way we can limit future costs.

We've done that in the past when we advocated for seat belts and random breath testing, or for building standards that made smoke detectors an integral part of Australian homes.

Following the construction of a flood levee in Roma, Queensland, premiums dropped by an average of 34 per cent.

A joint program between the Queensland and Federal governments to improve the resilience of homes to extreme weather in that State saw premium reductions of up to 25 per cent.

When you mitigate risk, you don’t just better protect lives and property, you take pressure off the cost of premiums.

That must be the focus of industry and government now and in the future as we tackle the protection gap.

We must derisk, we must remove impediments to insurance, and identify ways of removing costs from insurance products.

There are long-term, medium term and immediate actions we can take to help make sure that insurance remains affordable and accessible to Australians into the future.

Let me now address those options.

Long-term action to reduce the Protection Gap

I want to start with long-term actions because they are the hardest area to deal with.

It is the most difficult because none of us, including governments, are particularly good at making decisions where the costs are incurred now and the benefits take time to be realised.

I appreciate there are great pressures on governments for land release.

We have a serious issue regarding housing affordability, where a generation of Australians is struggling to even enter the housing market.

Record levels of immigration are exacerbating this problem.

The temptation for governments to take short cuts on land release is real.

But the lesson of past years is that we must incorporate natural disaster risk into decisions about land releases.

Last December, National Cabinet declared that the days of putting homes on flood plains must end.

We agree.

The Sunday Telegraph's recent front page got it absolutely right when it said about the Hawkesbury-Nepean that we are releasing land that is in "bathtubs".

It has to stop.

The recent decision by the Minns Government to halt further development in parts of Sydney's north-west due to flood risk was the right one – it was the right decision on planning grounds and is the kind of long-term thinking we need to see more of.

And it's not just driven by a need for cheap land.

Australians love nature. We love being by the water. And we love the sun.

All too often, we have built our homes in places where we can touch and feel and absorb nature – in bushland, on river frontages, and backing on to beaches.

But in so doing, we have put ourselves on floodplains, in fire-prone bushland, or coastal areas in direct paths of cyclones.

We have ignored the red flags of nature.

Too often we have seen warnings of something called a "one in one hundred year" event as an invitation to roll the dice.

The problem is that we are finding those old probabilities – the risks of cyclone, fire and flood – are increasing.

And those probabilities will continue to increase as the climate changes.

So we need to plan better, particularly as our population continues to grow.

Medium term action to reduce the Protection Gap

In the medium term, we must mitigate risk – not just to put downward pressure on premiums but to better protect lives and property.

In 2014 the Productivity Commission found that 97 per cent of disaster funding was spent after an event, with just three per cent spent on mitigation measures before events.

This has to change, and the good news is that it is changing.

The Federal Government – led by Assistant Treasurer Stephen Jones and Emergency Management Minister Murray Watt – is demonstrating a real commitment to addressing the protection gap by coordinating the various branches of government.

As part of its first Budget, the Federal Government launched the Hazards Insurance Partnership that has become a single touchpoint between government and the insurance industry – to share data and information around mitigation infrastructure and reducing risk and insurance costs.

We welcomed the establishment by the Federal Government of the two billion dollar Disaster Ready Fund for disaster mitigation projects.

Matched by states and territories, over time investment at this scale is projected to reduce costs to governments and households by 19 billion dollars.

However, given the scale of the challenge, the program should be expanded to be permanent and ongoing, with a focus just on hard infrastructure.

The amount of money invested by governments should at least rise with inflation, ensuring that it doesn't decline over time.

We can mitigate risk by further strengthening the National Construction Code.

We must build resilience into the Code.

Homes must be built that are durable for the environment in which they sit – for the next one hundred plus years.

Yes it will add to the upfront cost of construction. But estimates are that strengthening the Code can reduce the costs from cyclones by up to two billion dollars a year.

We are also working with government to constructively identify ways of reducing regulatory duplication across the industry.

The “twin peaks” of insurance regulation – APRA and ASIC – have served Australia well.

No one ever wants to see another insurer collapse like HIH.

But work can be done to reduce duplication of effort – and reduce unnecessary costs.

Giving the financial services sector good line of sight of proposed regulatory changes would allow us to understand and plan for changes that have significant – and costly – operational impacts.

This works in the UK through their Regulatory Initiatives Grid, and I know it’s an idea that’s supported by the banking sector and others.

I note the comments of ASIC’s Chair Joe Longo in Melbourne yesterday that Australia is looking at how it could adapt the concept here.

We also need to ensure our strong regulatory environment doesn’t stifle innovation in insurance products, delaying or limiting our opportunities to take up new ideas here in Australia.

It’s not just the rules that can be the barrier to innovation, but also the compliance burden.

When insurers have compliance enforcement teams that start to outnumber those managing claims, the balance tips and the costs increase.

We must always be checking we have the sensible balance right.

As a country, we have also become increasingly litigious.

We may have a British legal heritage but we are fast mirroring the worst aspects of the US system.

That has contributed to court determined payouts impacting on public liability cover, which has over the last three years experienced combined loss ratios above 100 per cent and peaking at 120 per cent.

In other words, this line of insurance has been losing money.

Public liability cover is vital to the economy, to businesses, and to the community.

But as public liability insurance prices rise in response to the growing risk of expensive court action, this impacts the ability of community groups like P&Cs, RSL clubs, charities and sporting clubs to undertake their activities.

Likewise, it affects every business, from the smallest operation to major projects.

Without public liability and professional indemnity coverage, our economy would grind to halt.

Insurance is a vital precondition for many businesses, and we recognise that being uninsured or underinsured is not an option.

This was the point made by Business NSW in their report released just this week.

We need to have a community debate about civil liability settings – because the trend in litigation practices and outcomes is putting great pressure on providing insurance in this market.

Immediate action to reduce the Protection Gap

So what are the immediate actions we can take to reduce the protection gap?

The most immediate area where we can actively reduce the insurance gap by bringing down the cost of insurance is in relation to taxes and charges.

The second biggest component of the cost of a premium, after the peril risk, is taxation.

I'll repeat that: The second biggest component of the cost of a premium is taxation.

So when we talk about insurance affordability, know that there is something all governments could do to bring down the premiums immediately.

I'm not suggesting we remove the GST, which is charged on nearly every good or service.

With the exception of right here in the ACT, insurance customers pay state stamp duties of around ten per cent, plus the GST.

These taxes have the greatest impact on low-income earners and the most vulnerable – and put their futures at risk.

In New South Wales all insurance customers have also been paying an Emergency Services Levy, which by itself has been adding up to 18 per cent to the cost of home insurance.

But I'm going to praise the Minns Government once again for its announcement just last week to abolish this terrible tax.

We have been campaigning for the reform of the Emergency Services Levy for years, and this change is just the sort of approach we need to see more of from state governments.

The Tasmanian Government too, is undertaking much-needed reform in this area.

Because for a long time, insurance has been seen as a taxation cash cow, little different than alcohol and cigarettes.

But insurance isn't a cigarette or a vaping product that harms your health; nor is it an alcoholic beverage where tax and price can moderate and temper excessive behaviour.

Nor is it a one-off purchase like a home.

No, insurance is a community good. A community good that is purchased every 365 days.

It allows a community to share its risk. To make risk more manageable for individuals.

By pooling and pricing risk, it means people can be protected on a bad day or on their very worst day.

This is the private sector managing risk.

Not just managing risk, but taking that risk off government.

If insurance policies for houses or cars did not exist, or were priced out of reach, then the population would demand it of the government.

But if the protection gap worsens, there will be calls for governments to close that gap and provide that protection.

For the sake of our future protection and productivity, Australian governments at the state and Federal level must have an eye on reform of insurance taxes.

The Federal Government is the insurer of last resort for our states.

There is a clear opportunity here to think about how to incentivise states to lower their insurance taxes to ensure more people have the private cover that will protect them.

It's not our Australian ethos that only wealthy Australians can be protected from catastrophic loss but the rest of the community must take its chances.

We must manage the protection gap so this does not happen.

Conclusion

Our job is to help Australians manage their risk.

Every working day, the insurance industry in Australia pays out 150 million dollars in claims.

That's 150 million dollars helping Australians deal with the unexpected.

Insurance is vital for households, community groups, businesses, and the productive capacity of the economy.

Insurance Council of Australia

We must keep insurance affordable and accessible – and we can do it, by working in partnership on the challenges before us.

By focusing on the trends, by mitigating risks, and removing unnecessary costs.

Australia needs to be able to tell a better risk management story.

We need to show the world that we are leaders in building communities that are resilient and durable to the climate they are living in for the next 100 years or more.

We need to show the world we are willing to learn from past mistakes and not repeat these in the future.

We need to provide our fast-growing population with safe places to live and do business.

And as where I started, we need to provide fewer opportunities for the Press Gallery to travel with Prime Ministers to the aftermaths of extreme weather events.

We need to lessen the impact of living in Australia on Australians.

By working together, governments, insurers and communities, we can prepare for the future and in so doing, ensure we don't end up with two classes of Australians – those who can insure against risk and those who can't.

Thank you.