Emerging Insurance Risks - An Overview

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"The biggest risk is not taking any risk"

- Mark Zuckerberg, Chairman, CEO and Co-founder of Facebook

Insurance is about anticipating, understanding and addressing risks with major focus on facilitating the risk transfer. It is as much necessary for insurers as it is for the insureds, to identify risks as they emerge and take the required steps to prevent or eliminate them in order to avoid the losses ensuing from the actualization of the risks or prevent further losses.

Key words : Emerging Risks, Insurable Risks, Risk Management

Introduction

Emerging risks are new risks or potential risks that become apparent in new or unfamiliar conditions (International Risk Governance Council, 2010).[i]

- **New Risks :** Such risks are not foreseen and their impact is unpredictable. While we are all very excited about Artificial Intelligence (AI) and the immense possibilities it presents for the progress of mankind in the near future, it is a new risk. It was not seen as a risk earlier, and, its impact has also not been estimated accurately. More on AI will be dealt with in the subsequent paragraphs.
- **Older Risks in Newer Forms :** The impact of these kinds of risks have been felt earlier. But, in the changed circumstances, the likely losses from these types of older forms of risks may become bigger in scale, more complex, and very unpredictable. These appear as new avatars of the old ones. Climate risk earlier was seen more as a property risk; but now climate change-related risks are considered more in the context of the environmental changes and also as social governance issues. Even though

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pandemics were prevalent previously, the loss of life and suffering caused by Covid-19 (in 2020-21-22 running) has been colossal world-wide.

From time to time reputed agencies bring out the list of risks, how these are perceived and managed and analyse their fallouts globally. Some of such reports are:

- *Allianz Risk Barometer* : This annual report identifies the top corporate risks.
- *The Global Risk Report* by the World Economic Forum forecasts economic risks.

Characteristics

Broadly, the following characteristics are noteworthy for the emerging risks:

- Limited data
- Inadequate understanding
- Uncertainty in terms of probability, potential impact, and likely losses
- Difficult to quantify

Emerging Risks

The risk landscape is changing rapidly resulting in repercussions in unexpected ways. A brief description of emerging risks are presented below.

- **Pandemic:** The dictionary meaning of pandemic is an outbreak of a disease that occurs over a wide geographic area and typically affects a significant proportion of the population. Humanity since creation has endured many deadly pandemics over the centuries. But, the wide-ranging effects of the current Covid-19 are well known for any recapitulation. Global (re)insurers have already booked $26 billion for Covid-19 losses in 2020-21, but a high degree of uncertainty still remains about the ultimate pandemic cost (Willis Re).[ii]
- **Cyber Risks:** These are also a much-talked about issue. These are prevalent risks across all industries in most of the countries causing cascading and collateral effects. Cyber risks permeate every aspect of our lives – whether it is for companies or individuals. These risks are becoming much more pronounced during the current Covid-19 pandemic period. A McAfee report[iii] estimates global cybercrime losses to exceed $ one trillion.
- **Artificial Intelligence:** This computer-based technology has a wide-ranging applicability capable of performing tasks that are akin to human intelligence

activities - comprising: understanding, memory and will. The most common applications of AI enable machines to learn from experience (data), adjust to new inputs and perform human-like tasks with ease. *An Artificial Intelligence Algorithm manipulates a combination of inputs and outputs simultaneously in order to "learn" from the data and produce outputs when new inputs are keyed in. Biased and ill-informed inputs have the potential to cause significant damage, and its application may result in* algorithmic issues, privacy violations, harmful applications that can endanger the security of individuals, societies and nations globally.

- **Nano Technology**[iv] refers to the study and application of extremely small things and can be used across diverse sciences, such as chemistry, biology, physics, medicine and engineering. Nano technology has definitely improved the precision in various areas of operation. It offers significant benefits in areas of health and the environment. But it also presents potential risks like health-side effects, privacy-breach issues and weaponizing technology and so on.
- **Genetic Modification:** With the rise of Genome sequencing and editing tools such as CRISPR (Clusters of Regularly Interspaced Short Palindromic Repeats)/Cas9, site-specific DNA mutations in human DNA can be induced. Off-target genome editing effects can lead to dangerous risks that have implications for all branches of insurance - Life, Health and Liability .
- **Climate Risk:** Natural catastrophes, unseen in terms of scale and location, are becoming increasingly common. Forest/bush fires are rampant. Global warming is causing Arctic ice to melt causing an increase in the sea level and flooding. Pollution of all kinds is causing havoc. Earlier climate risk was seen in the context of property damage. But, now, it is becoming a major corporate governance issue for the board rooms as well. It has the potential to cause management liability insurance claims. Insurers are called upon to address this risk not only as risk carriers but also as capital providers. Whilst on the subject of climate risk, recent media reports indicate that Zurich Insurance Co. Ltd.[v] is increasing pressure on companies it invests in to set climate action targets in line with the Paris Agreement and limit global warming to 1.5^{0}C.
- **Digital Distortion and Digital Misinformation:** With the exponential growth of the social media, without due regard to the authenticity of the information disseminated, distorted/wrong/false information is being circulated. Such news

travel fast and get spread far and wide, causing trust issues to the organizations and individuals these relate to.

- **Reputation Risk:** Damage to reputation is seen as a major concern by corporate boards particularly because of the speed of spread and the potential for direct and indirect loss/harm. While some insurance covers are available to contain the damage - more like crisis management expense - determining the value of reputation/brand equity is a huge challenge.
- **Geopolitical Risks:** These issues relate to the political sphere linked to geographic space or significant changes in the administrative structures as happened with Brexit deal and Hongkong in the recent past. It could lead to a change of government also in some countries, which may impact the unpredictability of future policy issues and action.
- **Social Inflation:** Increase in claims outgo due to inflation forecasts, increased litigation, litigation funding and liberal judgments. While these trends are currently seen only in a few jurisdictions like the USA, it may not be long before it reaches other jurisdictions as well.
- **Regulatory Risks:** These are possible governance issues. When governments start taking actions in response to unfavorable actions of other governments or because of domestic pressure, these become a matter of concern notwithstanding the fact that there are redressal mechanisms available in conformity with national laws and/or international agreements – both bilateral and multilateral.

Emerging Risks : Outcomes :

If there is no risk involved, there would be no need for insurance. Emerging risks do generate new opportunities for the insurer. When not addressed or addressed inadequately, the potential risks are likely to result in widening the protection gap, increasing the trust deficit, and also in lamenting on the lost opportunities.

- **Widening the Protection Gap:** Insured vis-a-vis Uninsured losses. When appropriate and adequate insurance covers are not available to address any risks, and these risks cause losses, it increases the uninsured losses contributing to the widening of the protection gap.
- **Trust Deficit :** dents the image of the industry. When insurers fail to provide the required covers to address the emerging risks, it is likely to generate an adverse

image and cause trust deficit for the industry as a whole. It may invite the attention of regulators. Have we not realized how regulators have nudged insurers to urgently launch corona-specific policies?

- **Opportunities Lost for Insurers:** Insurers are in the business for assuming risks prudently with proper underwriting policies, supported by suitable risk management measures. If risks are completely avoided driven by unadmirable caution, they would miss the opportunities. Risks not embraced would become opportunities missed.

How Do/Can Insurers Address the Emerging Insurance Risks?

By :

- Continuously scanning the risk horizon for signals and ascertaining the evolution of risks and their impact on customers and other stakeholders.
- Studying the insurability and market expectations relevant to the risks identified.
- Interacting with all the stakeholders – not just the end-users.
- Educating customers about the product features in terms of benefits to them in order to have a wider reach.
- Studying and developing methods to address risks for mitigation and working on risk quantification with the help of data from traditional and non-traditional sources.
- Adopting artificial intelligence and machine learning to help to build risk prediction models.
- Focussing on holistic solutions rather than dwelling on just profitable individual insurance policies. It is necessary to look beyond indemnification and touch upon prevention and re-mediation. Whilst on this topic, the insurance industry, in India and globally, deserves appreciation for its willingness to develop complete solutions rather than just insurance policies concerning cyber exposures.
- Using technology in order to address the emerging risks and taking a more proactive role.
- Employing Coopetition[2] vs Competition. In order to face the emergent risk contours, which are yet unknown, it is advisable to pool resources of the industry

and work in a cooperative environment rather than look at every issue through the prism of competition only.

- Crowdsourcing ideas about risk notions supported by automated analysis and detailed studies. Swiss Re SONAR (Systematic Observation of Notions Associated with Risk) process is a good example.
- Applying Alternative Risk Transfer (ART) Solutions. When the nature of the risk gets too complex, and the size of losses looks too overwhelming, conventional insurance policies may not be sufficient. This is when ART solutions should be applied.
- Making course corrections in products and processes to meet customer expectations without compromising on business sustainability.

Risks abound all around and will always be there whether one wants it or not. Insurance is not about operating through the rear-view mirror. Insurance is about looking far ahead with ingenuity. Insurers need to embrace the insurable risks after elaborate and diligent evaluation.[1]

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[1] *Disclaimer: The information contained and ideas expressed in this article represent only a general overview of the subjects covered. It is not intended to be taken as advice regarding any individual situation and should not be relied upon as such. Insurance buyers should consult their insurance and legal advisors regarding specific coverage and/or legal issues.*

[2] *The word Coopetition refers to cooperation between competing organisations (investopedia.com/terms/c/coopetition.asp#:~:text=Coopetition%20is%20the%20act%20of,producing%20complementary%20or%20related%20products.)*

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