SA CTP
Market briefing

Review of the risk premium for the 2021/22 underwriting year

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1 Risk premium

$143.20
▲ $8.30

The advised risk premium for the 2021/22 underwriting year,
excluding inflation and discounting

Taylor Fry estimates the components of the risk premium for the South Australian CTP scheme and advises the CTP Insurance Regulator on these components. The Regulator integrates our advice with its own views to set a floor and ceiling for insurer CTP premiums.

Due to COVID-19 related restrictions, traffic volumes reduced significantly since end of Mar-20 which led to fewer accidents. We have set our premium advice on the basis that COVID-19 will not have a material impact on claims frequency in the future.

Table 1 shows the risk premium for the 2021/22 underwriting year as the product of the advised claim frequency and average claim size, based on data to 31 December 2020. We examine claim frequency and size in detail, separately, in Sections 2 and 3.

Table 1 – Advised risk premium for 2021/22 underwriting year

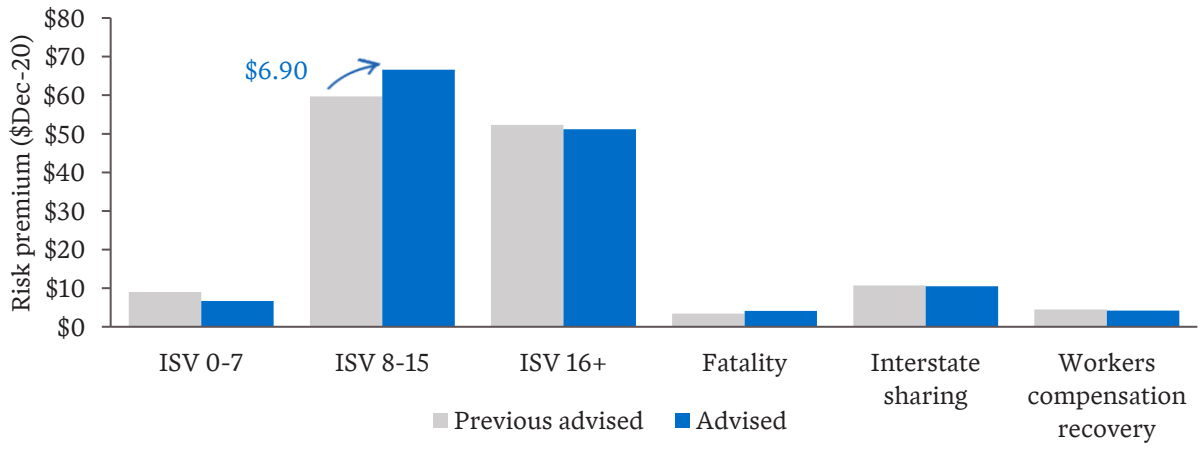
Claim frequency represents the number of reported claims per annual policy		0.153%
Average claim size represents the expected ultimate cost of a reported claim	×	$93,299
Risk premium is the expected future cost per policy of claims made to insurers		**$143.20**

Our advised risk premium is $8.30 higher than our advised risk premium at the previous annual review (based on data to 31 December 2019) because:

- ▲ $4.80 increase due to inflation over the year to 31 December 2020
- ▲ $3.50 due to updated assumptions for claim frequency and average claim size.

Figure 1 shows the revised assumptions in six segments based on claimants' Injury Scale Value (ISV), fatalities, interstate sharing claims and workers compensation recovery. The previous advised has been adjusted to include inflation in the year to 31 December 2020. The ISV 8-15 and ISV 16+ segments make up 82% the risk premium.

Figure 1 - Risk premium assumptions by segment



The $3.50 increase in risk premium due to updated assumptions is driven by the ISV 8-15 segment.

2 Claim frequency by segment

0.153%

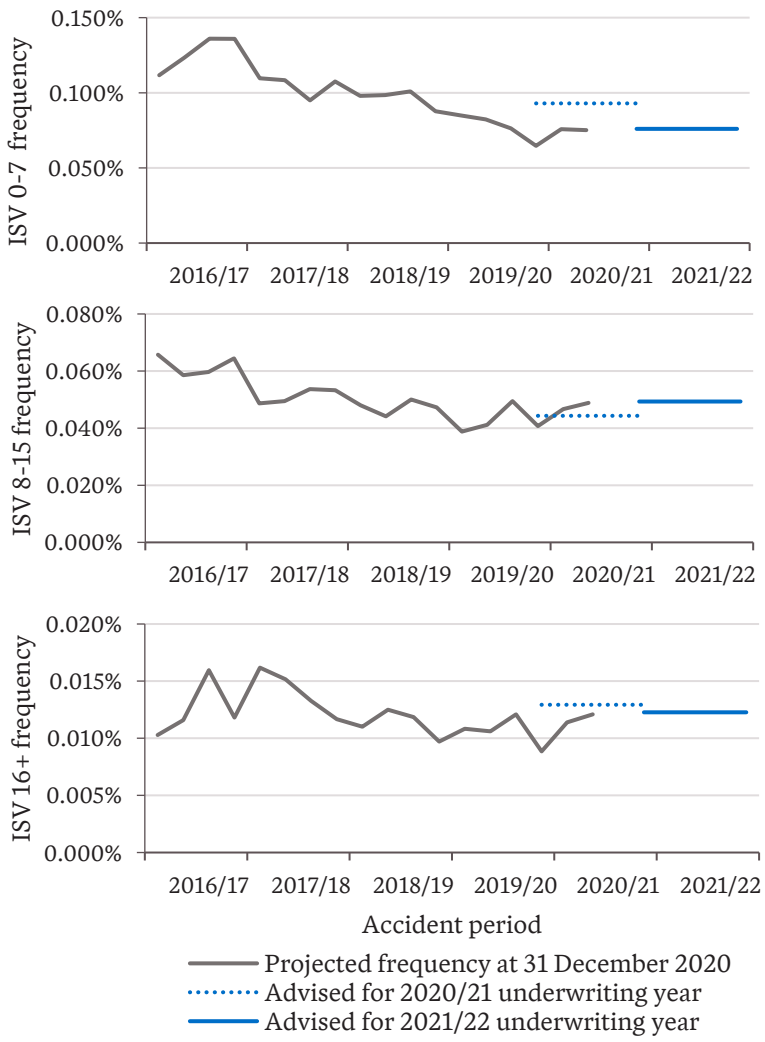
▼ 8%

The advised claim frequency for the 2021/22 underwriting year
which represents the number of reported claims per annual policy

Taylor Fry reviews the claim frequency by segment at each annual review. Claim frequency is the rate of CTP claims per annual policy.

Figure 2 shows the claim frequency for the three most frequent claim segments - ISV 0-7, ISV 8-15 and ISV 16+. These segments constitute 89% of claims. We compare the advised frequency for the 2021/22 underwriting year to the advised frequency for the 2020/21 underwriting year (previous review) and the projected frequency for previous periods. We have adjusted claim frequency for accident periods Mar-20 to Dec-20 for the impact of reduced traffic volume due to COVID-19.

Figure 2 - Claim frequency for major segment



We advise an **ISV 0-7 claim frequency of 0.076%** down 18% compared to a frequency of 0.093% at the previous review.

We observe more ISV 0-7 claims having their ISV revised upwards and moving to ISV 8-15 segment than was previously anticipated using MAC experience. Consequently, we advise an **ISV 8-15 claim frequency of 0.049%** up 11% compared to a frequency of 0.044% at the previous review.

We advise an **ISV 16+ claim frequency of 0.012%** down 5% compared to a frequency of 0.013% at the previous review.

The other segments – fatalities, interstate sharing and workers compensation recoveries – contribute 0.016% to the overall frequency (10% of claims).

3 Finalised average claim size

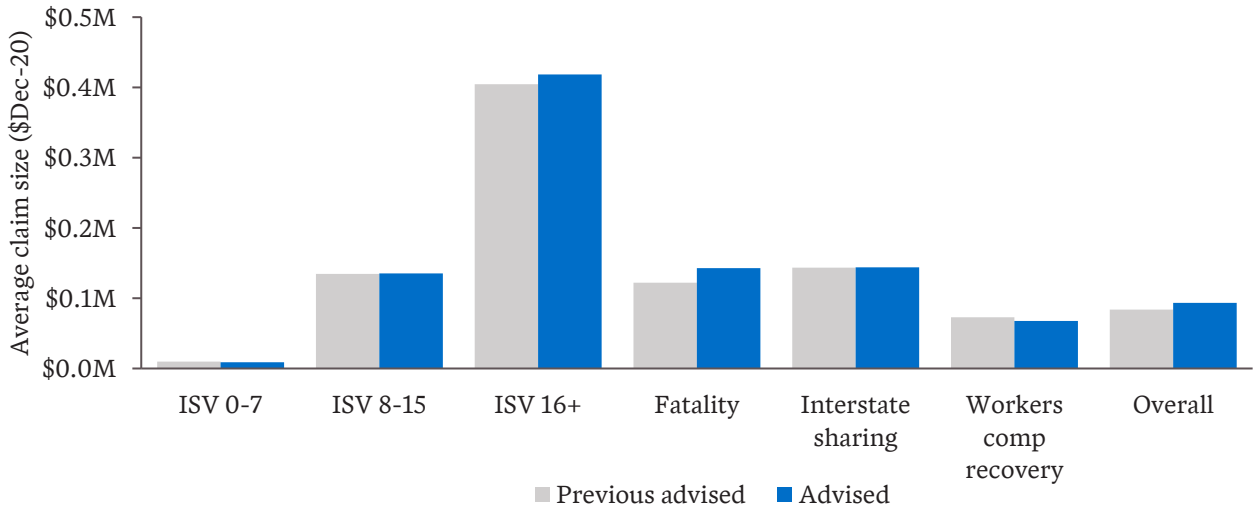
$93,299
▲ 11%

The advised average claim size for the 2021/22 underwriting year
which represents the expected ultimate cost of a reported claim

Taylor Fry reviews the average claim size by segment based on finalised claims at each annual review. Average claim size is the amount of compensation a claimant receives.

Figure 3 shows the revised assumptions in six segments. The previous advised has been adjusted to include inflation in the year to 31 December 2020. The size of compensation a claimant receives is highly dependent on the claim's ISV because access to future economic loss and benefits and general damages is dependent on ISV.

Figure 3 – Revised average claim size assumptions by segment and overall



Within each segment, we have kept the average claim size stable.

The 11% increase in overall average claim size is driven a change in segment profile because we advise a lower frequency for the relatively low cost ISV 0-7 segment and higher frequency for the relatively high cost ISV 8-15 segment.

4 Risk premium sensitivities

There is uncertainty in the assumptions underlying our risk premium estimate. There is a risk that the claim frequency and size that ultimately emerge for the 2021/22 underwriting year turn out to be different to our assumed values.

The privately underwritten environment has a short history and relatively few finalisations which leads to more uncertainty than for a mature scheme. With one more year of experience, the uncertainty is less than at the previous review but still exists. The main source of uncertainty around the risk premium is high ISV claims (ISV 8+).

High ISV claims segments constitute most of the risk premium and we have limited experience since the 2013 tort reforms on which to base our estimates. Specifically, there is uncertainty around our estimation of:

- Frequency: This year we experienced significantly more claims transitioning into the ISV 8+ segments after having their ISV revised upwards. While we have allowed for transitions to be higher in the future, there is a risk that this assumption is inadequate if the increase in claims with psychological injuries increases the mobility of claims in the ISV 8+ segments.
- Average claim size: We have not observed many late finalisations post-reform from the high ISV segments. We rely on the extrapolation of observed claims experience or modified pre-reform data to estimate the average claim size for late finalisations.

Table 2 illustrates the impact of uncertainty for high ISV claims.

Table 2 – Uncertainty scenarios for high ISV claims

Scenario	Risk premium impact
Transitions to ISV 8+ segment occur at 20% more than assumed	+ $10
Late finalising ISV 8-15 claims are over- or under-estimated by 20%	± $4
Late finalising ISV 16+ claims are over- or under-estimated by 20%	± $6

We consider that our advised risk premium appropriately balances these uncertainties and is a reasonable central estimate of risk cost using experience up to 31 December 2020.

5 Economic assumptions

-0.98%
▲ 0.99%

The economic gap for the 2021/22 underwriting year
The difference between the investment return and the projected inflation rates up to the time of claim payment

The risk premium from Section 1 is uninflated and undiscounted. To allow for claims inflation and investment returns, Taylor Fry reviews the timing of claim payments, risk-free investment returns and projected inflation.

Economic gap

The economic gap is the risk-free rate of return *minus* the SA Average Weekly Earnings (AWE) inflation rate. A higher economic gap translates to a lower CTP premium. Table 3 shows the projected risk-free rate of return and the projected AWE inflation rate to determine the economic gap. We have switched to a new market-based approach to forecast wage inflation because it is more stable than our previous Deloitte Access Economics forecast based approach.

Table 3 – Economic gap assumptions

Risk-free rate of return	**1.39%** (▲ 0.72%) p.a.
AWE inflation rate	**2.37%** (▼ 0.27%) p.a.
Economic gap	**-0.98%** (▲ 0.99%) p.a.

We have increased the economic gap in line with the 0.72% p.a. increase in the risk-free rate of return and the 0.27% p.a. reduction in wage inflation.

Superimposed inflation

Superimposed inflation is claim inflation in excess of AWE. We assist the Regulator in adopting a superimposed inflation assumption.

The 2013 tort reforms make it difficult to use South Australian CTP experience to assess superimposed inflation. Superimposed inflation experience has been benign in CTP schemes in New South Wales and Queensland, averaging 0%-1% p.a. over the last 10 years.

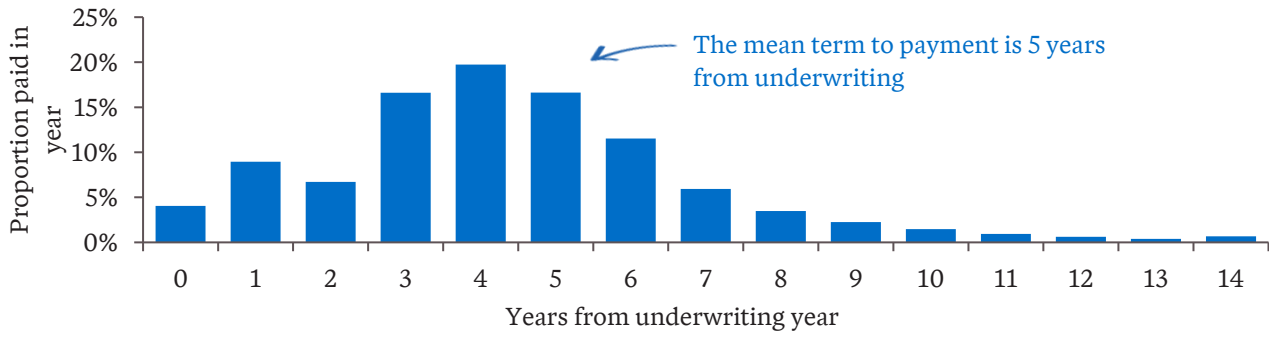
This suggests an appropriate **superimposed inflation rate of 0%-1% p.a.** over the medium term.

Timing of claim payments

The economic gap and superimposed inflation affect the risk premium more as the timing of claim payments extends further from underwriting.

Figure 4 shows the timing of the claim payments following underwriting.

Figure 4 – Timing of claim payments



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