Infrastructure insurance can prevent costly financial outlay

The value of infrastructure insurance should not be underestimated, especially in light of government's planned budget spend of R3.2 trillion on more than 43 major infrastructure projects. This is according to Krushayev Moodley, manager of engineering at Lion of Africa Insurance, who says that insurers and brokers should not underestimate the business opportunities presented by construction, engineering and infrastructure development projects.

"This can be a very profitable sector for insurers to be involved in infrastructure project development as South Africa's building and engineering quality is currently of high standard. Due to the skill in the engineering arena these projects are properly risk managed, so the risk for insurers on big projects is relatively low," says Moodley.

He argues that insurers are protected as there are various technical reports and quality and safety inspections that have to be passed during the construction period, which allows the insurer to have sight of the construction conditions.

Municipalities must cover risks

"Although there is a lower than expected risk involved in insuring construction projects from a local authorities stand point, it is pertinent that municipalities take out sufficient cover against risks that could lead to heavy financial outlay when investing in costly public infrastructure projects of this magnitude. This is especially the case in South Africa, where the most common risk includes natural disasters such as fires or flooding," Moodley says.

He notes that the recent fires in St. Francis Bay in the Eastern Cape have amounted to millions of Rands in damages to residential property, and less than a month prior to this, floods caused over R1 billion in damages to infrastructure in the area. "To use an international example, Hurricane Sandy in the US is currently estimated to have caused over $20 billion in damages.

"These types of events are also becoming more common and invariably leave governments with a massive bill for repairs to infrastructure, if they have not adequately investigated insurance options and strategies. The premium on a R1 billion project for example, is relatively low when compared to the cost of massive damage that can occur. When looking at the risk benefit analysis, it makes good financial sense to insure a project."

Financiers require insurance

He argues that besides being a cost-effective way to insure risk against damages, banks and financiers often require an insurance plan before approving finance for a project. This was recently the case when government and Eskom were under pressure to secure funding for the development of the Medupi power station from borrowers, including the World Bank. It's been reported that Eskom's spend will peak at R350nbillion in the next three years to complete the new build programme, which includes Medupi and Kusile.

"Insuring such projects gives financiers an understanding of planned risk management. It is a cost-effective way to insure risk against damages. It is the broker's role in this process to manage a client's risk profile and advise where possible to mitigate all financial risks, to prevent devastating financial losses."

While a variety of different strategies can mitigate or eliminate risk, the process for identifying and managing the risk is fairly standard. "Brokers first identify and track the risks and thereafter estimate their impacts and perform risk assessments to weigh the probability of occurring. The last two steps in the process are to figure out ways to reduce risks and then prioritise the risk management procedures based on their importance," Moodley concludes.