

Future trends in insurance

A global perspective on the life and non-life sectors

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Agenda



- Global insurance industry overview
- Regional distinctions
- Global NED challenges
- Looking forward
- Sustainable success lies in simplification



Global insurance industry overview

Global Insurance Industry

Developing market growth out-pacing the rest of the world



World Insurance Market: Current view with historical growth rates

	<u>Americas</u>	<u>EMEA</u>	<u>Asia Pacific</u>	<u>World</u>
2011 Premium Income (\$B)				
– Life	654.9	993.6	978.7	2,627.2
– Non-Life	825.2	765.1	379.1	1,969.5
2011 World Share (%)				
– Life	24.9%	37.8%	37.3%	100%
– Non-Life	41.9%	38.9%	19.2%	100%
2006-11 Premium Growth (%)				
– Life	1.8%	1,5%	10.2%	4.3%
– Non-Life	2.4%	4.9%	12.2%	4.9%
2011 Insurance Penetration (%)				
– Life	2.9%	3.2%	4.0%	3.8%
– Non-Life	3.7%	2.3%	2.2%	2.8%
2011 Share of World GDP (%)				
	32.0%	36.9%	31.1%	100%

Note: All data points taken from Swiss Re's Sigma World Insurance Reports 2011 and 2007 to facilitate comparison across regions. They may not match with the data used in detailed trends sections that are taken from respective regions Insurance regulators/ associations

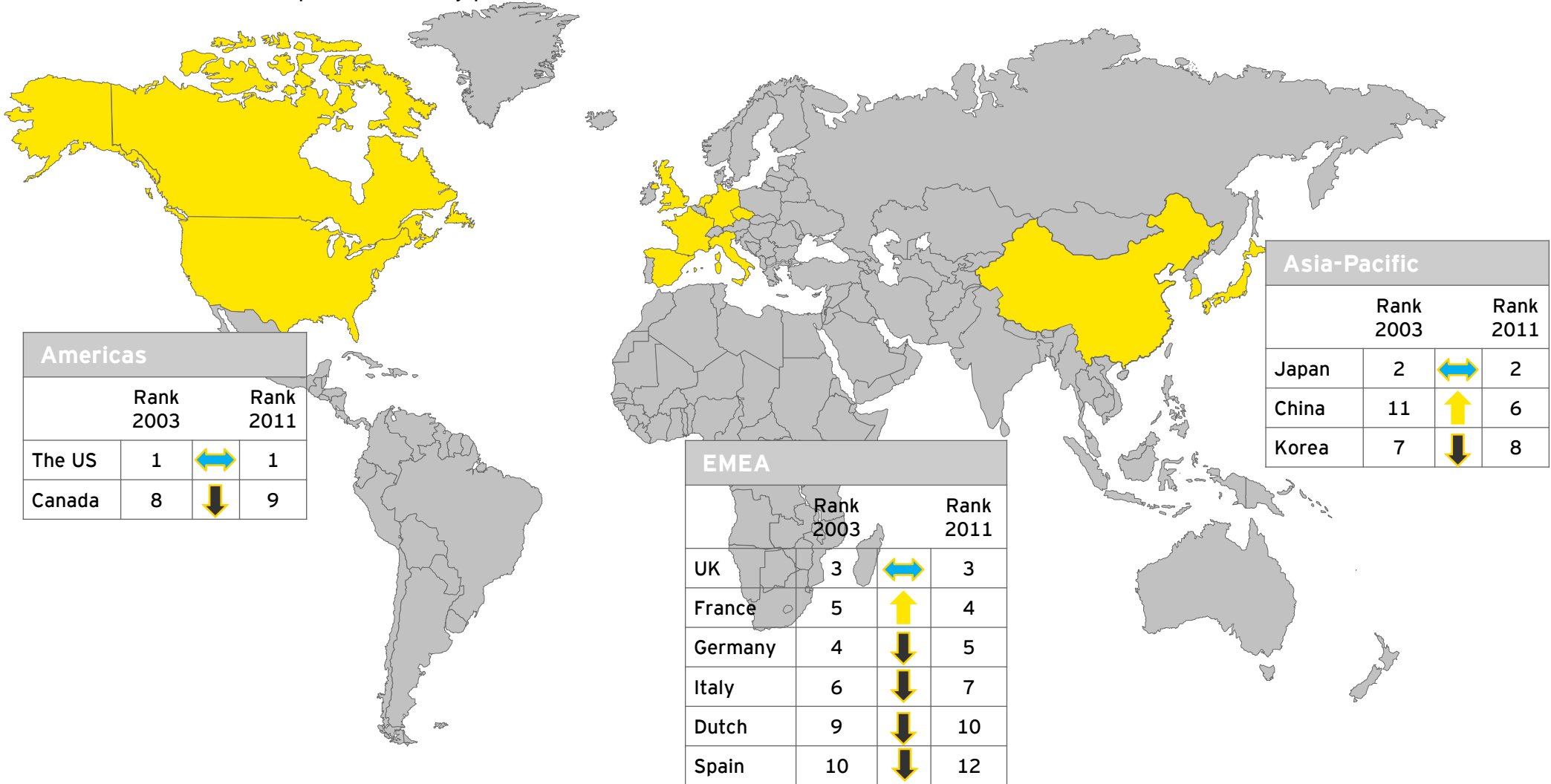
Source: "World Insurance Reports 2007-2012," Sigma, Swiss Reinsurance Company Ltd; Ernst & Young analysis

Global Insurance Industry

Developed markets continue to dominate



World Insurance Market: Top 10 markets by premiums



Source: "World Insurance Reports 2007-2012," Sigma, Swiss Reinsurance Company Ltd; Ernst & Young analysis

Global Insurance Industry

Macro considerations for insurance leaders



Global Insurance Industry

Macro considerations consolidated



Stakeholders & capital markets	<ul style="list-style-type: none">• Desire for transparency• Creditworthiness of sovereign debt• Managed risk• Funding restrictions
Competition	<ul style="list-style-type: none">• Step changes in established market structures• Weakened incumbents and new contenders – some from emerging markets• Intense downward cost pressure and market consolidation
Regulatory intervention	<ul style="list-style-type: none">• Increased regulation, public oversight and in places public ownership• Capital management - Solvency 2 directive likely to have more global impact• Risk of re-emerging trade barriers
Geographic shift	<ul style="list-style-type: none">• Growing unemployment in mature economies• Sustained growth in emerging economies• Shift of economic power fuelling the trend – West to East• Climate change and catastrophic events
Customer demand	<ul style="list-style-type: none">• Consumer confidence not as damaged by financial crises as other industries• Demand depressed with increased price sensitivity• Demographic need remains



Regional distinctions

Regional distinctions



Developed Markets	Europe	<ul style="list-style-type: none"> • Market contracting? • Euro crisis – continue for some time with impeded growth for how long? • Need to rebuild capital during soft pricing cycle • Solvency II preparations • Search for growth – drives new strategies and M&A outside Europe
	United States	<ul style="list-style-type: none"> • Non-life less impacted from financial crisis than other FS sectors • Regulatory uncertainty and impact of healthcare reform • “Back to basics” – focus on core business & product / distribution strategies • Risk based capital management / Corporate governance / SIFI status
Emerging Markets	Asia Pacific	<ul style="list-style-type: none"> • Overall higher growth • Highly diverse local insurance markets • Government involvement / ownership in industry • Market development efforts / distribution channel issues
	Latin America	<ul style="list-style-type: none"> • Higher growth prospects • Highly diverse local insurance markets • Markets / Distribution channels needing development
	Africa	<ul style="list-style-type: none"> • High growth prospects • Relatively simple product range • Distribution channels remains a challenge

Emerging markets



- Although there are market entry challenges and risks, there are significant growth prospects
- Continued robust growth is driven by growing economies and rising wealth
- Fast developing regulatory environment and shift in consumer mindset is leading to new product opportunities
- Underwriting loss within the non-life industry continues to be a major concern
- State owned or closely affiliated insurers dominate many African countries

Developed markets



- Most developed markets experienced shrinking life insurance premiums due to reduced demand for long-term savings products and rising competition from banks
- Low investment yields continue to afflict earnings
- Recent fiscal crisis has led to a number of broad regulatory reforms aimed at improving risk management and solvency although life insurance companies fared better than the banks
- Many insurers are reacting to the challenges by following a “back-to-basics” strategy
- Despite higher catastrophe losses, larger non-life insurers remain awash with surplus capital
- Due to a lack of organic growth, large insurers are increasingly looking to emerging markets for strategic growth

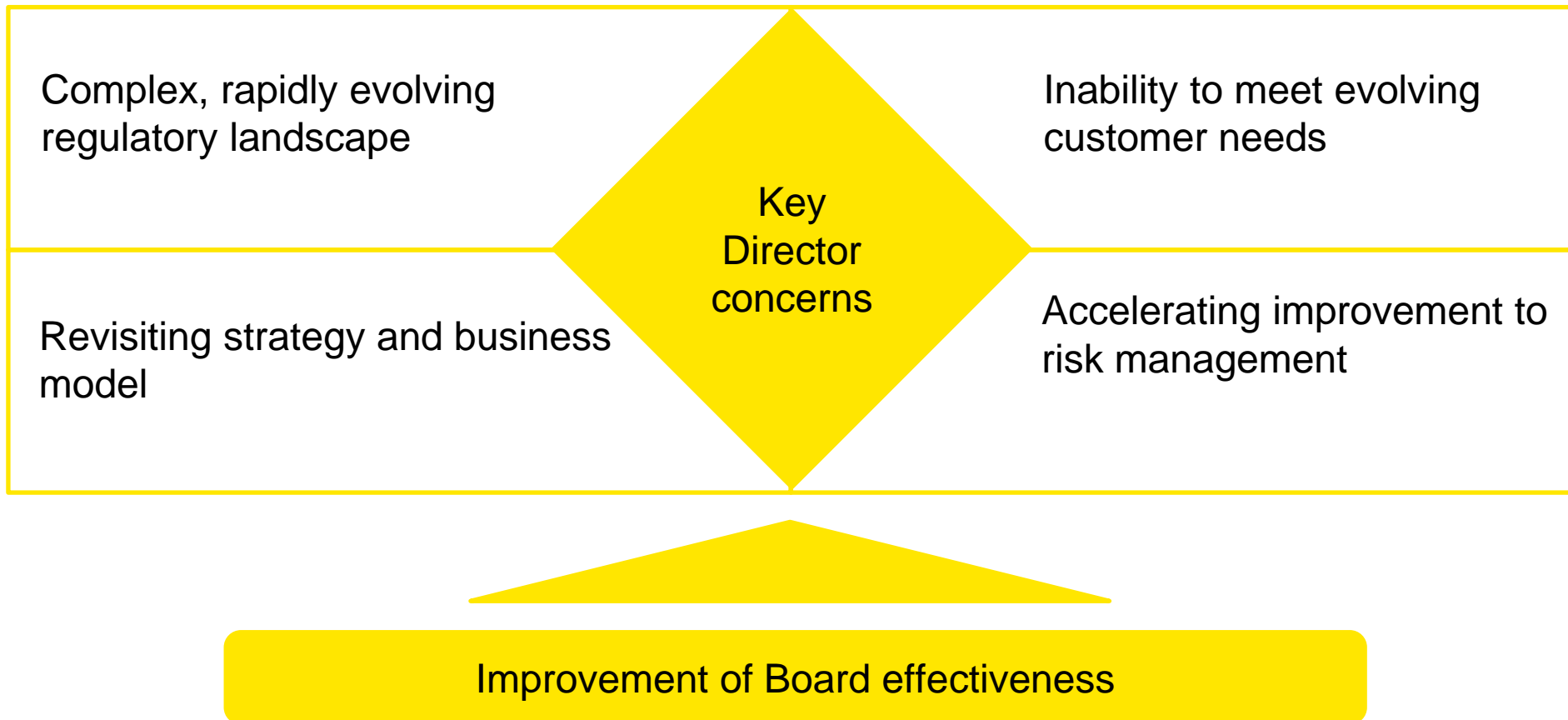


Global NED challenges

We interviewed* 30 Directors of the world's largest insurance companies, plus 12 regional regulators



“How can we be all things to all people?”



*In conjunction with Tapestry Networks TM in Q3 2011

Key director concerns





Looking forward

Long term conditions



Insurance Industry

- Potential for depressed sales until consumer debt levels are reduced
- Pressure on interest rates and inflation as government spending and debt levels managed
- More demanding regulatory, rating agency & compliance environment
- Consumers will demand less complexity and ability to interact with insurers through far more integrated retail experience
- It may be a time of watershed for the industry over the next 2 years as RDR regulations are introduced

Industry Outlook

Non-life Insurance

- Increasing fraud and persistent low investment returns will continue to place pressure on profits
- Investments in advanced technologies (such as predictive modelling) can boost sales
- Challenging operating environments will continue to force organisations to reduce costs
- Established insurers will be under increasing pressure from new entrants (especially direct insurers) making smarter use of digital channels
- Response to climate change and resource scarcity will drive future profitability
- Consistent rate hikes will continue to boost premiums growth

Life Insurance

- Higher cost of capital, driven by greater capital requirements, less leverage, higher volatility and risks
- Equity markets will remain off peak levels for several years
- Continued margin pressures
- Consumers will demand capital or income protection as part of traditional insurance and pension products
- Regulatory reforms will drive investment in more advanced risk management, capital efficiency and reporting capabilities



Sustainable success lies in simplification

The need for sustainable success



- As with every previous economic slowdown, insurers are once again challenged to deliver sustainable growth in a period of uncertainty
- Many have undertaken ‘traditional’ cost cutting and have found significant short-term relief this way. However, with no end in sight, this latest economic spell is forcing organizations to improve efficiency like never before

When compared to more complex competitors, simplified insurers and brokers are:



- 1 More agile and can demonstrate stronger sustained growth
- 2 More profitable
- 3 Customer centric to their core
- 4 Achieving sustained improvements in ROE through acquisitions with effective integration and a product focus
- 5 Global or single-location – they can sustain low expense ratios either way
- 6 Threatening traditional life companies' positions with their more focused and agile 'new models'
- 7 Using partnerships to support growth across the value chain
- 8 Responding to regulation with a thematic, enterprise-level approach
- 9 Reducing the complexity of tax planning through the targeted use of specific simplification levers

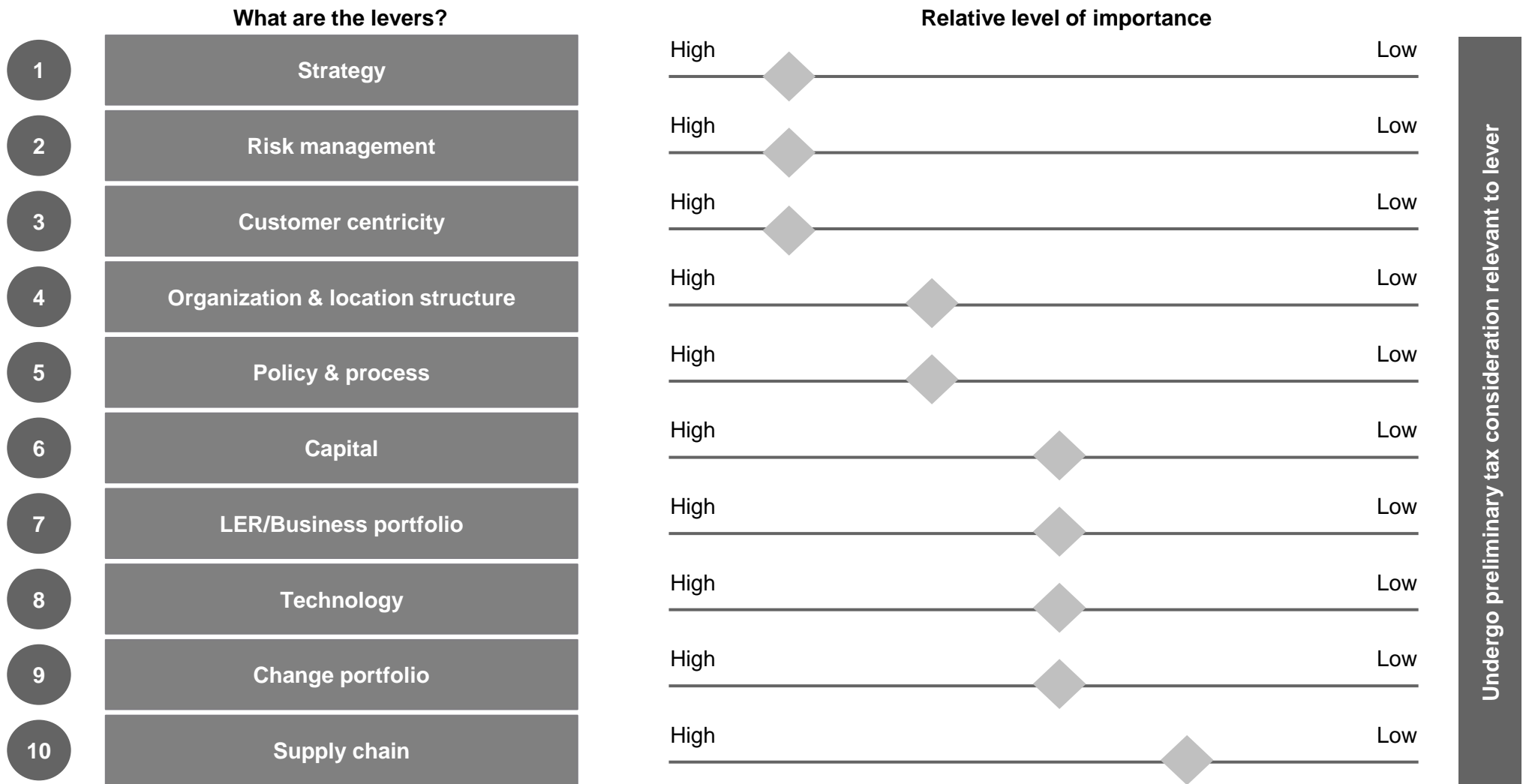
How do organisations deliver sustainable value?



These 10 levers highlight the key elements of the business model which must be addressed to deliver sustainable performance improvement through simplification ...

	What are the levers?	How do they deliver sustainable value?
1	Strategy	Drive simplification through a clearly articulated and effectively cascaded strategy
2	Risk management	Measure the risk impact of simplifying the business model – ensure risk does not drive complexity
3	Customer centricity	Focus on the right customer segments, products and channels – simplify the business as both an input and an outcome
4	Organization & location structure	Sustain simplification by minimising duplication – maintain control , focus on activities which drive competitive advantage
5	Policy & process	Standardize operational processes and policies – focus on sustainability via continuous improvement
6	Capital	Focus on aligning capital with chosen products and geographies, and releasing working capital currently trapped by complexity
7	LER/Business portfolio	Dispose of non-core and align legal entities with business portfolio – removes unnecessary capital restraints and aids acquisition integration
8	Technology	Taking advantage of other simplification levers (e.g., Product) to rationalize systems and focus future investment on delivering the strategy
9	Change portfolio	Deliver a simplified portfolio – focus on delivery of strategic objectives and mandatory change
10	Supply chain	Group vendor management to simplify relationships and manage down cost of supply

... but they must be addressed in a logical order



Methodology – greater detail



We developed a set of simplification hypotheses to test the overarching theme: ‘a strategy of simplification drives sustainable success’

Business Complexity Indicators* include:

- ▶ No. of geographical locations
- ▶ Acquisitions over last 3 years
- ▶ Range of specialisms
- ▶ Regulatory intervention
- ▶ Size of change portfolio
- ▶ No. of legal entities
- ▶ No. of legacy systems
- ▶ Effective tax rate
- ▶ Complexity questionnaire

These criteria formed the basis of our complexity assessment and were used to derive the score

Analysis

Business Performance Indicators include:

- ▶ Market Capitalisation
- ▶ Expense ratio
- ▶ Return on Equity (ROE)
- ▶ Earnings per share (EPS)
- ▶ Combined Operating Ratio (COR)
- ▶ Life internal rate of return (IRR)
- ▶ Gross margin
- ▶ Gross Written Premium (GWP)
- ▶ European Embedded Value (EEV)
- ▶ Earnings before interest, taxes, depreciation and amortisation (EBITDA)
- ▶ Assets under administration (AUA)
- ▶ Sales

Analysis

Evaluation and development of findings

* These indicators have been corroborated with the Global Simplicity Index published by Professor Simon Collinson and Simplicity

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