

Insurance 2020:
Turning change
into opportunity

*Insurers who anticipate and
plan for change can create
their own future*

January 2012



Contents

<i>Introduction</i>	<i>01</i>
<i>The key STEEP drivers</i>	<i>02</i>
<i>Implications for the future of your business</i>	<i>12</i>
<i>How to design your business strategy to face the future</i>	<i>16</i>
<i>Giving you the edge</i>	<i>19</i>
<i>Contacts</i>	<i>20</i>

Introduction

The future may be hard to predict, but need not be hard to prepare for. Insurers are grappling with the tough new business, investment and regulatory environments that are emerging from the financial crisis.

The industry, however, also faces far broader challenges. Demographic shifts, the rise in power of the emerging markets and changing customer behaviour will all help shape the sector's longer term future.

Insurers who can anticipate and plan for change can create their own future. Others who are 'fast followers' will need to be agile enough to recognise the leaders and adopt similar strategies. The 'survivors' are likely to be focused on short-term performance. **Which one are you?**

In this report we take a two-stage approach (see Figure 1) to help you address this key question and to develop a strategy to exploit the opportunities the future holds:

1 Analysis of the key market drivers. We have conducted extensive research to develop a set of future scenarios. We have based our research on an 'outside-in' scenario planning analysis that takes into account the impact of global social, technological, environmental, economic and political factors (STEEP) across three major insurance industry sectors – personal, commercial and life, annuity and retirement. We take into consideration more than 30 different drivers that could potentially impact insurance, globally. (We describe in this document the drivers, but due to space limitations do not cover each one in depth.)

2 Implications for insurers' business models. Our second stage is an 'inside-out' business design analysis, which evaluates the impact of these different scenarios on developed and emerging market insurers' strategies. We also consider the changes you could make to your business design to avoid risks and maximise opportunities. The business design framework can help you to exploit the data and insights in this study, and tailor them to your specific strategic direction and unique capabilities.

Figure 1: Scenario planning based business design

Factors & Drivers	Mega trends	Sectors	Scenarios	Industry impacts	Strategies	Design levers
What Social, Technological, Environmental, Economic, and Political (STEEP) factors and its component drivers impact the future?	What mega trends can be inferred from the STEEP factors and drivers?	How do these factors, drivers, and mega trends change by the three insurance sectors – personal lines, commercial lines, individual life, annuities and retirement?	What are the primary dimensions and macro-scenarios that can be mapped from the 'outside-in' analysis?	What are the key industry impacts that arise out of the three sectors of insurance?	Given their strategic intent and core capabilities, what strategies can develop and emerging market insurance players adopt to prepare for the future?	What design levers should companies use to execute their strategies to exploit the uncertain and fast changing future?

"Outside-in" Scenario Planning Analysis

"Inside-out" 3D Business Design Analysis

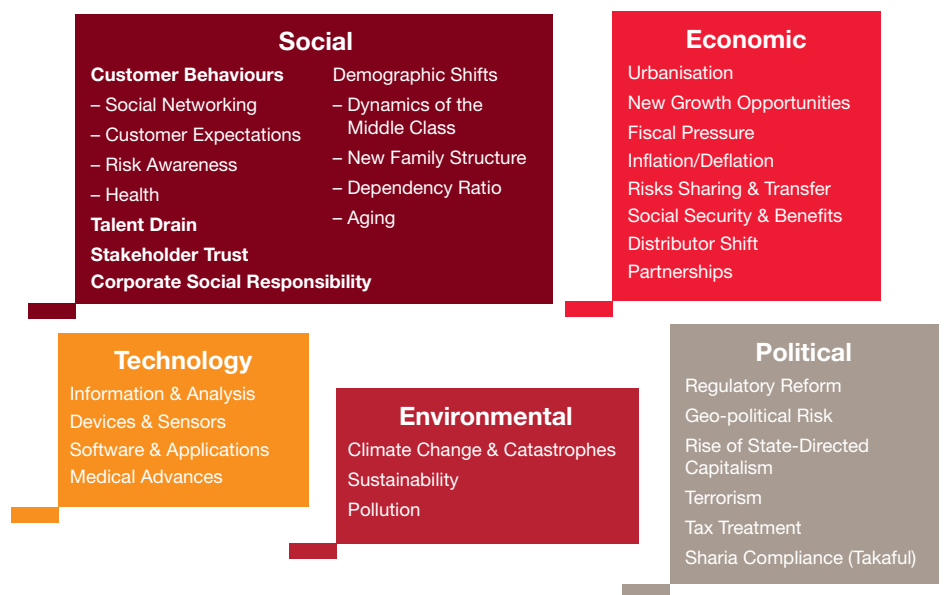


The key STEEP drivers

We have explored the five STEEP drivers to identify 32 factors that we believe will have an impact on the insurance industry (see Figure 2). STEEP factors have an impact on all sectors of insurance – personal, commercial and individual life, annuities and retirement – but not all changes will affect insurers positively. Economic growth, for example, in the short to medium term will be stronger in emerging economies. Forward-looking insurers in developed countries, however, can still grow in their local markets by exploiting socio-demographic and technological trends, while at the same time targeting emerging markets for growth. Similarly, insurers from emerging economies have an opportunity to reshape insurance products for their local markets while expanding on the global stage to build their technical expertise.

Although no one can predict exactly what STEEP changes will occur in the next decade, we believe five key mega-trends will influence the insurance sector. There are many more to consider (review the scenarios described in Figure 3) and with our research in place we are happy to walk you through them, but in this publication we will focus on:

Figure 2: STEEP drivers and factors



Source: PwC analysis

- **Social:** The balance of power is shifting towards customers.
- **Technological:** Advances in software and hardware that transform ‘big data’ into actionable insights.
- **Environmental:** The rise of more sophisticated risk models and risk transfer to address the increasing severity and frequency of catastrophic events.
- **Economic:** The rise of economic and political power in emerging markets.
- **Political:** Harmonisation, standardisation and globalisation of the insurance market.



Figure 3: STEEP Drivers: The range of possible scenarios you face

Our detailed analysis of over 30 key STEEP drivers has enabled us to determine a range of possible macro-scenarios that the insurance industry faces. These macro-scenarios underpin the implications we have drawn for the future shape of the insurance sector.

	Regressive 1	Combination of factors		Progressive 5	
		2	3	4	
Social	Customers predominantly seeking face-to-face interactions with intermediaries.	Distribution disruption in which multiple channels compete for customer interaction.	Distribution disruption where integrated multi-channel interaction is the norm.	Distribution destruction, where customers buy directly from carriers.	Distribution destruction, where self-forming groups of customers negotiate bulk purchases from carriers.
Technological	Insurers face increased data overload, quality and privacy issues, and cyber threats, resulting in a regression to 'gut-driven' decision-making.	Insurers continue to manage information overload and ever-increasing sophistication of analytical techniques that require ongoing investment to keep pace with competitors.	Sophisticated information analytics becomes the key determinant of competitive differentiation, which underwriting talent magnifies.	Sophisticated information analytics, new sources of information (from mobile sensors), and underwriting talent become the key determinant of competitive differentiation.	Sophisticated information analytics progresses to a point where no more useful information can be extracted and all key decision-making has been automated; competition shifts to prevention and productivity gains.
Environmental	With catastrophic events on the rise and insufficient data to accurately predict them, insurers will exit unprofitable areas.	Insurers will continue to rely on catastrophe models, but regulatory restrictions will prevent them from restructuring innovative risk transfer/sharing deals.	Insurers will continue to rely on catastrophe models and sell innovative catastrophe insurance products through securitisation and reinsurance.	Catastrophe modelling gets more sophisticated and uses advanced, early warning technologies to underwrite in specific, catastrophe-prone areas.	Advanced early warning technologies and new risk transfer/sharing mechanisms with public and private enterprises reduce human and property loss from catastrophic events.
Economic	The world moves from globalisation to regionalisation and insurers operate in and create products specific to narrow boundaries.	Emerging market insurers grow in scale and importance, and limit opportunities for developed market insurers.	As developed market insurers enter emerging markets, margins in these markets decline.	New emerging market insurers move into developed markets and become global businesses.	Truly global markets with products that are able to integrate multiple parts of the value chain, regardless of location.
Political	Governments in both developed and emerging markets enforce equally burdensome regulations on insurers decreasing their profitability.	Emerging markets erect more onerous regulations than developed markets' decreasing profitability and limiting control of developed market insurers.	Majority of regulations focused on banks, and insurers in developed and emerging markets are able to get away with minimal regulatory changes to pricing, coverage, rates and reserves.	Emerging markets and developed markets enact less burdensome regulations and emerging markets relax their regulations to ease the entry and control of developed market insurers into emerging markets.	The regulatory climate improves with greater harmonisation across countries (and within states in large countries). Regulatory harmonisation leads to standardisation across products and practices.

Source: PwC analysis



Social: The balance of power is shifting towards customers

New and ongoing social trends will shake up traditional business patterns in the insurance industry, resulting in an increase in consumer power:

Customer expectations: Customers (consumers and businesses) are increasingly demanding simplicity, transparency and speed in their transactions with businesses, including insurance agents/advisers and carriers. The relentless march of online and mobile technology is continuing to fuel this change in customer expectations.

In a recent survey of US consumers, more than 32% of all respondents – and 50% of those aged 18 to 25 – said they prefer to work directly with insurance carriers.¹ This ‘push’ towards direct interaction will continue across both personal lines and individual life insurance sectors. In addition, the online world is also becoming increasingly mobile as smartphone and tablet use increases and fuels the demand for localised information, available anytime, anywhere. By 2014, for example, the number of mobile internet users is expected to overtake desktop internet users.²

These changes will substantially impact the insurance sector:

- More and more insurance will be ‘bought’ by customers as opposed to being ‘sold’ by agents destroying the age old wisdom of ‘Insurance is sold and not bought’. This fundamental shift will force insurers and agents to re-examine their roles in the insurance value chain and become more relevant to the end-customer (consumer or business).
- Customer expectations of simplicity and transparency will foster innovations in product/service design and delivery. Leading insurers will get better at targeting customers and customising product and service attributes to meet their specific needs, amassing greater customer surplus.
- Mobility and speed of service demanded by customers will translate into investments in mobile and interactive technologies for multimedia content creation and distribution as well as transactional capabilities across multiple digital platforms.

Social networks: The rapid adoption and fast evolution of social networks will continue to empower both consumers and businesses to communicate more transparently and to harness the

buying power of virtual communities. The growth of social networking – one of the fastest ever global adoptions – will help shift the balance of power towards customers. In just six years since its launch, for example, Facebook has attracted over 800 million users.³ As consumers become even more comfortable with social networks several scenarios are likely to develop:

- People exchange more personal information and start building networks of trusted friends, family and acquaintances, shifting the balance of trust from insurance agents and advisers to online communities.
- Online social networks wielding substantial purchasing power become new group insurance channels, benefiting from information-driven online intermediaries.
- Eventually, online social networks become pooling mechanisms for self-insurance, changing the role of insurers at a primary level from product manufacturers to administration service providers.

1 Source: Coverhound: Car Insurance shoppers still prefer to deal with local agents over direct carriers, January 2011

2 Source: mashable.com: mobile by the numbers (infographic), March 2011

3 Source: Facebook statistics, November 2011



From distribution dominance to distribution destruction

Historically, the insurance sector has been dominated by intermediaries who have played the role of understanding consumer and business needs, and then matching and tailoring insurance products and solutions to their needs. Internet, mobility and social networking have changed the game over the past decade and have created a new generation of customers who demand simplicity, speed and convenience in their interactions. These trends will accelerate, leading to a situation where customers will be more willing to buy 'direct' using their online and offline 'trust' network of friends and family to guide their choice. This will result in a fundamental redefinition of the role of advice and the disappearance of distributors as a sales channel.

- 45% expect 'distribution destruction' where customers buy direct and even form groups to negotiate bulk purchases direct.

Source: PwC Research from more than 150 C-suite executives polled at a presentation of the Future of Insurance to the International Insurance Society (IIS), June 2011.

Technological: Advances in software and hardware are transforming 'big data' into actionable insights

As the insurance industry reaps productivity gains from the most recent wave of automation, new technologies are significantly enhancing operational efficiencies, increasing revenue opportunities and improving the customer experience. The important new technological developments for the insurance industry are:

- The growth in smartphones and tablets, coupled with cloud computing, which provide constant access to the internet.
- The explosion of computing power and storage, enabling the accumulation and analysis of extremely large amounts of data.
- The growth in active sensors and devices connected to the internet.

Big data: The growth of internet connected devices and sensors, which are projected to reach 50 billion by 2020,⁴ will have a significant impact on the availability of real-time information – a trend often referred to as 'big data'. Insurers who can exploit this information for better pricing, underwriting and loss control will have a distinct competitive advantage over their peers.

To harness the 'big data' trend, global investment in advanced analytical techniques is increasing in order to develop the capabilities to process large volumes of unstructured and multimedia data, such as continuous real-time video, life blogging and social chatter. These advances will lead to software – and eventually hardware – that can translate 'big data' into actionable insights.

Advances in Artificial Intelligence techniques, such as machine learning, natural language understanding and intelligent decision-making will allow insurers to advance from using technology for transaction processing to decision-making. Today, analytical techniques are used for making ad hoc decisions using structured data.

By 2020, the use of unstructured data (e.g. social media, devices, video and audio) will complement structured data, allowing insurers to make strategic forward-looking decisions.

From a reactive to a preventative business model: Commercial insurers are already using connected devices and sensors to develop risk and loss management and improve productivity, but we also envision life and health insurers using them as well.

By 2020, a number of biotechnologies will be available at the nanoscale, providing the ability to embed devices and sensors unobtrusively within the human body. The nanotechnology drug delivery market is expected to grow at a CAGR of 21.7% between 2009 and 2014, and reach almost \$16bn by 2014.⁵ Such nanotechnologies have the potential to dramatically improve health outcomes through enhanced monitoring and preventive control of chronic disease.

⁴ Source: CISCO, The internet of things: How the next evolution of the internet is changing everything, April 2011

⁵ Source: Companies and Markets, Nanotechnology in Healthcare: Market outlook for applications, tools and materials, January 2010

The medical service and treatment model is evolving towards the customisation of healthcare; the resultant decrease in morbidity and mortality will have a profound impact on life and health insurers. Consumers will eventually use personalised medicine to create highly customised healthcare solutions that actively change the body's biochemistry in response to risks and conditions that are unique to each person. We anticipate that these medical advances will flatten the cost curve as mortality and morbidity rates dramatically improve. Some of these advances can also reduce litigation costs as medical product manufacturers can provide detailed evidence on the efficacy of their drugs.

Commercial insurers have always focused on loss control and risk management, but that trend will deepen and expand into other lines of insurance. Personal and life carriers will be able to move from passively identifying and pricing risk and reactively paying claims to proactively using 'big data' and actionable insights to reduce losses and better manage risk. For life and health insurers as well as annuity and retirement income providers, monitoring devices could significantly extend life expectancies and increase the number of years of active retirement life.



From a structured data/tactical decision-making/reactive business model to an unstructured data/strategic decision-making/preventive model

Historically, the insurance sector has used, primarily, internal data in a structured format to make tactical and operational decisions around which customers to target, how to price the risk, how to estimate the losses, etc. However, in the next decade the industry will increasingly use large amounts of real-time sensor data, unstructured data from social networks, and multimedia data such as text, voice and video. As sophisticated artificial intelligence techniques evolve, insurers will start using this unstructured data for forward-looking strategic decisions such as, which product or solution is most suited for a client given their current and future situation, which emerging countries to enter as well as when and how proactively to manage customer experience to enhance retention of the most profitable customers. Insurers who are able to use real-time 'big data' and advanced forward-looking simulation techniques will establish a significant competitive advantage.

- In a recent survey, 49% expect new sources and techniques in the use of data analytics to be the key competitive differentiator.

Source: PwC Research from more than 150 C-suite executives polled at a presentation of the Future of Insurance to the International Insurance Society (IIS), June 2011.

Environmental: The severity and frequency of catastrophic events is increasing

The severity and frequency of catastrophic events, both natural and man-made, have been increasing over the past 20 years. Between 1990 and 2009, hurricanes and tropical storms accounted for 45.2% of total catastrophe losses,⁶ and the rate and intensity of these storms is predicted to increase with global climate change. A large portion of claims' payouts result from business interruption coverage losses – in the Chilean earthquake, for example, over 50% of claims were filed for business interruptions and extra expenses.⁷

In addition to catastrophic events, insurers must also consider man-made degradation of the environment. Increasing energy consumption and associated atmospheric pollution will directly impact carriers' risk exposure. The US Energy Information Administration, for example, predicts world energy consumption will grow by 49% between 2007 and 2035.⁸ With

continued fossil fuel use, pollution will remain a significant health issue, threatening the well-being of populations in both developed and developing countries. Life and health insurers will need to closely monitor trends in atmospheric pollution in order to accurately assess risk in different regions.

Environmental measures will help mitigate the most serious consequences. Renewable energy sources are projected to account for 23% of electricity by 2035.⁹ Increased consumer investment in sustainable solutions (e.g. solar panels) will gradually create new modelling and pricing risks for Property & Casualty (P&C) insurers.

Managing these types of risks will require insurers to be more sophisticated in their risk modelling and innovative in structuring risk-sharing and risk transfer deals. Catastrophe modelling will become more sophisticated and use advanced, early warning technologies to underwrite in specific, catastrophe-prone areas. Insurers who fail to keep pace with this increasing sophistication might be forced to exit markets in certain coverage areas, such as those prone to flooding or forest fire.

Increased severity and frequency of catastrophic events overwhelming insurers vs technology and risk transfer easing the pain

Historically, the insurance sector has been good at developing catastrophic models that capture known high severity/low frequency events (e.g. earthquakes, tsunamis, etc). However, most of these models perform poorly when it comes to unknown 'Black Swan' events. Over the next decade the insurance sector could be overwhelmed with uncorrelated catastrophic events reducing capacity and raising prices. Alternatively, new sensing and monitoring technology, together with risk transfer mechanisms, could cushion insurers and reinsurers against abnormal losses.



6 Source: Insurance Matters: Information for policymakers, Catastrophes: Insurance Issues, June 2011

7 Source: Insuring Florida, Catastrophes: Insurance issues, October 2011

8 Source: US Energy Information Administration, World energy use projected to grow 49 percent between 2007 and 2035; Rapid growth projected for renewables, but fossil fuels continue to provide most of the world's energy under current policies, Press Release May 2010

9 Source: US Energy Information Administration, International Energy Outlook, September 2011

Economic: The rise of emerging market economic and political power

The increasing attractiveness of the emerging markets, combined with uncertain growth in the developed world and stricter regulatory guidelines will make carriers re-evaluate their strategic goals towards developing countries.

The E6 countries' (China, India, Brazil, Russia, Indonesia and Mexico) proportion of global GDP has been increasing over the past 20 years, and the liquidity and debt crunch precipitated by the financial crisis of 2008 continues to affect developed economies far more than emerging ones. It is estimated that the E6 will contribute 47% of Global GDP growth between 2006 and 2020, while the G6 will contribute less than 24% during the same period (Figure 4).¹⁰

A number of factors are contributing to the ongoing shift from a world dominated by developed markets to a world in which the majority of growth is in emerging markets:

- In the developed world, the old outnumber the young. In emerging markets (except China) the working age population will continue to outnumber the dependent population, and thereby result in more productive growth.
- The rise of the middle class in emerging markets is fuelling increased consumption, which is leading to impressive small business growth.
- Government infrastructure investment, population growth, new businesses and wealth creation are driving growth in construction, land development, energy and transportation sectors, all of which are creating a greater need for insurance.





The rise of economic influence and power of emerging market countries and emerging market insurers

Over the past couple of decades the world's economies have become more interdependent and this trend is likely to continue. However, the power and influence of the US, Europe and other OECD nations will wane as the emerging markets continue to grow as well as become the engine for global growth. As consumption in these countries increases, the insurance market will grow, resulting in big opportunities for emerging market insurers. The developed market slowdown, due to the financial crisis, will accelerate this shift in power towards emerging market economies and emerging market insurers. In a recent survey conducted by PwC:

- 30% believe new emerging market insurers will move into the developed world to become global insurers.
- 28% foresee truly global markets.

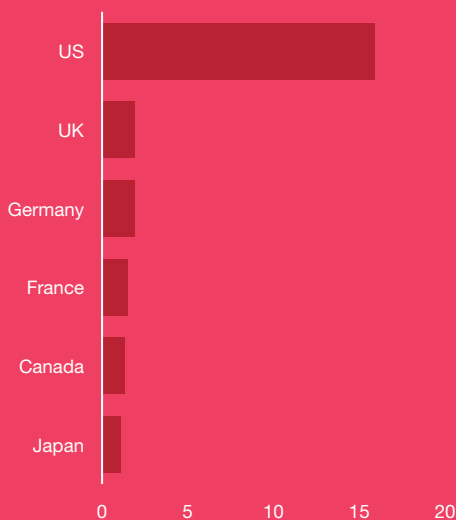
Source: PwC Research from more than 150 C-suite executives polled at a presentation of the Future of Insurance to the International Insurance Society (IIS), June 2011.

The uneven distribution of economic growth between the developed and emerging markets creates different scenarios for insurance industry competitive dynamics:

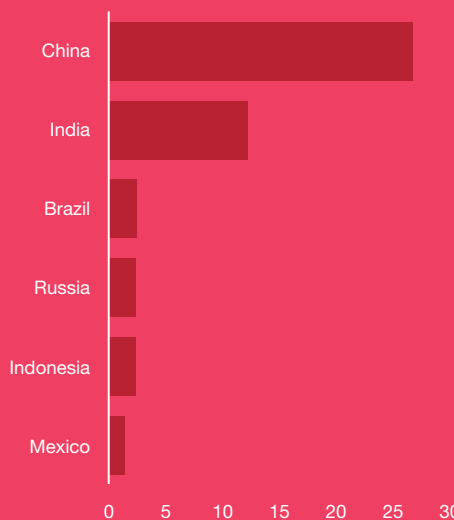
- The insurance industry as a whole could become more globalised as countries harmonise regulations, standardise practices and distribute products across borders (see 'Political' on page 10). This could lead to greater market share for global insurers, as well as economies of scale and scope that drive the globalisation of the insurance value chain.
- Conversely, twin-track growth and the loss of the developed world's authority in the wake of the financial crisis could result in greater protectionism by countries or regions.
- In-between these two extremes, developed market insurers could increase their attempts to find growth in emerging markets, and or emerging market players could expand into developed markets for know-how and talent.

Figure 4: E6 vs. G6 Contribution to global growth (2006–2020)

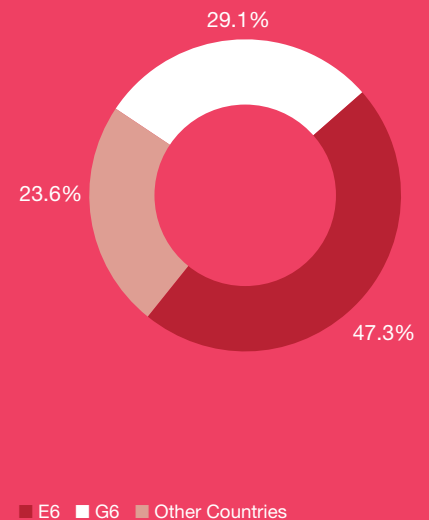
G6 Contribution to Global Growth (%)



E6 Contribution to Global Growth (%)



E6 vs G6 Contribution to Global Growth (%)



Source: Economic Intelligence Unit, Foresight 2020

The developed market slowdown, due to the financial crisis, will accelerate this shift in power towards emerging market economies and emerging market insurers.

Political: Harmonisation, standardisation and globalisation of the insurance market

We see a range of potential outcomes from a regulatory perspective. The financial crisis has enhanced communication and dialogue between and among the US, EU and emerging market regulators:

- If regulators are successful at negotiating and harmonising global insurance regulations, this could lead to greater standardisation of products and policies, and promote more globalisation of the insurance value chain.
- On the other hand, regulators could continue to develop new but different (and potentially onerous) regulations in each market.
- In-between these two extremes, it is possible that emerging markets will prevent developed market players from entering their markets or put limits on their activities. (An alternative intermediate scenario is that emerging markets encourage developed market entry by removing restrictions and easing regulatory burdens.)

Outside the regulatory arena there are several additional political trends for insurers to consider:

Pressure on the solvency of social security and welfare programmes throughout the world will increase because of rising dependency ratios. Dependency ratios (defined as the ratio of the number of persons aged under 18 or over 64 to the number of persons between these ages) are expected to increase by an average of 14% in the G6 between 2000 and 2025.¹¹ Using current projections, the US Social Security Trust Fund will be depleted in 2037 and Social Security will be able to pay only 78 cents in the dollar.¹²

Consumers lacking faith in the solvency of social security programmes will begin to focus on providing their own savings for retirement, as governments pare back benefits. This will create new opportunities for life and annuity insurers, although governments under financial pressure are likely to seek ways to reduce spending while increasing tax revenue. The preferential tax treatment of life, annuity and retirement policies may be viewed as an easy target for revenue generation. Insurers will need to adapt nimbly in order to weather these changes.

Terrorism. Over the past 30 years, there has been an increase in terrorist attacks around the world. Terrorists currently attack global supply chains once every four days on average.¹³ Carriers will have increased exposure as the frequency of major attacks increases. In addition, terrorist attacks often impact multiple product lines (e.g. commercial property, business interruption, workers compensation, life and benefits), which are often modelled independently. As a consequence, the potential losses from so-called ‘uncorrelated’ risk factors could be large, requiring substantial industrywide or state-provided capital to insure losses beyond a certain level. Further detailed modelling is required to understand the capacity requirements for terrorism coverage.

Geopolitical instability. Resource scarcity around the world is magnifying the risks of geopolitical instability, as evidenced by the current political upheaval in the oil-producing nations of the Middle East and North Africa, or the ‘Arab Spring’. This has caused resource-consuming nations to reassess their energy policies. We anticipate that the potential for fewer despotic regimes in the Middle East and technological solutions to resource scarcity will lower geopolitical risk over the next ten years.

¹¹ Source: Alliance for Health & the Future, The Dependency Ratio, Issue Brief Vol 2, Number 1

¹² Source: Centre for Retirement Research at Boston College, The Social Security Fix-it Book

¹³ Source: Terrorists attack global supply chains every four days. SupplyChain Digital, April 2011



Harmonisation and standardisation of insurance regulation, products and practices

Over the past couple of decades the world's economies have become more interdependent and this trend is likely to continue. However, the power and influence of the US, Europe and other OECD nations will wane as the emerging markets continue to grow as well as become the engine for global growth. As consumption in these countries increases, the insurance market will grow, resulting in big opportunities for emerging market insurers. The developed market slowdown, due to the financial crisis, will accelerate this shift in power towards emerging market economies and emerging market insurers. In a recent survey conducted by PwC:

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Source: PwC Research from more than 150 C-suite executives polled at a presentation of the Future of Insurance to the International Insurance Society (IIS), June 2011.



Implications for the future of your business

We have analysed the STEEP factors and drivers for each of the three insurance industry sectors. While some drivers, such as direct purchase, are common, their impact could be greater in one sector (e.g. personal lines) than in others (e.g. commercial lines). Also, some sectors will have additional drivers, such as health advances and their impact on life and disability insurance.

Personal lines

We believe personal lines insurance will change in four fundamental ways:

- **Greater commoditisation.** Price transparency, dis-intermediated direct purchase and virtual social community-led bulk purchase will all lead to greater commoditisation of personal lines insurance. In the immediate term, insurers in some emerging and underdeveloped markets will be able to generate good margins. As personal lines insurance becomes more global over time, however, these margins will vanish in a price-based, competitive world.
- **Decreasing profitability.** The increased number of megacities being built in areas prone to natural disaster could result in catastrophic losses. With no opportunities for diversification, this could result in highly volatile earnings and decreasing profitability for insurers.
- **Automated underwriting.** As personal lines insurers expand globally, ageing underwriting resources in the developed world and lack of underwriting skills in emerging markets will lead to severe talent shortage. However, insurers who are able to recruit or retain top underwriters and use their knowledge to build sophisticated predictive modelling should be able to gain greater market share. Automated underwriting, more standard in the developed world, will be increasingly adopted in the emerging markets as the globalisation of the personal lines sector continues.
- **Greater loss control.** In the immediate term, insurers will use advances in telematics primarily to price mileage-based insurance. But, in the medium term, they will use telematics to proactively control losses and manage risk, which should substantially enhance operating profitability. Over time, this competitive advantage will disappear as automotive safety features and advanced analytics become commonplace.

Projecting future scenarios on a global scale with countries growing at different rates, insurance sectors at different stages of maturity, and insurance carriers with different strategies and capabilities is a challenging task. Rather than detail all different combinations of scenarios coming out of the 32 drivers, we highlight here some key scenarios from the perspective of illustrative insurance carriers and their strategies. Scenario A highlights the story of a hypothetical personal lines insurer and how it 'Creates its own future' by expanding globally.



Scenario A

In March 2012, the CEO of PL Insurer came out of a three-day strategy session determined to shape the company's future. PL Insurer, operating in more than 25 countries across the globe, was struggling to cope with tectonic social changes in consumer attitudes and behaviours. An increasing number of customers were migrating online, while use of mobile technology and social networks (including in the emerging market countries) was increasing rapidly. The agency-based distribution model that the company employed in 18 out of the 25 countries was being challenged by the adoption of innovative usage-based business models and telematics by the competition, as well as by increased capital requirements and regulatory oversight across the world. The CEO was determined to reinvigorate his global growth and innovation strategy, redefine the experience that consumers and agents shared with PL Insurer, and to build an insight-driven business model that would revolutionise decision-making across the organisation.

On 3 April 2020, as the CEO of PL Insurer is flying back to New York from Shanghai, he reflects on the past eight years since the pivotal historic meeting with his senior management in 2012. In that intervening period PL Insurer has become the largest global P&C insurer, now operating in 150 countries, with a combined ratio that is the envy of the industry. Over the past five years, profitability has been steadily climbing and the company has a war chest of cash to acquire companies. The regional distribution and operational model adopted by PL Insurer to serve its six global regions acts as a hub to share best practices, increase efficiency where possible through automation and centralisation as well as enhance effectiveness by devolving decision-making to the regional or country level. The SocInsurance global subsidiary is the fastest growing subsidiary of PL Insurer, offering personal insurance to social networking affinity groups. The advanced analytical and underwriting capability that SocInsurance has built allows it to select targeted segments and tailor its products, based on their social affinity. The patented interpretive underwriting engine offers PL Insurer a distinct competitive advantage over its competition, which will continue for at least three more years. The CEO is pleased that the steps he took to 'Create the Future' in 2012 have paid off so handsomely.

Commercial lines

We expect commercial lines to experience the following significant changes over the next decade:

- **Virtual business affinity groups.** Social networking among small business owners will create virtual business affinity groups that pool their risks and retain greater predictable layers of risk. Greater availability of information and increased price transparency will facilitate this trend.
- **Automated underwriting.** Current trends in automation of quoting and underwriting functions for commercial insurance will continue as insurers try to match underwriting capacity with the complexity of application inflow. The talent premium, especially underwriting talent, will have a much greater impact on commercial insurance than on personal insurance.
- **Business model transformation.** Real-time data from sensors and devices will continue to transform the commercial insurance business model. Commercial insurance will increasingly focus on providing standardised products and value-added services that involve working with the clients to proactively avoid or reduce losses and manage risks. In addition, risks are becoming more complex, offering the opportunity to harness improved data analytics to develop new risk transfer markets.

Similar to the scenario we discussed earlier, the following Scenario B highlights the story of a hypothetical regional commercial lines insurer and its success in adopting a 'Fast Follower', 'niche player' strategy.

Scenario B

RegCo Insurer, is a regional commercial insurer, focused on commercial lines insurance. In 2012, large global commercial insurers, capable of serving clients globally as well as regionally, were challenging RegCo's business. These competitors were operating at a combined ratio that was hard for a regional player like RegCo to match. RegCo can offer more customised risk management solutions to its commercial clients, but at a cost that adversely impacts its combined ratio, making it less profitable. As RegCo started planning for its future, it decided to reinvent itself by following other regional commercial insurers and move from being a product manufacturer to a risk management solution provider.

By 2020, RegCo is flourishing and has become one of the top 20 risk management solution providers. Starting in 2012, RegCo progressively withdrew from the product manufacturing business and instead partnered with brokers, reinsurance carriers and commercial lines carriers, to transfer its customers' risks. RegCo built a leading risk management solution that utilised embedded sensors and devices to monitor commercial risks in real-time and thereby control losses. Adopting a fee-based solution and value-share business model, RegCo was able to demonstrate the huge reductions in losses its solutions could provide and took a share of those savings. Its 'fast follower' strategy adopted in 2012 allowed it to flourish in the risk management space while some of its competitors were acquired, or went bankrupt.

Individual life, annuities and retirement

Environmental factors, urbanisation and changing customer behaviours will all greatly affect the life, annuities and retirement sectors. These sectors will also experience significant changes in response to global demographic shifts over the next decade:

- **New products for seniors.** An ageing population in most developed countries will result in new growth opportunities in drawdown or retirement income products, long-term care products and longevity insurance. While the growth opportunities for managing retirement portfolios before and after retirement is huge, insurers will face intense competition from other financial service providers, including banks, wealth managers and asset managers.
- **Insurers step onto government turf.** The increasing dependency ratio in most developed countries (and China) will increasingly strain government support for the elderly and sick, leading to prolonged employment and/or a reduction in the standard of living. This could open up the opportunity for insurers to form public and/or private partnerships to offer value-added solutions in response to a political challenge.
- **Better risk management.** Greater availability of medical and behavioural data, along with personalised medicine, will continue to drive greater sophistication in, and automation of, underwriting and provide the opportunity to better manage risk and to expand the boundaries of insurability.
- **Tailored products.** For group benefits, the responsibility for protection and retirement savings will continue to shift towards the individual. This will result in increasing voluntary coverage, as well as worksite marketing.

Current trends in automation of quoting and underwriting functions for commercial insurance will continue as insurers try to match underwriting capacity with the complexity of application inflow.

Scenario C

LifeCo is a global life, annuities and retirement (LAR) carrier operating in the US, Europe and Australia. In 2012, the low interest rate environment had decreased profitability and LifeCo's legacy technology made it difficult to adapt to the changing needs of its customers. LifeCo's executive team was faced with customers' ongoing desire for simplicity, transparency and speed as well as solutions to help them lead healthier lifestyles. Other challenges included data aggregation and value extraction, staying ahead of medical advances and developing products to accommodate longer lifespans and working years. Gaining approval from the Board, LifeCo's CEO embarked on a strategy to provide an industry-leading customer experience, develop an organisation focused on business intelligence and create products and partnerships to reinvigorate LifeCo's growth across the globe.

Preparing for 2020's first board meeting, LifeCo's CEO is proud of what his executive team has accomplished. The strategy he implemented has made LifeCo profitable again, with one of the lowest operating expense ratios in the industry for the past three years. By developing a personalised customer portal while providing binding quotes in a matter of minutes, LifeCo has become the first choice among agents and consumers. Hiring an experienced business intelligence (BI) leader was one of the best decisions the CEO made. Reporting directly to the CEO, the BI leader enabled the consistent flow of insightful, fact-based information, helping the executive team make the right decisions, faster. Utilising this information and partnering with a medical device company providing biotechnology to monitor health, LifeCo developed low-priced, consumer-specific, localised products offering discounts in later years for consumers living healthy lifestyles. LifeCo developed novel long-term care products for the increasing elderly population and also entered the Takaful market as it expanded into the Middle East. As LifeCo's product breadth grew, the company expanded its distribution channels by working with local carriers and brokers in other countries to expand its global footprint. As the CEO adds the finishing touches to his board presentation, he realises that LifeCo has become a true innovator in the industry and he looks forward to conveying that story to the board.

Some changes affect everyone

In addition to these sector specific factors, all insurers will be effected by the shift towards a global interconnected model, automated and assisted decision-making, based on data and insights and changes in the industry cost structure:

Globalisation and interconnectivity of risks. Apart from reinsurers and some commercial line insurers, most others have typically operated at the local or national level, and have been primarily involved in measuring risk exposures and determining the premium that they need to charge customers to insure their risk. However, given the scale of change implied by the STEEP trends, we believe that more insurers will be forced to think globally. In the future, insurers will be more involved in deciding which geographies, products, customer segments and channels will offer their desired level of growth, profitability and risk appetite.

Automated and assisted decision-making. Following the automation of transactional systems and the automation of interactions with customers, we are entering a new era of automating decision-making. Extensive internal and external data, as well as new artificial intelligence-based techniques will expand the scope of assisted and automated decision-making of insurers across a variety of functions. These include identification of markets/segments to enter or grow, customer segmentation, risk selection, advice engines that assist agents/advisers or end-consumers, claims triaging, and proactive preventive loss prevention and management.

Changing cost structures. Insurers who fully exploit the potential offered by the internet to transform their cost structures will be able to scale themselves exponentially and leverage their people, operations and technology infrastructure globally:

- Insurance distribution has traditionally relied on a commission-based variable cost model for sales; the route to increased sales was to 'put more feet on the street'. With increasing investment in direct online channels, cost structures are moving towards a larger upfront fixed cost, but a lower ongoing variable cost (provided you achieve the desired scale).
- Over the past two decades, insurers have invested heavily in operations and technology, incurring largely fixed costs to build IT infrastructures capable of dealing with their estimated customer base. Now, as more and more applications migrate to the 'cloud', information is available anywhere, anytime and at very little cost. If you have more standardised and streamlined processes you can use the cloud to move to a low variable transaction cost model that scales exponentially.
- With the right talent and proper use of information and analytics in underwriting, a greater number of transactions can be automated. This will allow the application of superior underwriting insight to a greater number of your transactions, helping overcome the looming talent gap as the current generation of underwriters approach retirement age.





How to design your business strategy to face the future

There is no prescriptive solution about how you should prepare your business for the future scenarios we have described.

While STEEP drivers impact all insurers globally, they have different levels of impact within each region and country.

In addition, the actions that insurers choose to take will depend not only on their national or regional markets, but also on their strategic intent, core capabilities, availability of talent, capital and organisational culture.

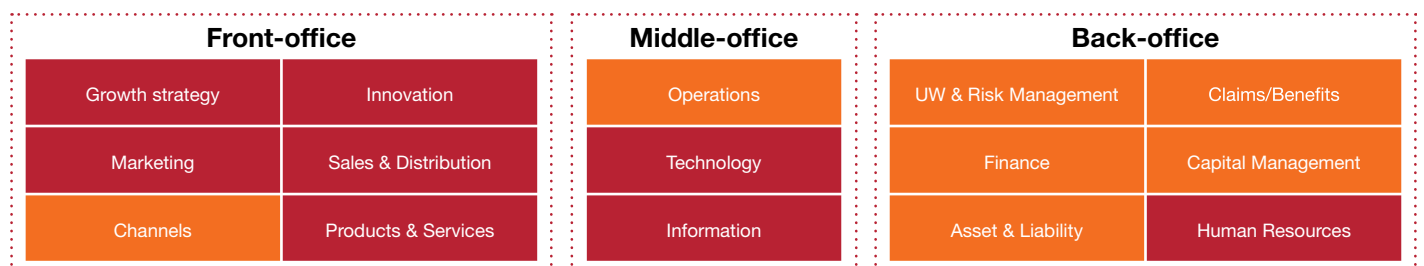
We have, however, identified four broad strategic directions that developed market and emerging market insurers could take, based on their specific situations:

Create your future: Innovators

Insurers who want to reshape the future through innovation. Whether these innovators are in emerging or developed markets, their focus will be on R&D, new product innovation and analytical decision-making techniques. (See Figure 5 for an Innovator's primary areas of focus.) In light of the limited growth opportunities in developed countries for traditional insurance products, developed market insurers will focus on creating value-added loss control and risk management services.

Figure 5: Create your future - innovators and expansionists

This diagram shows the areas of primary focus for an innovator and an expansionist. As both look to reshape their business, much emphasis is placed on front-office activity to disaggregate and re-engineer the value chain. Leaders in these areas will need to be cognisant of the drivers of change and their implications; they'll need to understand the potential impact on the business and also how the business is likely to respond. As change will impact functional teams simultaneously, strong communication, coordination and alignment of thinking will be required to succeed.



■ Primary areas of focus

Source: PwC analysis



Information-based services will be the key innovation in developed markets, using new sources of unstructured real-time information to draw operational and strategic insights. Insurers can use these insights to underwrite and price risk, as well as reduce losses and manage risk. In emerging markets, traditional insurance products will need to be adapted to suit local needs (e.g. micro-insurance or alternative distribution channels).

Create your future: Expansionists

Carriers who want to reshape the future through expansion. They will be growth seekers and not necessarily innovators of new products and services. These carriers will focus on leveraging their capabilities (e.g. customer understanding, product portfolio, capital, diverse talent, Takaful) into adjacent and similar markets around the globe. (See Figure 5 for primary areas of focus.) Expansion can come from moving into new geographies, targeting new customer segments for existing products, and/or introducing new distribution channels to reach customer segments.

Create your future: Fast followers

Carriers who do not want to be the first, but are adept at following the leaders and establishing a strong presence. Fast followers focus on scaling capabilities across a broad market. They are good at sensing new innovations and market opportunities, and are agile enough organisationally to follow and establish a lasting presence.

As Figure 6 shows, the primary focus of activity for fast followers lies away from the front office, demanding agility in operations, technology, information and the back office to respond to new business models and create operational excellence.

Figure 6: Create your future - fast followers and survivors

Front-office		Middle-office	Back-office	
Growth strategy	Innovation	Operations	UW & Risk Management	Claims/Benefits
Marketing	Sales & Distribution	Technology	Finance	Capital Management
Channels	Products & Services	Information	Asset & Liability	Human Resources

■ Primary areas of focus

Source: PwC analysis

Create your future: Survivors

Carriers who are focused on short-term performance and survival.

These carriers wait for a majority of the industry to adopt new ideas and practices before adopting them. They tend to be organisationally hierarchical and slow to respond, but can be operationally resilient and efficient.

What do you want to be?

Each of the above strategies is not necessarily superior or inferior to the others. In a conservative industry like insurance, there will be more survivors and fewer fast followers, expansionists and innovators. However, having a clear strategic direction about 'what you want to be' will be critical in determining how you design your business to manage the risks and exploit the opportunities that come your way.

What's on your mind?

Figures 5 and 6 show the functions engaged in implementing and embedding a new business strategy. Your perspective on change will be shaped by where you sit in the business. Here we've highlighted just a few considerations for the executive team when formulating a new strategy:

CEO	<p>Who do you task with shaping the response to all this change?</p> <p>Who will drive innovation to anticipate and respond to a changing market?</p> <p>How do you decide which markets, countries and customer segments to target?</p> <p>How do you prioritise your investments, and build the capabilities to survive and exploit the changing market?</p>
CRO	<p>How well is risk management embedded in your organisation and will you be comfortable with the risk assessments on new products, services and distribution channels?</p> <p>How can you be better prepared to anticipate and prepare for extreme 'Black Swan' events?</p>
CFO	<p>What will be the impact on your message to the market?</p> <p>How can you manage the capital and balance sheet structure of your company under changing regulatory, market and rating agency expectations?</p>
CMO	<p>How do you transform your organisation into a customer-centric organisation that is capable of marketing and tailoring products to your consumers' changing attitudes and behaviours?</p>
CTO	<p>How do you ensure the organisation is not only aware of the emerging technology trends, but is also actively involved in experimenting with new technologies as they come to market?</p>
CIO	<p>How do you ensure that you build an information advantage enabled by rich, insightful data, fully supported by a cost-effective technology platform?</p>
Head of Actuarial	<p>How are you ensuring that you can select and price risk appropriately, based on your risk appetite?</p>
Head of Underwriting	<p>Can you exploit new sources of information to improve better risk selection and pricing?</p>
Head of Claims	<p>Can you transform your organisation from paying claims to actively managing the losses based on real-time data and loss management techniques?</p>
Head of HR	<p>How do you ensure that you continuously attract and retain the right talent within the organisation – especially when the talent has to be culturally aware, multidisciplinary and global?</p>

Giving you the edge

Whether you are a personal, commercial, individual life and annuities, group benefits, or retirement provider, you will see fundamental changes to your business models, value chain and how you acquire, retain and train your highly skilled talent over the next decade.

Irrespective of whether you are a developed market, emerging market, or global insurer, you need to anticipate these changes and prepare for growth.

PwC has developed and facilitated three types of workshops to help clients plan for the future:

Fiercest Competitor workshop

Fiercest Competitor is a rich, fast-paced experience that challenges leadership teams to imagine what could significantly disrupt their sectors, and then think about how they can drive that disruption to elevate their businesses to a higher level of competitiveness. We will help you create your worst competitor nightmare, so you can identify your organisation's weaknesses and where you need to modify its approach. This session helps you explore what plans you need to put in place to future proof your business and identify who is best placed to deliver.

Future Positioning series

PwC works with insurance clients to identify the business drivers key to their business and market positioning across the five STEEP categories and then helps the client rate those drivers against what they feel are important. After assessing the impact of each driver on business functions, PwC will help clients make changes to their business design to avoid risks and exploit future opportunities while equipping them to Act, Prepare and Monitor:

- **Prepare:** Determine 'no regret' moves to be completed in the near-term.
- **Act:** Start those activities that have a longer lead time.
- **Monitor:** Identify future signposts to act at a later time.

Global growth strategy

By utilising our detailed and multifaceted approach to planning international growth, insurers can implement a well-planned and executable strategy. When expanding internationally, insurers should consider the unique profile of specific territories relative to their unique capabilities and positioning. Our proprietary frameworks and tools, including Growth Radar™, Growth Navigator™, and Growth Pursuits™ help insurers define and execute their international growth strategies.

This paper covers only a little of the picture and there is much more to share and discuss. To find out how PwC can help you understand what's beneath the surface and support you in the creation of your future, please contact the team listed on the next page.

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