Willis Towers Watson

The future of financial services:

how work is impacted by the connection and convergence of people and technology

How insurtech could alter the foundations of risk: capital matching

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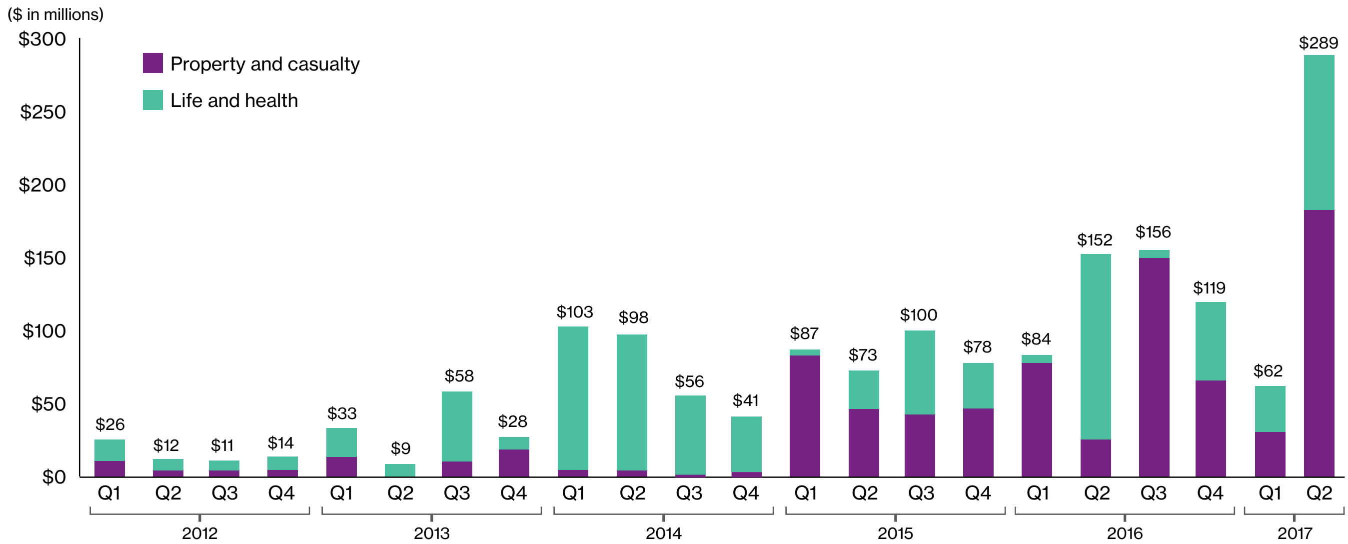
Insurtech is the portmanteau of 'insurance' and 'technology'. It refers to no specific technology, or usage of technology, rather a general leveraging of innovative, contemporary technology. Sound bites echo throughout the industry; promoters portend uber-like or skype-like disruption, spelling the imminent end to the insurance industry as we know it, meanwhile naysayers expound the barriers to entry surrounding the industry and, less than a decade after regulation was broadly considered to be ruining the insurance industry, it is viewed by some as a formidable strategic protector of the status quo.

The view we express to clients is ignore insurtech at your peril, however focus on substance and not noise. Rather like the world of phone apps, there is lot of so-called clever kit that ultimately delivers an irrelevant outcome. Many readers might recognise the knee-jerk decision to download an app, only to realise that benefit was both irrelevant and illusionary.

> "The last decade has seen technology fundamentally alter the value chain: Alibaba, the world's most valuable retailer holds no inventory, Facebook, the most popular media owner creates no content and Google the largest software vendor doesn't write apps. Might the largest insurer of the future have no owned capital?"

Globally, there are approximately 1,500 recognised insurtechs. Of them, over 40% are focused on distribution and 30% are focused on new product innovation. As the data below indicates, growth in investments and transactional volumes in the insurtech space are not slowing down; in fact, Q2 2017 represents the single highest insurtech funding volume of any quarter. Furthermore, a great number of non-US based insurtechs are coming to the fore, in Europe and Asia specifically.

Quartely insurtech funding volume - early stage



Deal count

P&C:	4	1	4	3	4	2	5	5	4	2	5	6	8	8	8	13	33	9	23	20	15	21
L&H:	6	3	6	7	8	4	6	4	7	9	16	8	7	8	10	18	8	9	4	11	10	19

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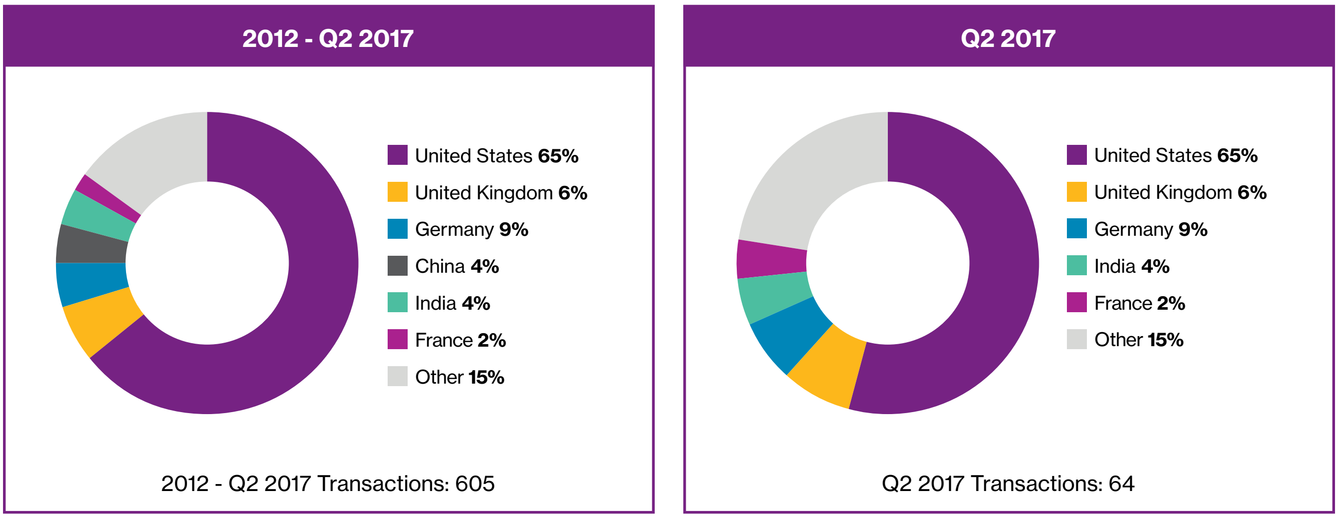
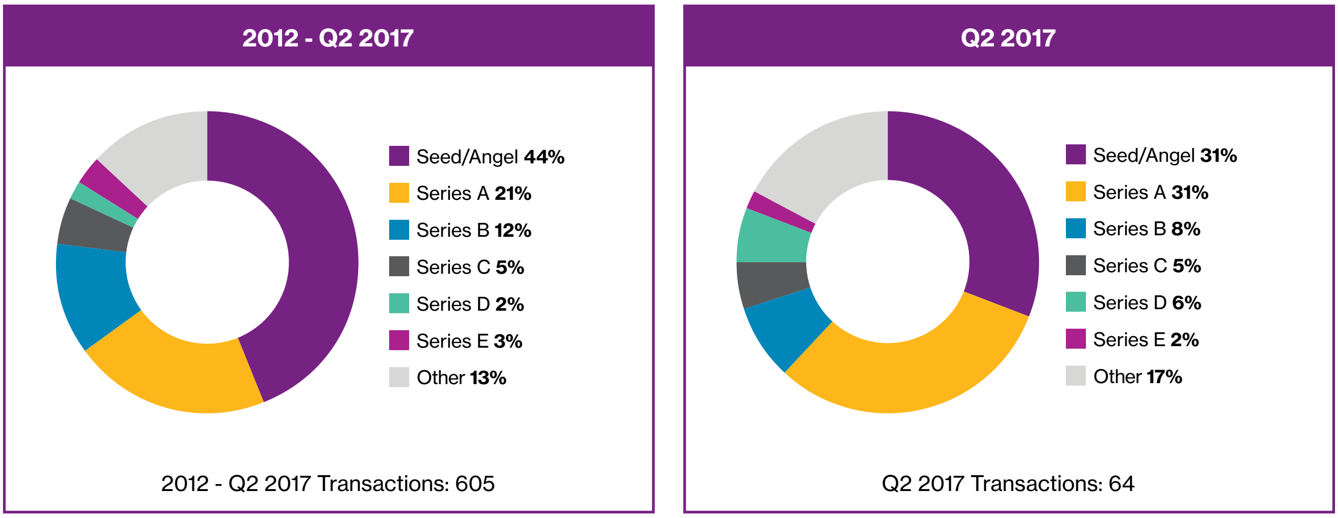
Insurtech transactions by target country



Insurtech transactions by investment stage



Sifting through WTW data on insurtech, it's clear that the capacity to deliver tangible or strategic outcomes for insurers' day-to-day dealings is, unsurprisingly, causally connected to the three fundamental drivers of cross-cycle operating performance within the industry.

Distribution

The delivery of products and the accessing of risk by the broadly distributive networks; made possible by widely adopted, highly innovative technology

Distribution

Does it (more) directly connect the customer universe and/or otherwise improve the customer experience in a compelling and distinctive way thereby fuelling growth and/or reducing distribution costs and/or real stickiness in the customer relationship?

- *Old-world example:*
  DirectLine – leveraged wire technology and the cultural norm of buying over the telephone
- *New-world example:*
  PolicyGenius – independent online insurance marketplace

Underwriting

The use of big data, real-time analytics and telematics devices to better price risk for the purposes of more effective, appropriate and ultimately, accurate underwriting. Made possible by the leveraging of innovative technology

Underwriting (risk pricing and/or risk selection)

Does it provide access to information that allows for materially improved precision in the pricing or selection of risk, delivering a measurable advantage relative to competitors?

- *Old-world example:*
  AIR/RMS – catastrophe modellers, using historical data to price risk
- *New-world example:*
  30mHz – censor-driven, real-time data derivers, presenting real time risk profiles in the commercial space.

Operational efficiency

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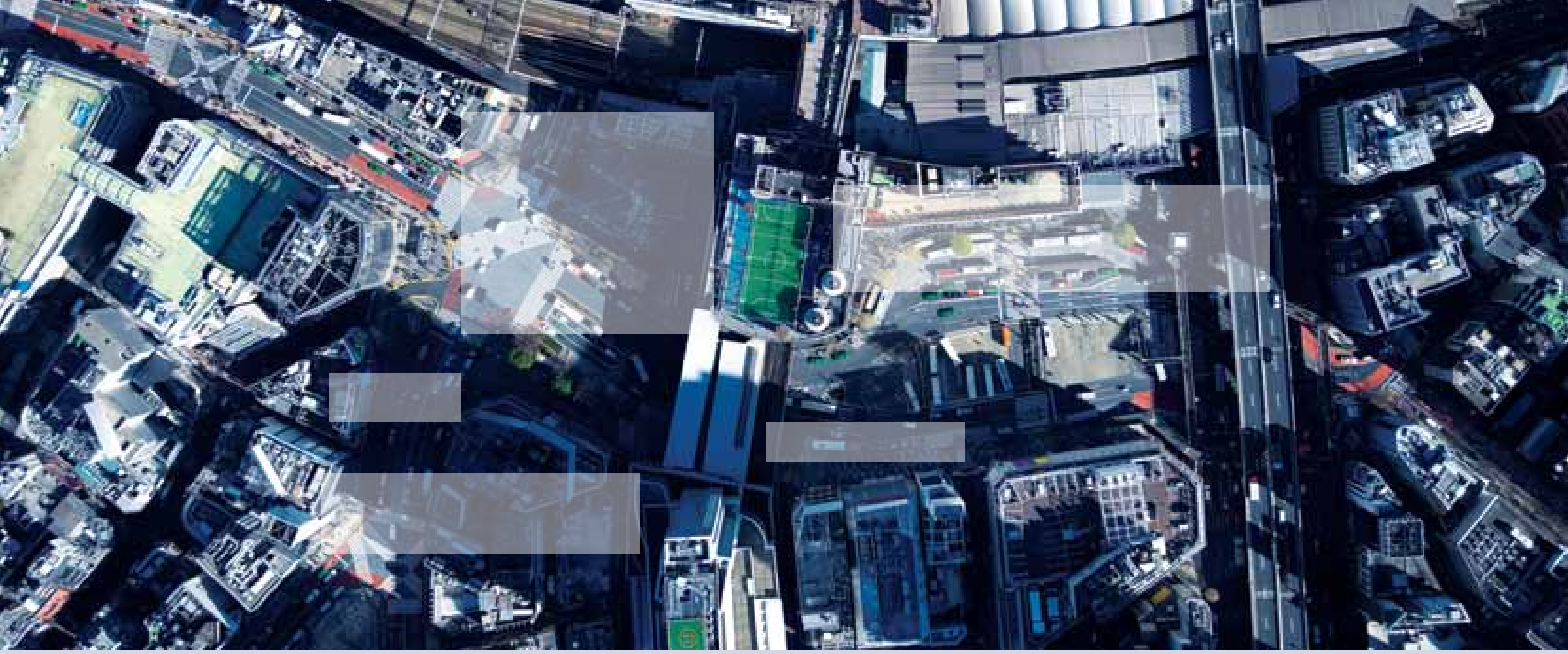
The use of technology to automate systems, improve processes in order to lower expense ratios. The expedition of incumbent modes of practice at lower cost and higher speeds

Operational efficiency

Does it reduce the non-loss cost of the business, improving performance through enhanced efficiency thereby widening gross margins that translates directly to improved returns to owners, improved pricing to customers or both?

- *Old-world* example:
  IBM Watson – analysis with automated data visualisation, capable to automating high volume low complexity tasks
- *New-world example:*
  InsureScan – using photographic imagery and scan technology to generate motor policies



Most large insurance groups have implemented digital or insurtech strategies for some time, variously incubating, investing or forging other forms of partnership with insurtechs that they believe will support their chosen strategy.

What becomes crystal clear is that those insurers who use the new technologies available to improve the insurance industry model most effectively will achieve an advantage; those that don't will suffer as others secure proximity to the client, improve efficiency, underwriting the three main pillars of the insurance model.

What is less clear is the longer-term impact of technology generally and insurtech specifically especially when combined with the changes in both type and source of capital available to finance insurance risk. Clearly insurtech has the potential to attack established distribution channels and in select lines to collapse large swathes of the value chain; personal lines auto insurance is an obvious example. Insurance companies are, at their simplest (largely) fixed pools of capital seeking portfolios of insurance risk from which to earn a return. Today's business model is rooted in the 19th-century concept that the key stakeholder is the capital provider and risk taker in the system. The implicit assumption is that the risk taker is entitled to the majority of the reward, which made sense when capital was scarce and opportunity plentiful. We can see that in technology-intensive sectors the balance of power between the owners of capital and the owners of ideas has swung dramatically in favour of the entrepreneurs, essentially because of the shift in emphasis from physical to human capital.

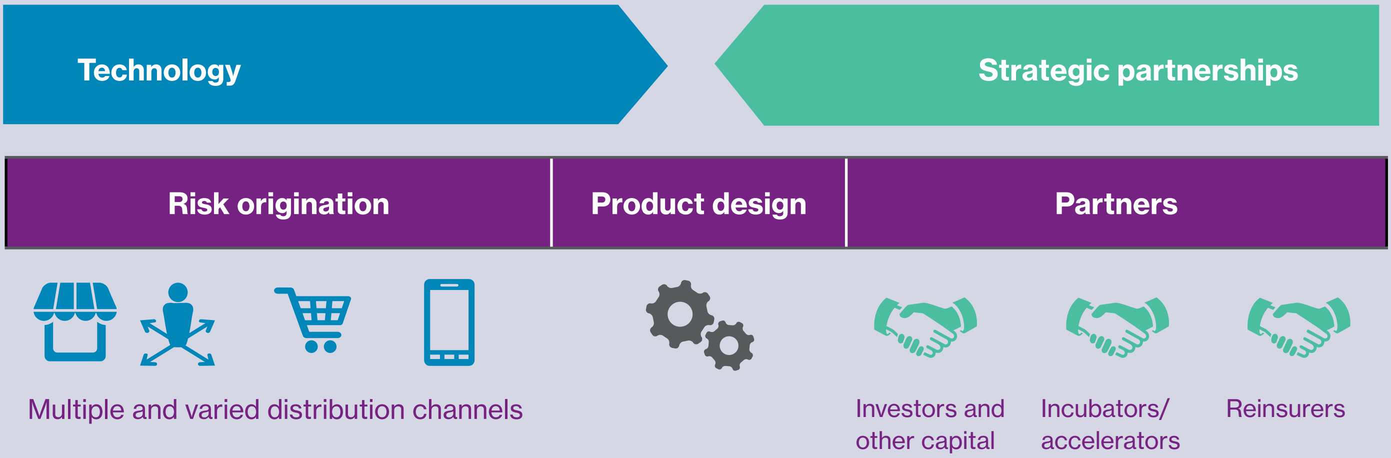
In an insurance world where technology has the potential to eliminate barriers to entry, weaponise data and create new forms of information from which to more precisely gauge risk thereby lubricating the appetite of alternative capital, frankly, who needs a conventional insurer other than to provide a piece of regulated paper?

Conversely insurtechs themselves are invariably not fully fledged full-stacked end-to-end insurance companies, complete with balance sheet and regulated paper. More often than not, they specialise in one part, perhaps even the critical defining part but one that only works as part of a myriad of processes. The vast majority of insurtech start-ups will not survive infancy – not because they are not innovative or creative, but because they are not solving pertinent insurance pain points; both internally and externally. Much of what is observed in the marketplace is either tech for tech's sake, or projects that are so specific and nuanced that issues of scale will pervade them until their demise. Navigating our industry can take such a long time that firms simply exhaust their operating capital. Furthermore, despite what they may have you believe, a user-friendly website, tech jargon and buzz wordery alone is not enough for an insurtech to make it, even in an industry that is so clearly ripe for some form of change.

Our role at Willis Re is to match risk with capital. Our insurtech strategy leverages those skills to the broader source of risk that insurtech might unlock with the broader sources and forms of capital that are looking to get as close to the source of risk as possible and align with those who a sustainable competitive advantage.

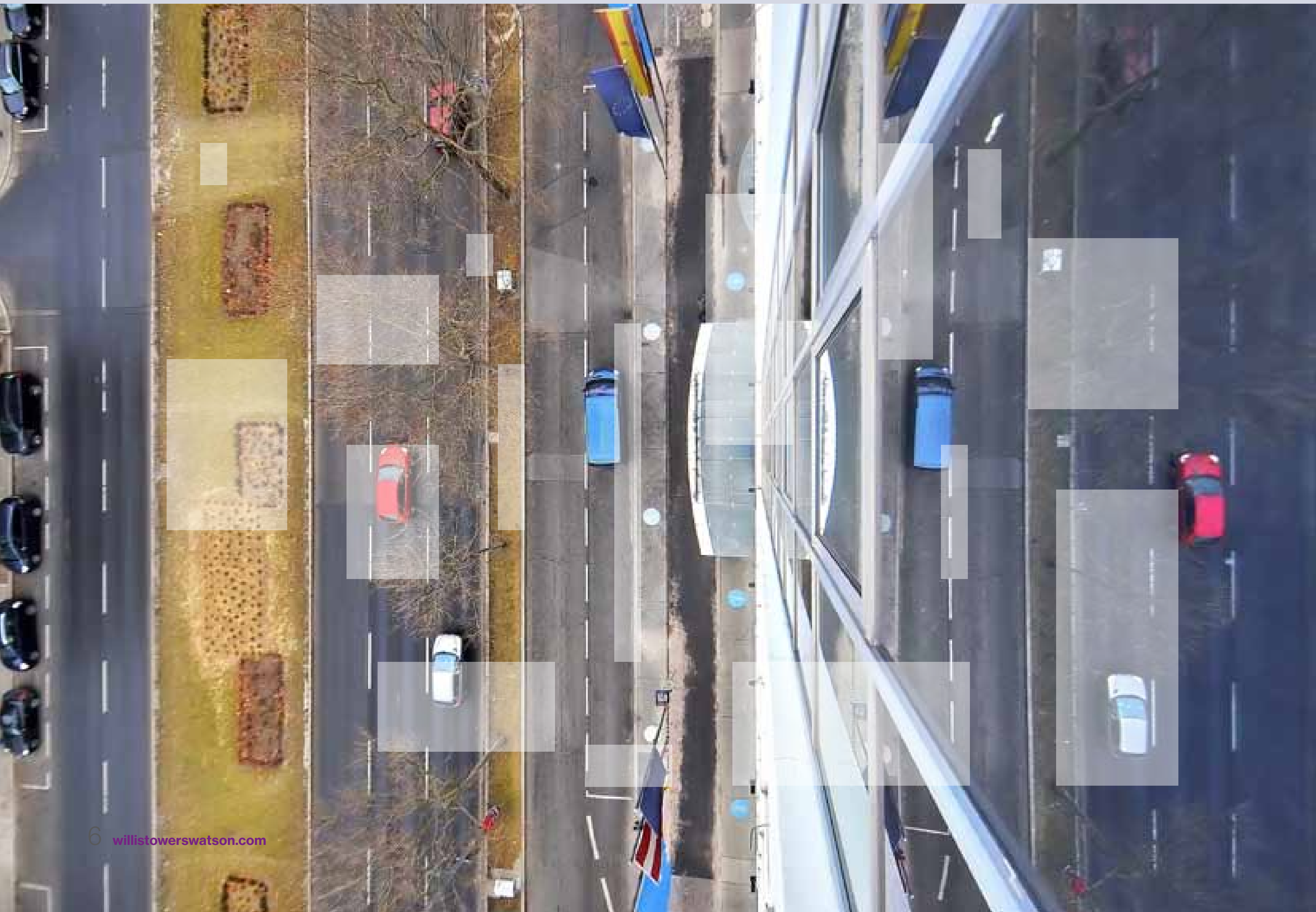
The last decade has seen technology fundamentally alter the value chain: Alibaba, the world's most valuable retailer holds no inventory and Facebook, the most popular media owner creates no content. Might the largest insurer of the future have no owned capital?

If that's too grand, fast forward to a more moderate prediction: the combination of effective, readily available technology, a consumer market with different buying expectations and an ever-increasing influx of non-traditional capital must surely be ripe for the more dislocation than at any other time in living memory.



Given the potential dislocation the insurance industry is facing, it may well be that companies of the future will be structured around a model like the one the graphic here depicts. This is where technology and risk origination are synonymous with one another, delivered through a number of devices and platforms. Financing and capital come from a variety of traditional and non-traditional sources predicated on a variety of strategic alignments between incumbent and nascent. All of these are centred on the centrifuge of product design.

Whatever the future holds, at Willis Re we focus a great deal of time and energy on monitoring the market, analysing trends and engaging with both start-ups in the insurtech ecosystem and our clients. We continue to fortify our position as thought leaders in the space by predicting such potential outcomes and consulting and advising around how best we can all take advantage of and benefit from the changes the industry is undergoing.



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