Trends and developments impacting the life insurance industry and their CFOs & CROs

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Paul Headey, Head of Life, Asia-Pacific, Insurance Consulting & Technology, was recently interviewed by A.M. BestTV. Following is an edited transcript of the interview.

Q: Best's News Service A: Paul Headey

Q: What trends or developments are you seeing in the life insurance product mix in Asia-Pacific? What's driving that?

A: On the supply side, life insurers in Asia have traditionally focused on longer-term savings business with guaranteed returns to the customers. As yields have fallen and as regulatory capital requirements have increased, this has placed financial pressure on insurance companies, in terms of lower profitability and higher capital required.

We've seen a trend to diversify away from market or duration risk and towards insurance protection products and health products. Typically, term life, critical illness, accident and health products are more profitable and have a higher value-added of new business or return on capital. This boosts a company's financial results.

On the demand side, in many Asian markets, there is a significant protection gap, meaning that much of the population is under-insured. The challenge has been how to close this gap and to increase the penetration of insurance in these markets. In particular, for medical coverage, the perennial challenge is the high medical cost inflation, sometimes more than 10% in some markets.

This creates demand from the public for medical insurance, but then also a challenge for insurance companies - how to manage and control the claim cost. They can address this through regular repricing of medical business or altering product design, offering wellness programmes, or distributing through private clinics and HMO (health maintenance organisation) networks. Overall, there is a trend for insurance companies to move away from just quantifying and pricing risk towards influencing and reducing the risks they face by adopting a more long-term and collaborative model.

Q: What are some of the key trends and issues life insurance CFOs and CROs are facing these days?

A: We're seeing trends towards increased compliance, efficiency, and good governance. This is partly driven by new regulations, a more demanding regulatory environment, particularly on accounting standards and capital requirements such as the new risk-based capital regimes.

We're moving towards greater automation and real-time processes to enable faster and more accurate valuations and improved auditability. We're also seeing increased focus on cost control, improving efficiency of processes, and considering options such as outsourcing or offshoring to lower-cost locations.

Another trend is that capital management is becoming a much higher priority as yields staying low and regulatory requirements becoming more onerous. In general, we're seeing more sophisticated capital models being developed. Enterprise risk management practices are evolving such that the risk management function is moving much more towards being a strategic business partner, rather than purely a compliance function. Last, but not least, reinsurance is increasingly used to optimise risk and return and to manage solvency volatility.

Q: How do you see the new accounting standard IFRS 17 impacting the insurance business in Asia-Pacific?

A: I think the impact is going to be in three main areas. First, implementation. Second, presentation of financial performance in the future. Third, the strategic implications to the business model. In terms of implementation, this is going to be a massive development change project. It will impact data systems, accounting interfaces, actuarial models, and finance functions. In short, really it impacts the whole company. In many cases, this will be a catalyst for process transformation. I think it has huge implications for human resources, skill sets, experience required, time, and cost.

Most, if not all, insurers will need to upgrade their staff and systems to cope with this. There really isn't much time left to prepare, less than two years in some cases. Really, companies need to start as soon as possible. Secondly, in terms of presenting financial performance, this will be a complete change, including different treatment of profitable and unprofitable contracts and separation of insurance and investment business.

The intention is to improve consistency, transparency and comparability of financial statements between different companies and to better reflect the underlying nature of the contracts, the risks, and the profitability. It's likely to result in a different rate of profit emergence and book value being presented to stakeholders for insurance companies. There may be some surprises.

Finally, in terms of strategic implications, some insurers may find they need to adapt their business models or strategies as a result, for example, to avoid excessive P&L (profit and loss) volatility. The areas that they could look at would be ALM, how to improve their asset-liability matching; product development and design, for example, moving towards less-risky or more-profitable products; and adopt an active capital management approach. In short, this is a complex project with potentially material implications for business models.

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