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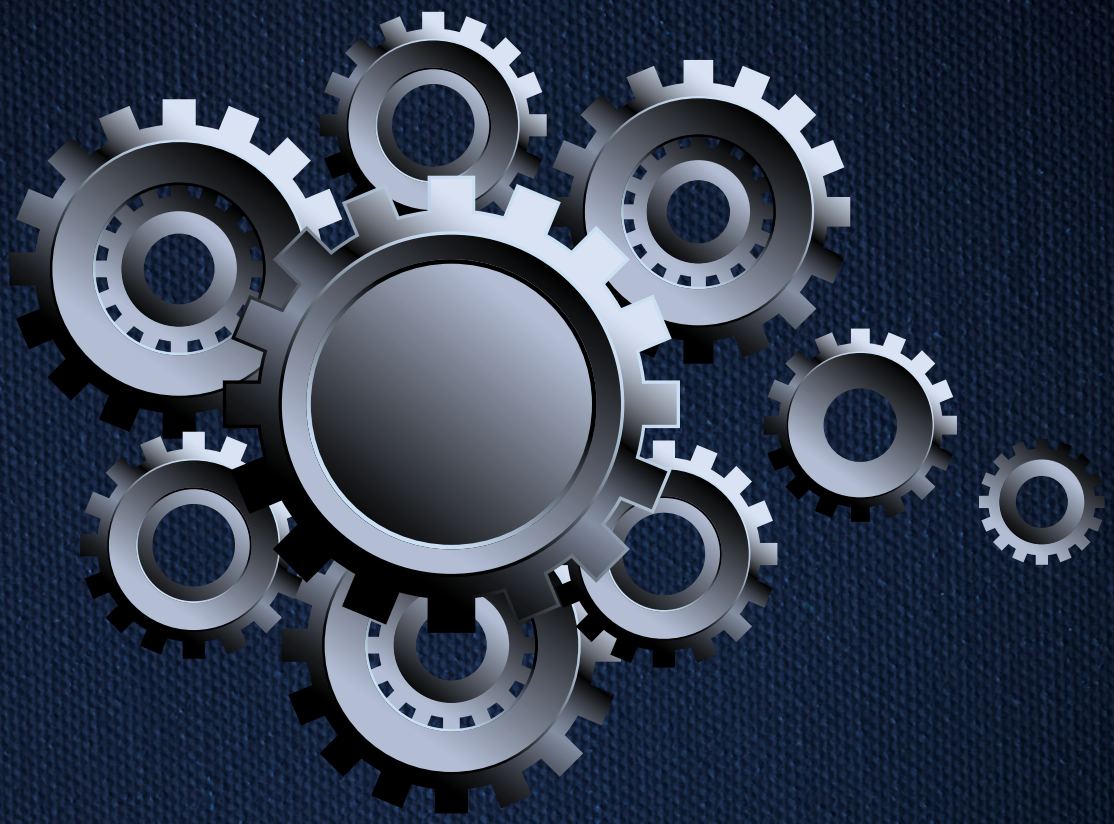

Insurance Outlook Report 2020/21

East Africa

November 2020

Content

Where do insurers stand in 2021?

While insurers have been able to absorb the underwriting impacts of large loss events such as COVID-19, the impact on insurance companies' profitability is still uncertain. Despite the efforts put in place by governments to cushion the public from the adverse economic effects of the pandemic, the outlook on long-term impacts and recovery from the pandemic is still uncertain as it will take time for businesses to recover. With stock markets showing declines in performance and flattening yield curves, insurers are set to experience poor performance in their investments and this will flow through to their bottom line results.

Consumers are under pressure to cut down on "unnecessary" expenses, and insurance premiums are likely to fall under this category, putting pressure on both new business volumes and client retention. This will be exacerbated by the increased level of mistrust in the industry as insurers rely on exclusion clauses to limit their claim pay-out exposures, fuelling even higher than expected lapses and policy cancellations. Given that COVID-19 has had a varying impact on the health and welfare of individuals, it is also uncertain whether insurers will need to revise key mortality and morbidity assumptions.

However, COVID-19 has also brought the digital revolution in insurance closer than before. Insurers have traditionally been on the outside of insurance innovation and are now facing the pressure to transform their operating and business models. InsurTech start-ups and companies that are completely outside the traditional insurance space are encroaching the territory which largely belongs to insurers in the past. Therefore, it is critical for insurers to upgrade their technological capabilities under the umbrella of innovation to maintain or grow their market penetration.

Social distancing measures are challenging the status quo from an external and internal perspective. Insurance companies have long depended on legacy systems and traditional face-to-face distribution models to maintain their share in the market. With lock-down measures and strict protocols across the region, these "business as usual" models are being challenged. Insurtech companies are much more agile and able to respond to business environment changes, challenging insurance companies to pivot towards disruptive technologies faster than they had planned.

Insurers will need to rethink their operating models, reimagine their workforce, and start thinking of agile ways to bring innovative products to the market. With the increasingly discerning consumer, insurers should start being aware of the potential for external market participants to encroach their market share. Consumers are looking for solutions to manage their risk in a way that is convenient to them, and insurers need to develop solutions that meet these needs instead of the traditional product-push approach that has been successful in the past.

With growth in premiums already constrained moving in to 2021, insurers need to immerse themselves into transforming their businesses from the inside out. It will take transformative changes in insurers' strategy and operating models to withstand the waves of change that are threatening to disrupt the future of insurance.

As if insurers don't have enough on their plates, the effective date of IFRS 17 for insurance contract reporting is fast approaching. The business pressures that Covid has brought has meant that insurers will need to be extra focused on an efficient financial reporting transformation to be compliant with the requirements of the standard. Deloitte has developed several accelerator tools to support clients in reviewing, refining, and developing their systems to reach compliance before the 1 January 2023 deadline.

The time to start thinking strategically about how to pivot during these uncertain times, in a way that not only protects insurer's balance sheets, but ensures survival, is now.

Our outlook is based on the first-hand experience and insights of Deloitte's subject matter specialists, supplemented with research and analysis by the Deloitte Centre for Financial Services. We hope you find it thought provoking as you contemplate your strategic priorities and adjust your agenda for the year ahead.

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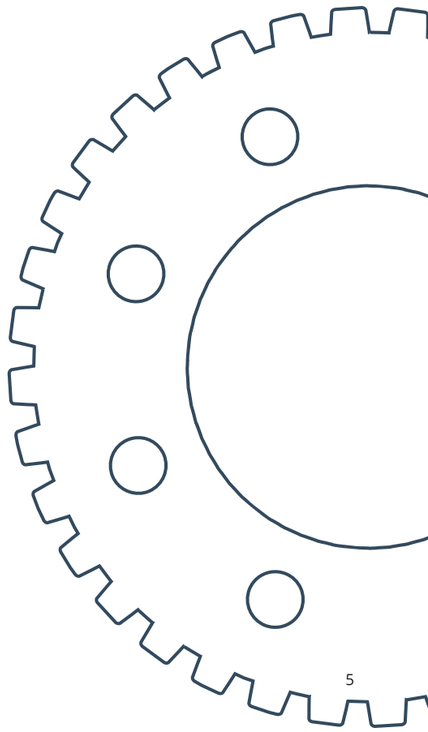


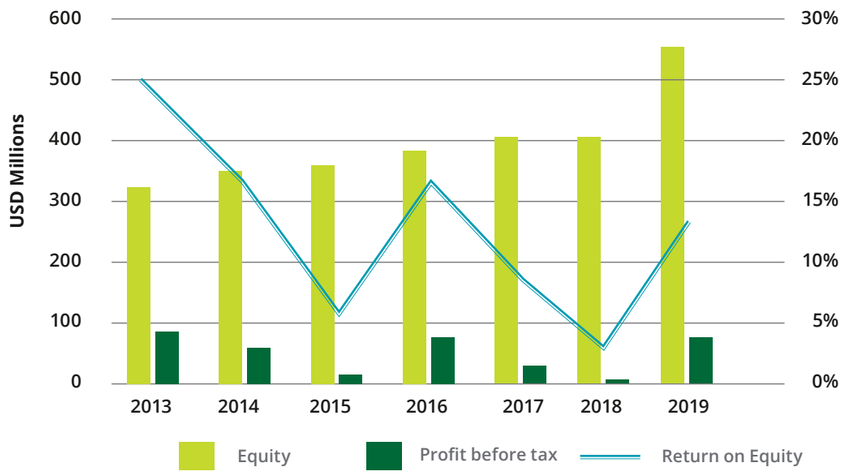
Kenya

Life Insurance - Kenya

Life insurance industry performance

The insurance market in Kenya has experienced consistent growth since the year 2013 marked by the increase in premium revenue and capital investments. However, the Return on Equity has declined since 2016.

Life insurance industry overall performance (2013 - 2019)

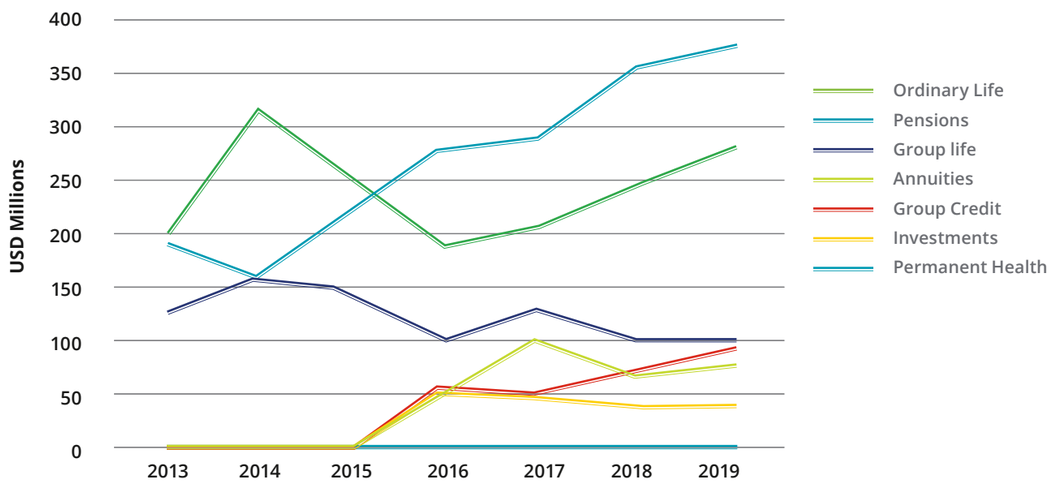


Source: IRA Kenya Industry reports 2013 - 2019

Constituents of life industry premiums

The insurance life market is characterised by seven main products with ordinary life, group life and pensions being the key products in the market. Group credit, annuities and investments entered the market in 2015 and have shown an overall steady growth rate. Permanent Health has not experienced significant growth within the last 4 years.

Index of total L&A direct premiums (2013 - 2019)



Source: IRA Kenya Industry reports 2012 - 2019, BMI Economic data

Ordinary life has experienced a steady growth since the year 2016.

Group life has experienced a slower growth rate in comparison to other business classes in life insurance due to the price wars that have been prevalent among the industry players.

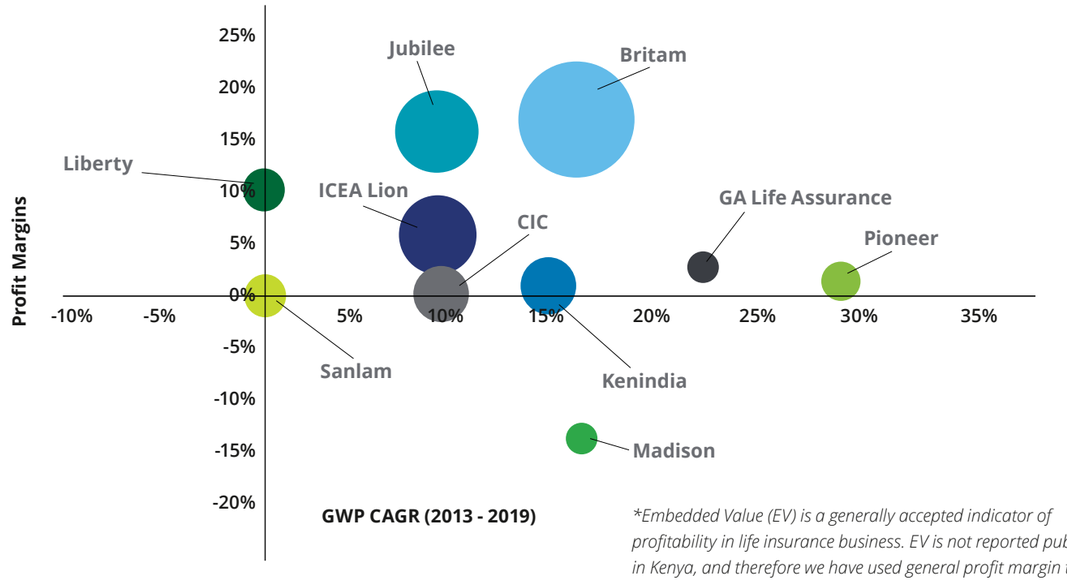
The pension business has grown since 2014 due to increase in demand and uptake of retirement and savings products, especially among Small and medium-sized enterprises (SMEs). Given that the pension business has consistently been the fastest growing product line, there is an opportunity to enhance annuities and maximise on customer lifetime value.

Insurers need to be prepared for a potential contraction in premium growth arising from corporates cost-cutting on non-essential expenses. Loss-making products such as Group Life are likely to experience a further deterioration as insurers further undercut to maintain their client base.

Competitive landscape

The graph below shows an analysis of the top 10 life insurance companies in Kenya, highlighting their compounded growth in relation to their profit margin.

Kenya top ten life insurers performance



**Embedded Value (EV) is a generally accepted indicator of profitability in life insurance business. EV is not reported publicly in Kenya, and therefore we have used general profit margin to rank these insurers by profitability.*

The size of the bubble represents the gross written premiums for the year 2019.

Most of the top 10 insurers have experienced reasonable premium growth with an average premium growth of 11% over the year 2018/2019.

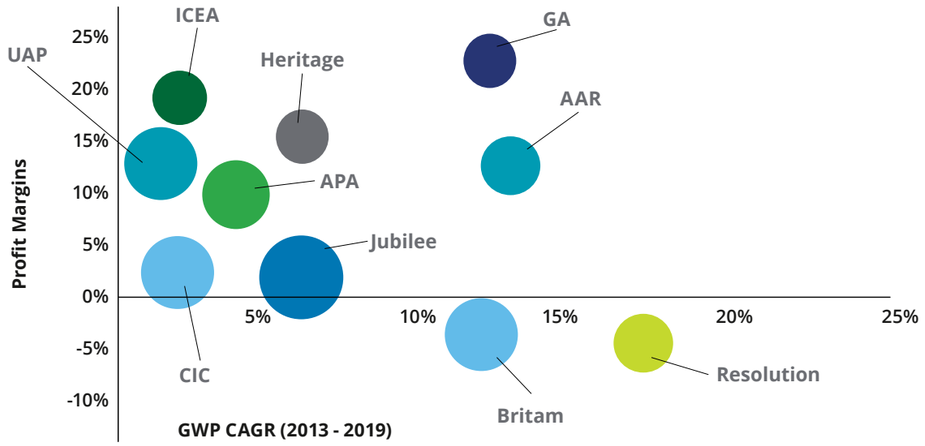
Given the low penetration of life insurance in the market and the need for cover, there is opportunity for insurers to repackage their products in a way that appeals to customers. Distribution through social groups and organizations will be key – this requires investment in Information and Technology (IT) that supports convenient and transparent perception from customers' perspective.

General Insurance- Kenya

Competitive landscape

The graph below shows an analysis of the top 10 general insurance companies in Kenya, highlighting their compounded growth vis-a-vis their profit margin. The size of the bubble represents the gross written premiums (GWP) for the year 2019.

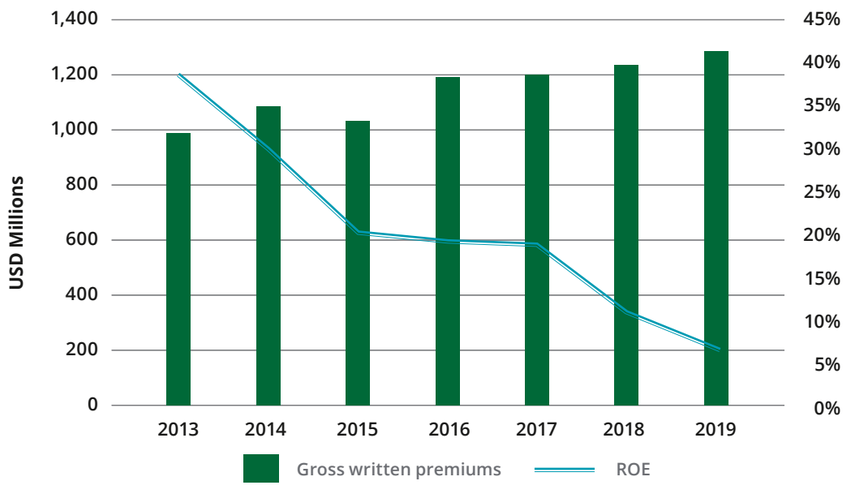
Top ten general insurance players' performance



Source: IRA Kenya Industry reports 2013 - 2019

Insurers experiencing diminishing returns on equity

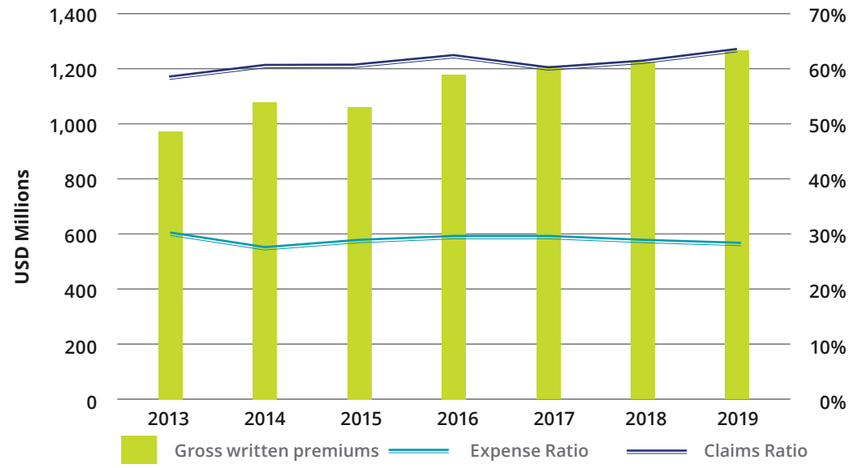
The returns on equity have been on a downward trend despite consistent year-on-year increase in GWP. Squeezed margins in the sector, continued cases of fraud, and premiums that have grown at a slower rate than the economic growth, have had a negative impact on shareholders' returns. As premiums have increased by less than the GDP growth rate, the general insurance industry should prepare for a slow-down in premiums as corporates and consumers cut down on insurance costs. The motor class is also expected to experience a slow-down in premium growth as travel restrictions that prevailed earlier in the year reduced the need for motorists to renew their cover.



Source: IRA Kenya Industry reports 2013 - 2019

Expense and claims ratios in 2019

The general insurance industry has experienced stable but slow growth in GWP from 2013 to 2019. The expense and claims ratios have been on a slightly upward trend for the past six years with a slight decline in expense ratio for the years 2018 and 2019.

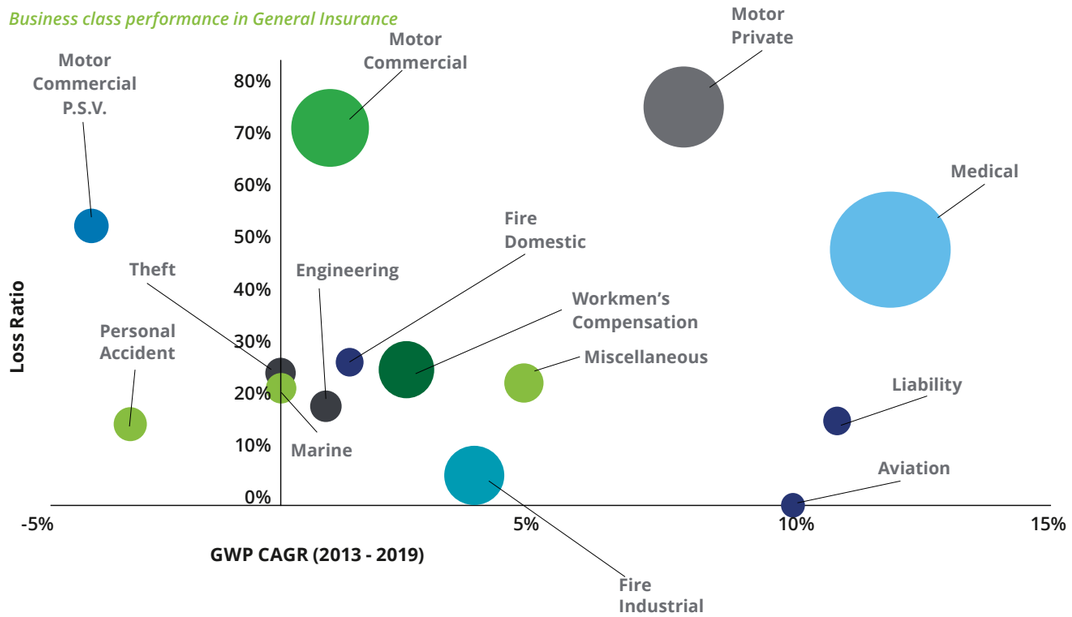


Source: IRA Kenya Industry reports 2013 - 2019

Performance of insurance classes of business

The graph below shows an analysis of the insurance classes of business in Kenya. Their annual growth rate is plotted against their profit margin.

Business class performance in General Insurance



Source: IRA Kenya Industry reports 2013 - 2019

As seen in the graph above, motor private, motor commercial, and medical business are the largest classes of business by GWP. However, they are also among the least profitable business classes, and have consistently underperformed as loss leaders in the market.

Insurers are yet to provide innovative products in the retail market that meet the evolving needs of their consumers and adequately cover the risks involved; opportunities to better serve and price customers using digital are yet to be capitalised.

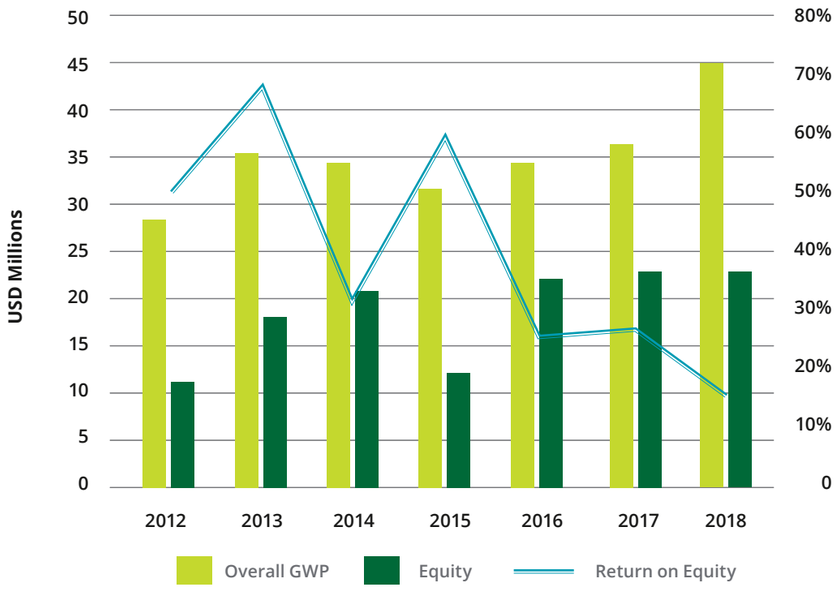
Tanzania

Life Insurance - Tanzania

Life insurance industry performance

There has been a positive year-on-year growth in GWP from 2012 to 2018. Similarly, capital invested in the industry has been on the rise over the last three year, while returns on shareholders' equity have been on a downward trend over the last four years.

Life insurance industry overall performance (2012 - 2018)

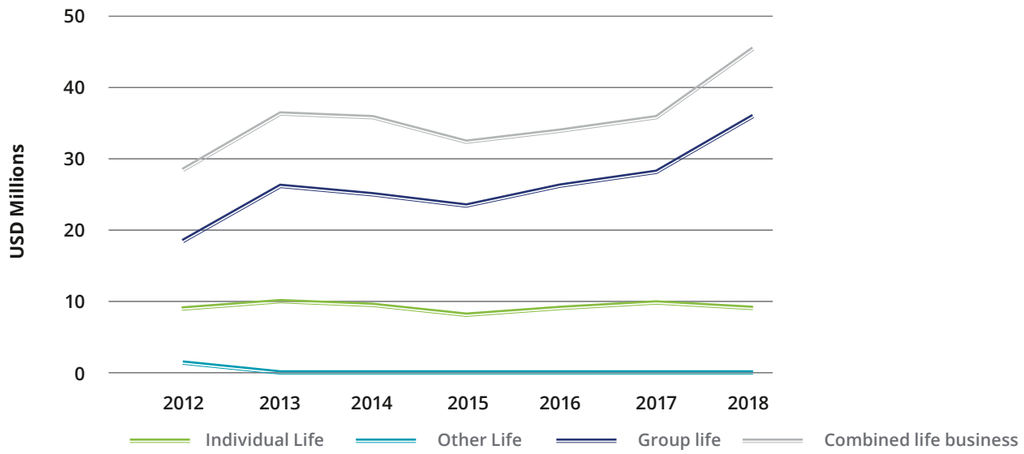


Source: IRA Tanzania Industry reports 2012 - 2018

Constituents of life insurance industry premiums

Group Life contributes the most towards the life insurance industry in Tanzania followed by Individual Life class of business.

Index of total L&A direct premiums (2012 - 2018)

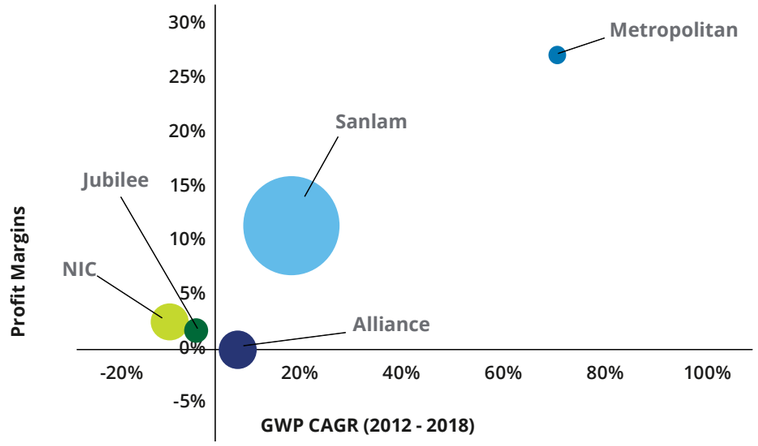


Source: IRA Tanzania Industry reports 2012 - 2018

Competitive landscape

The graph below shows an analysis of the top 5 life insurance companies in Tanzania and highlights their annual growth rate against their profit margin.

Tanzania Top 5 life insurers performance



**Embedded Value (EV) is a generally accepted indicator of profitability in life insurance business. EV is not reported publicly in Tanzania, and therefore we have used general profit margin to rank these insurers by profitability.*

The size of the bubble represents the gross written premiums for the year 2018.

Source: IRA Tanzania Industry reports 2012 - 2018

Life insurance is predominantly driven by Group Life. Retail life insurance products are the smallest in all three countries (Kenya, Tanzania, and Uganda). Given the small average market size, insurers need to investigate ways of profitably selling insurance to specific target customers within the population. Formation of strong partnerships with companies that have good distribution networks such as Telcos and banks, will be key in tapping unserved segments.

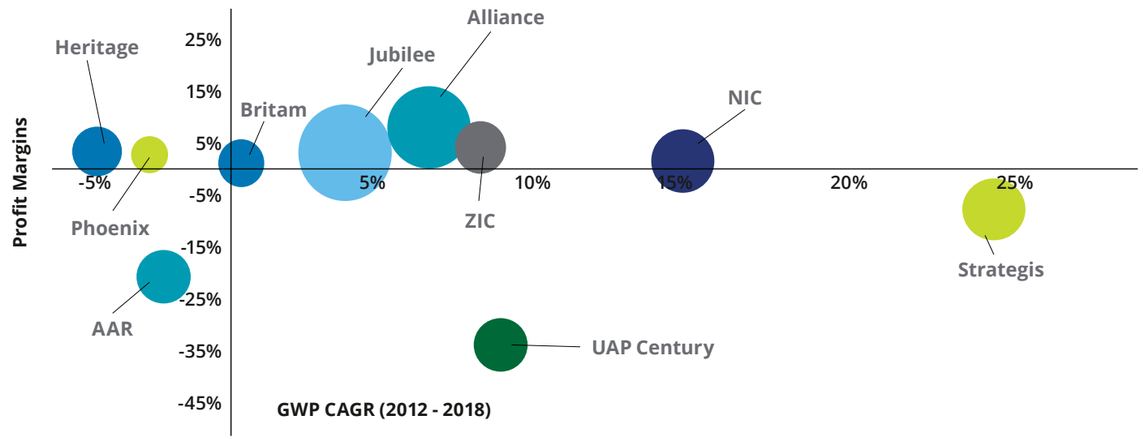
General Insurance- Tanzania

Competitive Landscape

The graph below shows an analysis of the top 10 insurance companies, highlighting their compounded growth vis-a-vis their profit margin.

Performance in this industry was low with most companies reporting profit margins within 3% and 6% bracket. The performance observed is in line with the undercutting practices and limited capacity of the players in the market to underwrite risks without transferring a significant part to reinsurers.

Top ten general insurers performance



Source: IRA Tanzania Industry reports 2012 - 2018

Performance of insurance classes of business

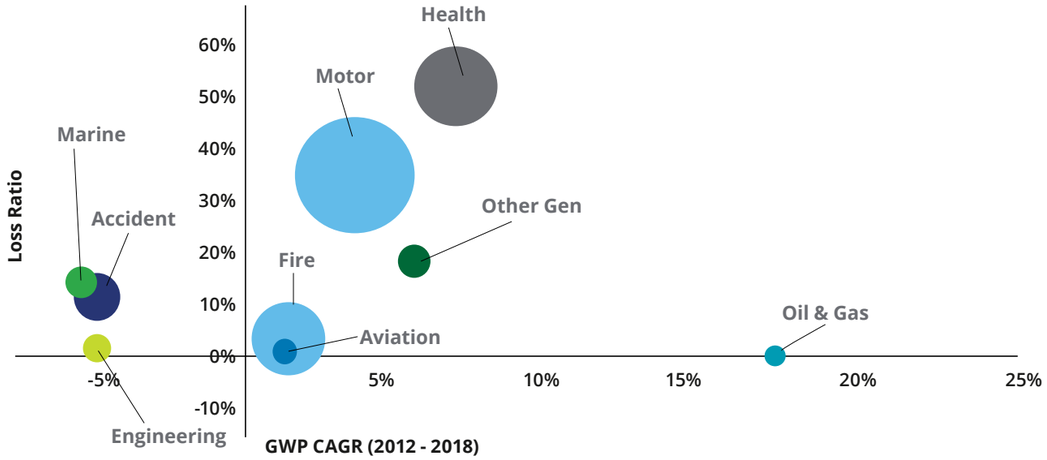
The graph below shows an analysis of the insurance classes of business in Tanzania. Their compounded growth is compared against their profit margin. The size of the bubble represents the GWP for the classes of business for the year 2018.

The largest growing business classes in the Tanzanian general insurance field are motor and health businesses. However, the classes with the largest size in terms of GWP are also the business classes with the highest loss ratios.

The motor business is the largest class with a significantly lower loss ratio than the medical business.
Private health insurance covers approximately 1% of the population and is significantly under scale. There is an opportunity for partnerships with companies that have established distribution networks to tap into the unserved retail segments. Given the high loss ratio associated with the medical class of business, proper underwriting needs to be put in place as this line of business remains largely untapped.

Companies need to differentiate themselves in customer and operational excellence using technology.
The fire class of business is worth noting as it is among the large classes of business in GWP recorded but has a significantly lower loss ratio compared to both the large and small classes of business in GWP.

Performance based on individual business classes

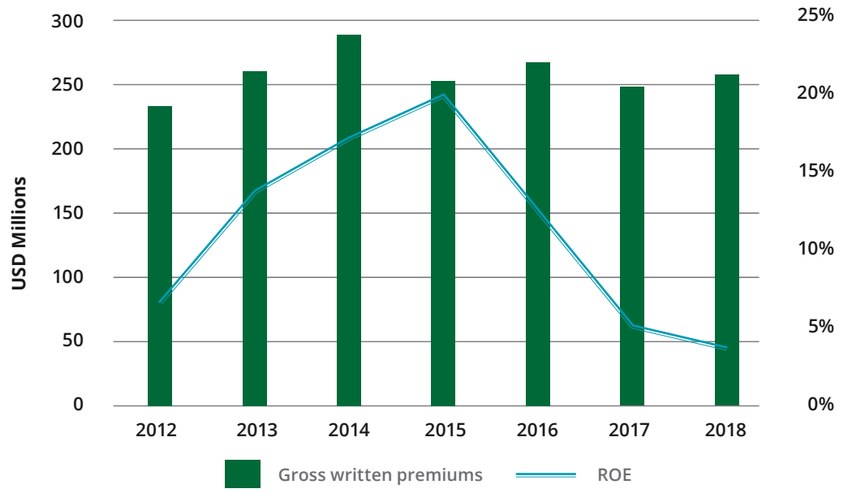


Source: IRA Tanzania Industry reports 2012-2018

Insurers are experiencing diminishing returns on equity

The Return on Equity has been on the decline over the past four years, and was at its lowest in 2018, in comparison to the previous five years. Given the onset of the pandemic, we are likely to see a further dip in returns to shareholders.

General Insurance Industry Performance (2013-2019)

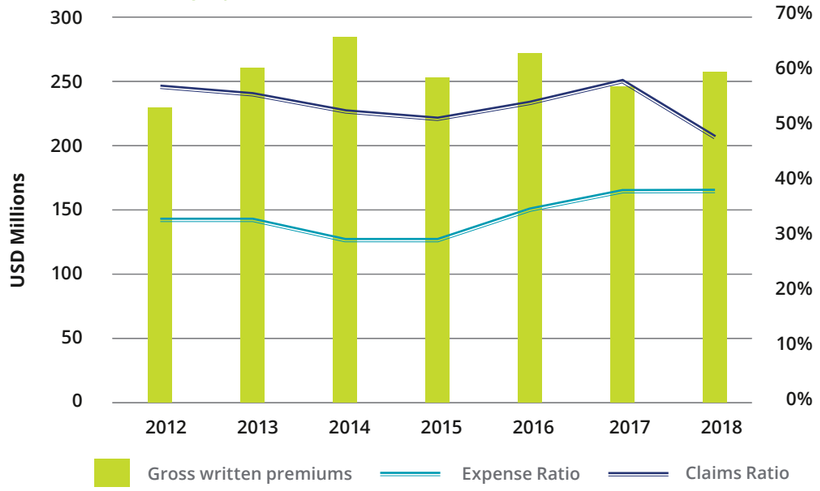


Source: IRA Tanzania Industry reports 2013-2019

Expense and claims ratios

The GWP have been growing at a stable rate from 2012 to 2016 with a slight decline in 2017 and then continued with an upward trajectory. The claims ratio has been on a downward trend from the year 2012 to 2015 then proceeded to rise from the year 2015 to 2017 and declined in the following year. The expense ratio has been on the rise over the past four years, indicating that the costs associated with underwriting general insurance have been increasing without a mirroring increase in the premiums charged for these risks.

General insurance industry expense ratio and claims ratio



Source: IRA Tanzania Industry reports 2013-2019

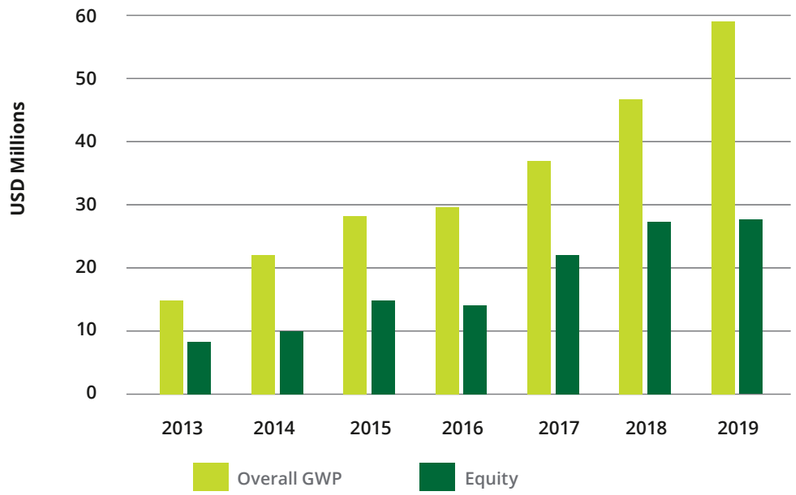
Uganda

Life Insurance - Uganda

Life insurance industry performance

There has been a steady growth in both the level of direct premiums and equity held by industry constituents in the life insurance market in Uganda.
The graph below shows the GWP and Equity invested in the life insurance market in Uganda.

Life insurance industry overall performance (2013-2019)

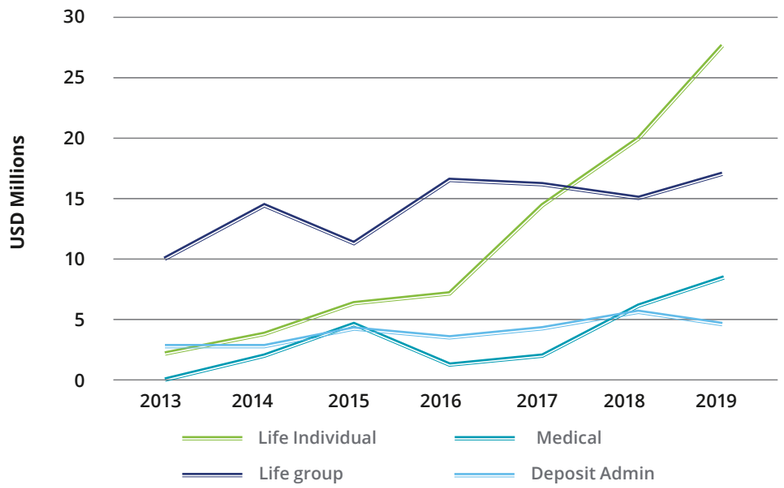


Source: IRA Uganda Industry reports 2013-2019

Constituents of life insurance industry premiums

Individual life is the fastest growing business class and has noted a consistent growth from 2012 to date. Deposit administration has also experienced a steady growth rate since 2013 to date. Group life and medical product lines have experienced a fluctuating trend characterised by volatilities in the movement of the GWP over the last three years.

Index of total L&A direct premiums (2013-2019)

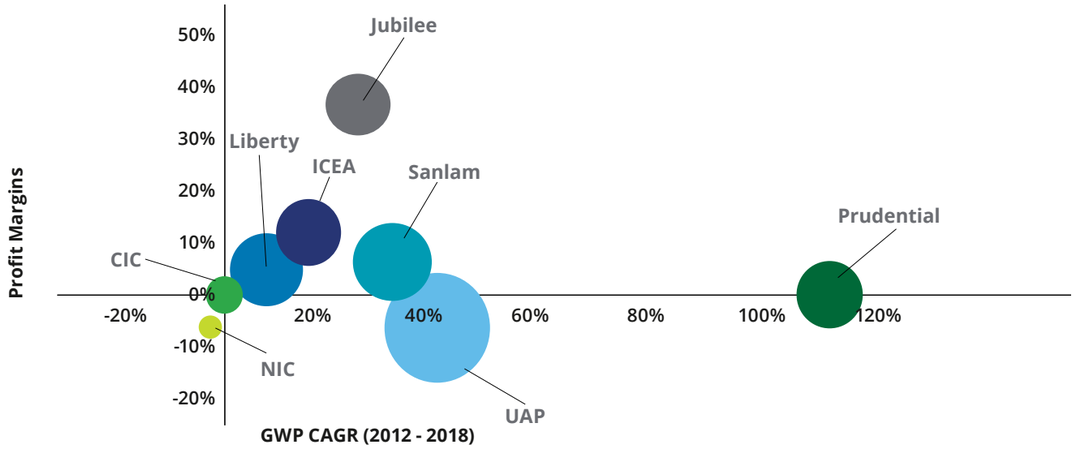


Source: IRA Uganda Industry reports 2013-2019

Competitive landscape

The graph below shows an analysis of the performance of life insurance companies in Uganda. The size of the bubble represents the gross written premiums for the classes of business for the year 2018.
Most market players have recorded profit margins within the range of 0% and 6%.

Life insurance overall performance (2012-2018)



Source: IRA Uganda Industry reports 2012-2018

**Embedded Value (EV) is a generally accepted indicator of profitability in life insurance business. EV is not reported publicly in Uganda, and therefore we have used general profit margin to rank these insurers by profitability.*
Profitability data for the year 2019 was not available. The data reflects the last 7 year's performance.

Individual Life is the fastest growing product group, mostly endowment/education-type policies. Take-up is largely by middle to affluent population.

There is a need to develop products that are more suited to customers at lower income levels – however, this will also require investment/ partnerships in distribution networks that are more efficient.

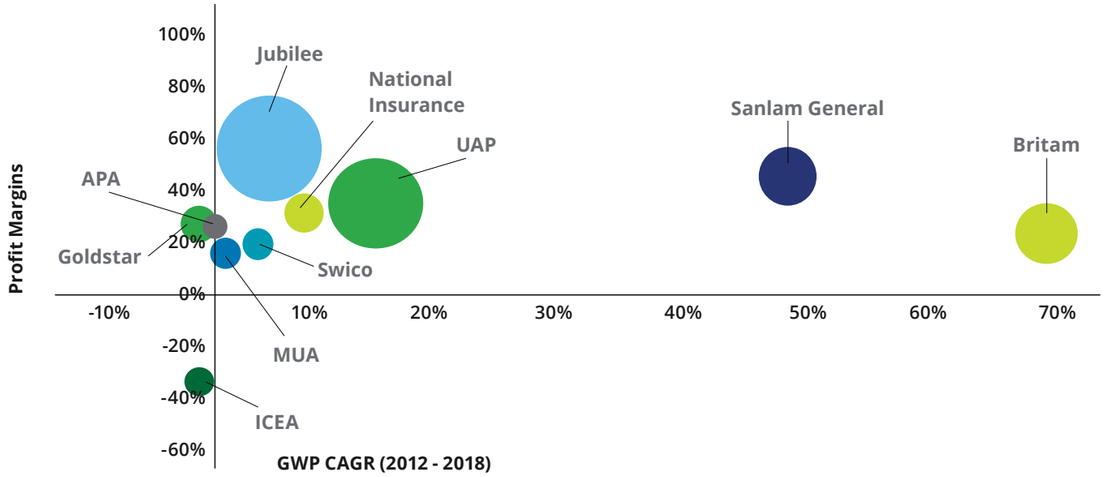
General Insurance- Uganda

Competitive landscape

The graph below shows an analysis of the top 10 general insurance companies, highlighting their annual growth rate vis-a-vis their profit margin. The size of the bubble represents the gross written premiums for the year 2018.

Most players in the market experienced an increase in growth and profitability in the year 2018.

CAGR vs Profit Margin vs GWP



Source: IRA Uganda Industry reports 2012-2018

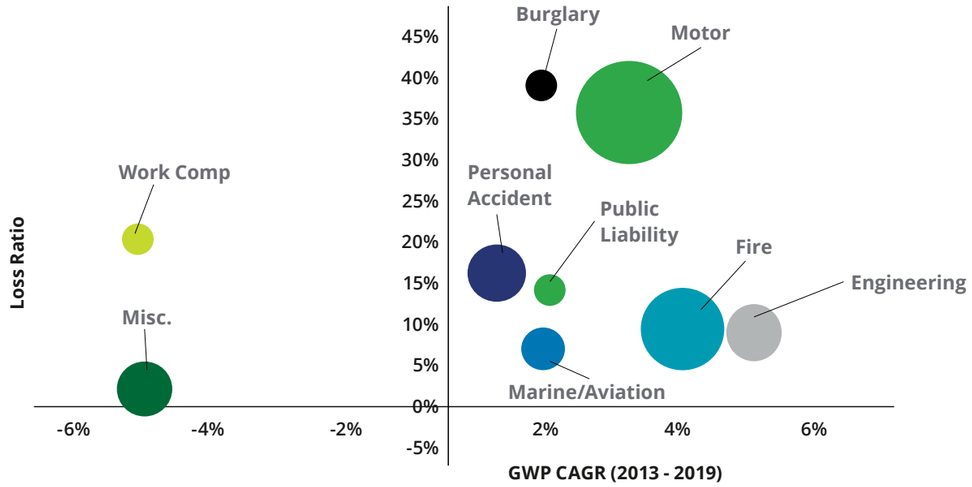
Profitability data for the year 2019 was not available. The data reflects the last 7 year's performance.

Performance of insurance classes of business

The graph below shows an analysis of insurance business classes. Their compounded growth is compared to profit margin for the year 2019. The size of the bubble represents the GWP for the year 2019.

The fastest growing business classes are engineering, fire and motor businesses as shown in the graph below. Engineering and fire have also recorded the lowest loss ratios besides being the fastest growing. Motor class of business is the largest in premium size; however is also one of the least profitable classes.

Performance based on individual business classes

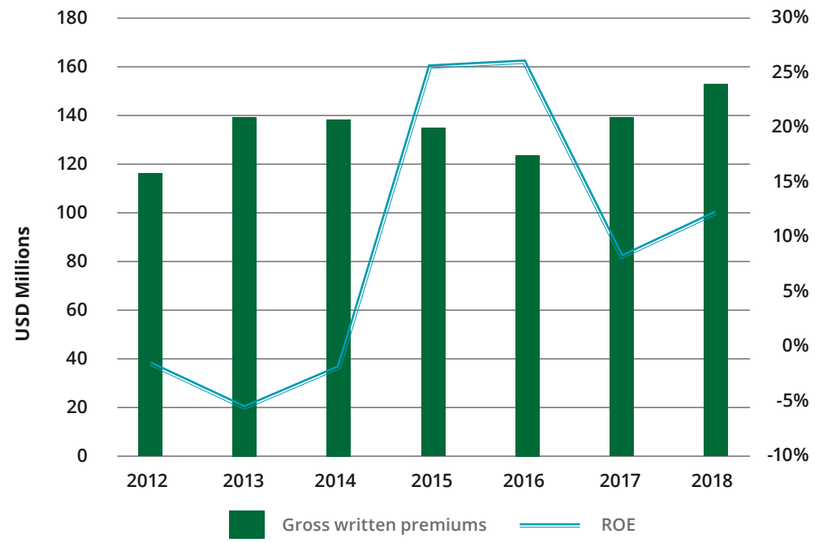


Source: IRA Uganda Industry reports 2013-2019

Insurers are experiencing diminishing returns on equity

The return on Equity has not been consistent with the increase in Gross written premiums, as shown in the graph below.

General Insurance Industry Performance (2012-2018)

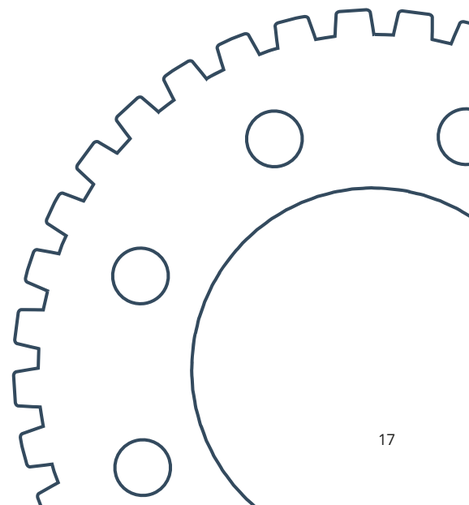


Source: IRA Uganda Industry reports 2012-2018

Profitability data for the year 2019 was not available. The data reflects the last 7 year's performance.

Motor is the largest business class (compulsory cover) and the least profitable. Fire being the fastest growing business class and has a relatively lower loss ratio.

Alternative distribution channels will be necessary for players to manage their costs as brokers and agents increasingly demand commissions.



Emerging themes in East Africa

As the industry continues to grapple with low penetration rates, obscure and complex products, a high cost of doing business as an insurer, and a slow-down in the economy due to the global pandemic, we see three key themes emerging from our analysis:

1. Customer experience

With market participants external to the insurance sector encroaching the territory of incumbents, it has never been of more urgency for insurers to start rethinking their business models to put their customers at the centre. The era of product push is far behind us, and discerning customers are looking for personalized experience that empowers them to self-manage their policies, and at the same time receive advice as and when needed.

Using big data, insurers can create hyper-personalized policies that are unique to each customer's needs. Customers are also increasingly looking to insurers as risk advisers as opposed to purely coverage providers after a risk event occurs. Globally, companies are using smart technology to step into this role and help their customers prevent risk events, reduce claim costs, and improve the overall customer experience.

Insurers must execute on a strategy that offers customers products and services that are relevant to them at a time when they need them. Incumbent insurers already have the customer base to start understanding their customers better and tailoring products to their needs, and now is the time to do so.

2. Insurance perception

The traditional approach of selling protection products will not be a marketing-beating strategy for the insurer of the future. Growth will come from new service-based models, innovative products, and a greater focus on risk prevention. Insurers must look at developing simplified products that are easy to understand and put more power in the hands of the consumer. Insurers should consider personalized policies and gamification of insurance, e.g. peer-to-peer insurance, as some of the solutions to offering simplified products that meet their customers' needs.

3. Reimagining the operating model

Insurers have long been waiting for disruption to hit their industry. Given the ever-increasing costs of providing insurance and the current economic environment, the insurers who will come out triumphant are the ones who will act on changing the status quo.

The pandemic has accelerated the rate at which disruption in the industry will occur, and this will shape the leaders and laggers of insurance in the future.

Innovation can simply not work on old legacy systems and ways of thinking. Not only do insurers need to rethink their operating models, they also need to reconsider the talent and culture of the people who will be driving the change.

To accelerate this change towards more digitally enabled and agile organizations, insurers need to consider partnering with InsurTech firms.

Enhancing customer experience

As the industry continues to grapple with low penetration rates, obscure and complex products, and the high costs of doing business as an insurer, and a slow-down in the economy due to the global pandemic, we see three key themes emerging from our analysis:

Today's insurers are being compelled by their existing and new competitors to deliver new offerings to meet consumer needs, preferences and market dynamics that continue to evolve at an accelerated rate. With other industries placing the customer at the centre of their businesses, insurers are still lagging behind with most continuing with a product-push approach.

This has given external companies an edge above insurers in the race for disruption, and it is imperative that insurers start rethinking their business model and how it addresses the needs of their customers.

Hyper-personalized policies, omni-channel experience, and the use of big data to accelerate artificial intelligence (AI)-driven product offerings are becoming increasingly popular topics in the insurance space.

Personalized policies

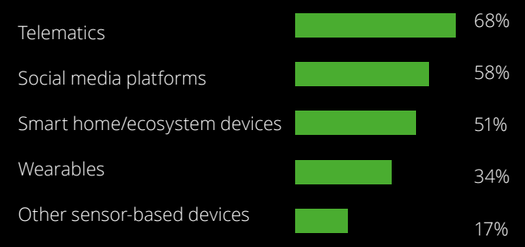
Traditional insurance is reactive – actions are mostly initiated by customers and then the insurance companies react – an approach that implies that insurers engage with their customers once a year, for a short period of time during renewal, unless there is a claim.

Start-ups are cognisant of this weakness, and are increasing their touchpoints with their customers through products such as usage-based insurance, such as "pay-as-you-use" or "pay-as-you-live".

California-based Trov offers its customers the flexibility of switching their insurance covers for gadgets on and off, as easily as they would switch their Wi-Fi connections. Not only are they increasing their engagement with the customer, they are also offering a better customer experience and collecting more data to better understand their customer behavioral patterns.

Hyper-personalized policies are possible only through the use of digital innovations to enable smart pricing and underwriting. The graph below indicates that insurers still have some ground to cover in using real-time customer data to personalize policies and almost create a customized policy that is unique to each customer.

How insurers are capturing real-time customer data



Insurers need to move away from focusing on providing a product and towards solution-based approach that meets the consumers' needs at any given point in time.

Changes in the way people live and work considering the current global pandemic, will change the way people view and need insurance.

The average household disposable income is expected to reduce because of business closures, employee salary cuts, and retrenchments. Consequently, insurers will experience decline in premium income as consumers prioritize savings-type products over risk-only products.

Customers will not be satisfied with the status quo when they only use their car for a limited time every day, or worse if they do not own a car as we see in the shared economy. They will look for better, smarter, and cheaper alternatives to the traditional annual policies. Start-ups are increasingly providing these solutions as the incumbents are slow to change.

Insurance companies need to take better ownership of the customer relationship that has been largely in the brokers' hands in this region, and start understanding their customers better.

As they work on this, there will be an increasing need to partner with companies that have already started amassing the data that is needed to enable usage-based insurance.

Digital channels

Consumers are increasingly preferring to self-manage their insurance policies online, with very few insurers having developed digital capabilities to enable this preference.

An analysis performed by Deloitte indicates that the following key themes emerged as the main issues that are challenging insurers' ability to embrace an omni-channel experience for their customers:

01. Marketing deficit: Insurers are failing to reach consumers at the right time with the right message, for example event-based marketing that is specific to an event that triggers the customer's need for insurance
02. Financial hurdles: Competition for share of wallet has been on the increase as customers look into alternative and less traditional products to cover the same risks that traditional insurance covers provide.
03. Advice compression: Given that most buyers prefer to complete the insurance-buying process without a third party such as a broker, there are less opportunities for the insurer to engage with the customer upfront
04. Digital gaps: Consumers are looking to compare different insurance options and get the best option that matches their needs, using digital channels.

Insurance companies need to start understanding when digital channels are preferred, and how these preferences are influenced by the type of insurance coverage that is required and the demographic factors of the customer.

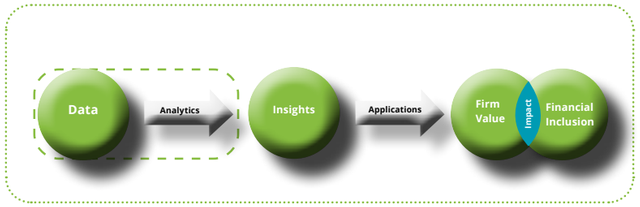
Now more than ever, it is crucial to meet the needs and preferences of the modern-day customer. This can only be done if insurers adopt bold and innovative thinking in transforming the customers' digital experience in insurance. Insurers need to partner with InsurTechs that can accelerate the pace at which digital innovation is adopted, as well as other firms such as insurance aggregators in providing platforms for transparent insurance pricing and comparison.

Big data

Insurers need to move from the traditional reactive experience to a predictive and proactive one. This new type of insurance offering is based on AI, machine learning, big data, and analytics.

These technologies play a key role in analyzing consumer needs and developing personalized products. Data collected by insurers on their customers' transactions can be used to customize insurance products, manage claims, and create an exceptional customer experience.

In the Internet of Things (IoT) space, insurers can use data from IoT devices to help policyholders prevent risk events and benefit from lower claims.



Neos uses smart devices to provide preventative home insurance. Once a smart device is installed, the policyholder receives alerts to threats that could possibly result in a claim. This enables the insured to act on the alert, prevent a claim, and the lengthy process of submitting a claim. Five percent of their customers have been alerted to a real threat and have reported to feel safer with the smart device in their homes.

John Hancock uses data generated from fitness trackers to generate a steady stream of data about buyers in return for price discounts on life insurance.

While some carriers have made headway in advanced analytics adoption, insurers should be doing more to fully harness the power of connectivity and the new data being generated by wearables and other alternative sources.

Challenges to overcome

Insurers are faced with several obstacles. The majority of insurers indicate that lack of appropriate IT infrastructure and human resources are significant inhibitors to exploring big data as a solution for their businesses. Some insurers are not aware of the potential that big data presents and how they can tap into it.

Finding a cost-efficient way of making the transition is at the forefront of insurers' concerns as the transition may require new and enhanced IT systems, and acquisition and retention of staff with both the technology and insurance knowledge, who are already in short supply.

Data protection and privacy is also a key concern as organizations need to consider the extent to which these big data projects are compliant with local and international regulations.

Where to start

Insurers should start with the data they currently possess, to start developing insights that can be passed on to the benefit of their customers. An increasing number of insurers are partnering with data aggregators such as social media channels and weather forecasters to use their data in better understanding their customers and potential pricing models that can be used from this data.

Big data is no longer an option but a necessity for insurers who want to remain competitive in the face of disruption and create a value chain that enables an enhanced customer experience.

InsurTech partnerships

Most insurers locally and globally have continued to focus on enhancing legacy systems, products, and business models, without allocating enough resources to innovations that will give them a long-term competitive edge in this customer-centric economy.

According to a study performed by Deloitte, it is estimated that less than 10% of resources that have been earmarked for innovation are going towards changing the fundamental operating dynamics of insurers, in comparison to the remaining 90% which is going toward running "business as usual", only faster, better and with cheaper solutions. With most of the innovation taking place outside of insurance companies, insurers are likely to be disrupted by external forces. Therefore, it is imperative that insurers start looking to form formidable partnerships with InsurTech firms, beyond the typical vendor one-stop shop solution provider relationships that have been the norm.

A number of barriers have been identified that inhibit insurance innovation.

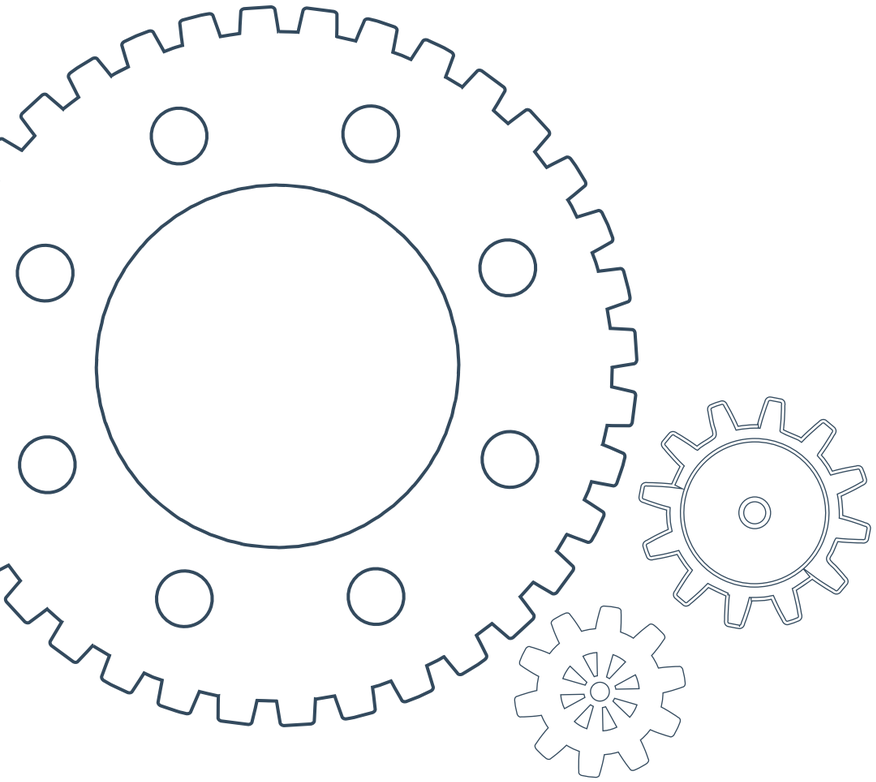
These barriers give rise to the opportunity for insurers to work hand in hand with InsurTechs to accelerate the pace at which insurers are rethinking and reshaping their customer experience, operating models and product offerings.

In this digitized space, tech companies can provide online platforms for insurers to launch their products to their digital and tech savvy consumers.

InsurTech companies are using emerging technologies to streamline insurance processes such as claims management, fraud detection, and insurance product customization.
The ability of InsurTechs to garner capital investments and develop solutions in a shorter period of time than the incumbents, are some of the positive aspects of partnering with these agile companies.

Through these partnerships, insurers would be able to accelerate their innovative ambitions without the bureaucracy and culture issues that would slowdown these initiatives if they tried to implement them on their own.
However, insurers will need to relook how they view InsurTech firms and develop ways of working with them to reimagine and implement a fundamentally different customer-centric value proposition.

Insurers should move away from viewing InsurTechs just as "technology" support firms to strategic partners that they can collaborate with or acquire in order to develop an unmatched customer experience.



Changing the perception of insurance in the region

Most insurers have struggled with innovative product solutions that meet the changing demands of their consumers. Coupled with regulatory oversight, constrained legacy systems, and long-established cultures in the workplace, this has only made it much more challenging for insurers to rise to the challenge.

There is a significant opportunity for insurers to simplify, modernize, and personalize policies, to achieve more meaningful engagement and results from the ever-discerning customer.

The lines between personal and commercial insurance are blurring out, especially in the East African region where SMEs want to receive fully-fledged packages that manage their risk exposures as a whole.

How should insurers start refining and improving their product offerings as they seek more agile ways of working and developing their operational processes?

Product simplification

This shift from offering a simple indemnity product to becoming an integral business adviser can best be achieved when the right technologies are implemented into operations.

Customers are looking to insurers to provide risk-preventative solutions as opposed to traditional risk covers. We have seen an increase in the use of smart sensors to help in preventing risk events in home-owners insurance and the use of smart plants to ensure safety of workers. The adoption of these technologies will enable insurers to use real-time data to offer transparent and simple solutions that enable their customers to better understand their risk profiles and get the best coverage for them.

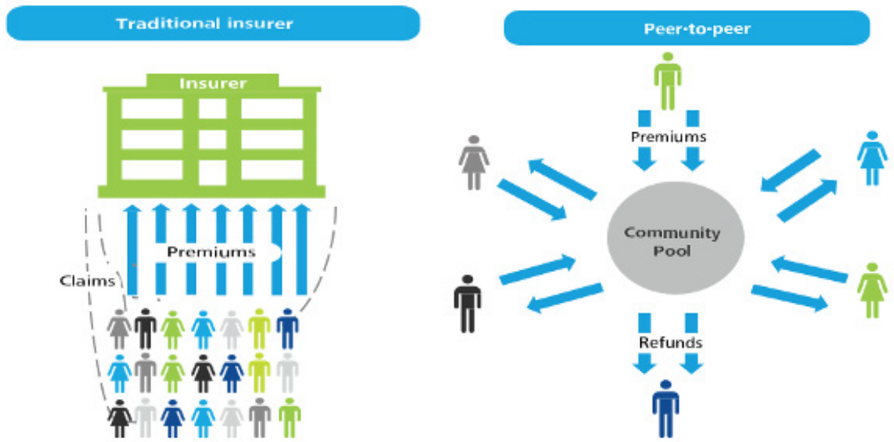
Peer-to-peer insurance

In the US property-catastrophe market, those offering alternative risk-sharing options have widened and deepened the pool of insurance capacity providers, putting tremendous downward pressure on pricing in the traditional market, squeezing profit margins, and prompting consolidation in the reinsurance sector. Such disruption could be exacerbated over the long term as securitization expands into additional lines, particularly for risks that are underinsured in the traditional market, such as cyber liability and longevity exposures in annuities.

On a more individualized basis, crowdfunding through relatively small peer-to-peer facilities could potentially disrupt insurer risk pooling in many basic lines of business (See Figure 6). The German-based Friendsurance allows people to insure one another for home contents, private liability, and legal expenses, while offering a cash-back bonus of up to 40 percent of premiums for participants who remain claimless. Another example is the UK-based Guevara, which organizes likeminded auto insureds into peer-to-peer groups.

In the East African market, peer-to-peer/ online/ mobile lending as well as the crowdfunding market has experienced a rapid growth over the years. Recently, Tala (a mobile based lending platform), reported that over three million Kenyans have used the platform to start and expand businesses, cover emergency medical bills, pay for school, and more.

Part of the new business model for peer-to-peer groups is to cut loss costs by discouraging fraud. The rationale is that small group insureds who often know one another or share an affinity group, and who are eligible for significant premium refunds based on individual and group loss history, are less likely to file fraudulent claims compared to those covered by larges and more anonymous insurers that insure millions of people but do not offer much for premium recovery, even if policyholders are loss-free.
The potential opportunity here may be quite substantial. Even if a fraction of these fraudulent outlays is eliminated in a peer-to-peer exchange, that could lower the overhead cost of insurance considerably and make such alternative risk-transfer vehicles a formidable competitor for standard insurers.



Reimagining the operating model

Digital transformation is revolutionizing different industries at a faster than anticipated pace. Despite the rapid transformations observed in other industries, insurance companies are yet to join the bandwagon. As we move into the future, insurers need to prioritize on rethinking and transforming their operating model to better serve their customers, manage their costs and leverage off technology to increase their market penetration. The pandemic has accelerated the rate at which disruption in the industry will occur, and this will shape the leaders and laggers of insurance in the future.

After long periods of working with outdated software, manual operational processes and masses of paperwork, a few insurance companies in the global scene are starting to adopt new digital technologies.

A major driver for the shift is due to changing consumer behaviors and increased competition that has resulted in the need to reduce operational costs.

The use of AI to manage the key processes in an insurance company has become a hot topic, as executives try to embed this into their digital strategy.

What digital solutions should insurers be prioritizing, as a bigger effort to transform into the digital insurer of the future?

Cloud computing

For many insurers globally, the cloud computing debate is long over. In the East African region, insurers will be forced to rethink their cloud computing capabilities especially in the current global pandemic where remote working has become the norm.

Insurance companies who want to deliver faster solutions to their clients need to place cloud computing as a high priority. As a step to transforming their operational processes and systems, insurers need to consider their options in using cloud systems to replace their legacy systems.

Not only will cloud solutions give insures more efficient processes, they will also ensure give insurers better analytics for business decision-making.

Survey data from Ovum in 2018 showed that insurers are already leveraging cloud applications for core operational activities such as claims, although there is still plenty of room for growth.

Cloud providers also seem to be actively evolving their capabilities to offer advanced solutions in partnership with system integrators to create industry-specific solutions, but these will need to be adopted within the regulatory framework.

Fraud detection and predictive fraud analytics

In the East African region, fraud continues to contribute a significant percentage towards the cost base. It is estimated that 25% of insurance industry claims cost in Kenya is fraudulently claimed.

This is a global phenomenon, and according to the Association of British insurers, in 2016 insurers detected 125,000 dishonest insurance claims valued at £1.3 billion and it is estimated that a similar amount of fraud goes undetected each year.

As such tackling insurance fraud remains a priority for insurers. It is of imperative that insurers come up with ways of early detection and prevention of fraud in order to prevent the large amounts of losses.

However there is a lot of ground work for insurers to cover in acquiring or developing solutions to successfully analyze fraudulent behavioral patterns and prevent future events from occurring.

Some methods used by insurance companies to detect fraudulent claims include;

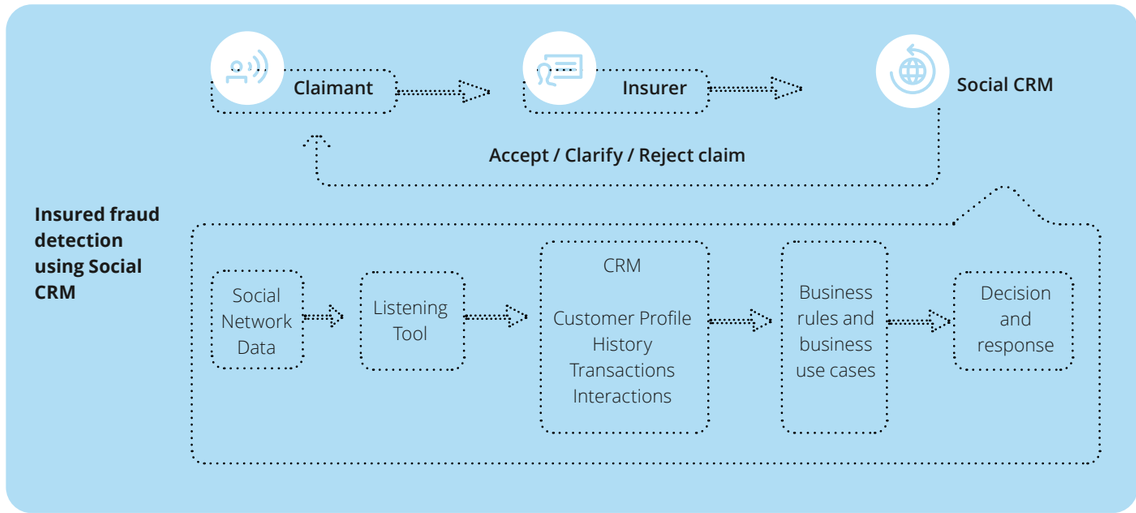
- **Use of technology**

Insurance companies can leverage technology by using data analytics where an algorithm is used to determine whether a transaction is fraudulent. For example, data mining techniques like clustering could help in classifying claims into various groups with similar characteristics. Thereafter, a different degree of attention is given to each of the groups, for example high claim frequency groups might be formed around specific addresses. The groups could also be assigned certain thresholds and an analytical tool for example Artificial Neural Networks (ANN) used to flag any claim that goes beyond the predetermined threshold. These ANN are computing systems that learn to perform tasks by analyzing examples, for example they might learn to identify a large claim by analyzing examples of large claims.

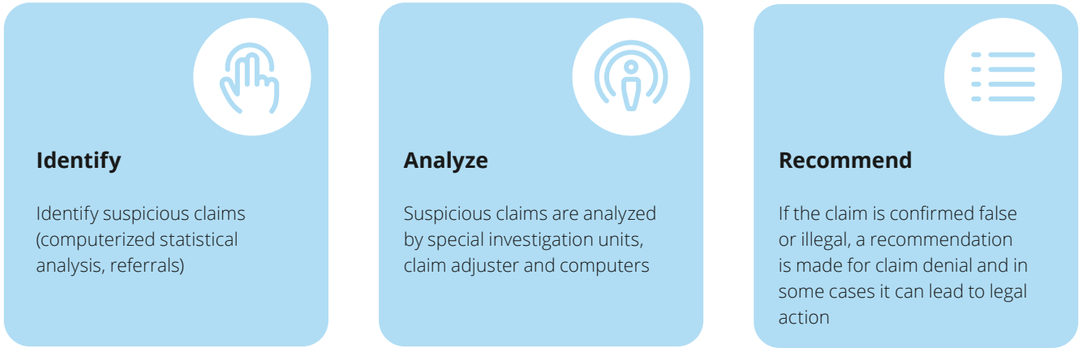
These computer software could also be used to detect suspicious billing for example in medical claims. Physicians may bill insurance companies for services that were not rendered or inflate the cost of certain services. These computer systems could be programmed to compare billed amounts with the other claim information and check whether the amount is reasonable within the said circumstances.

- **Use of social media**

Insurers are now using social media to detect suspicious claims. Social media information could also be integrated with the company's client relationship management system (CRM). The Social CRM gathers data from various social media platforms and uses a tool to extract data that is fed into a case management system. The system then analyzes the information based on the organization's business rules and sends a response.

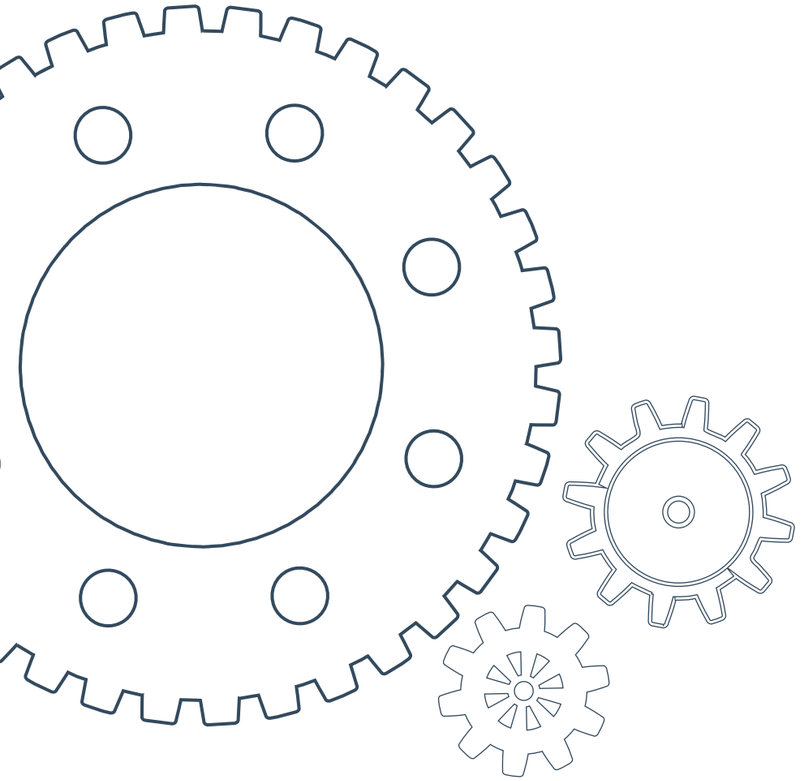


- **Data analytics**
  Traditionally, insurance companies used statistical models to identify fraudulent claims. However, these methods may lead to some frauds going undetected. The diagram below shows the three-step approach used traditionally;



- Analytics provides a better solution for fraud detection since it offers an enterprise-wide solution, it can integrate data from different sources and is able to derive value from unstructured data. In the context of insurance, unstructured data could be in the form of handwritten reports, opinions given by customers on a product or their experience after filing a claim, medical reports, and court decisions.

  Some examples of data analytics include; Social Network Analysis (SNA) and predictive analysis for big data.

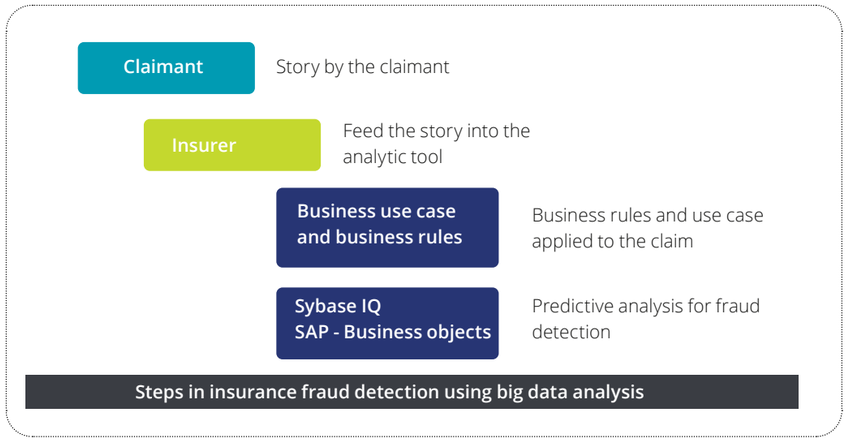


Predictive fraud analytics

Predictive analytics includes the use of text analytics and sentiment analysis to look at big data for fraud detection. When a claim is being investigated, claim adjusters write long reports with the details of how the insured event occurred. Certain clues may be hidden in the reports that may go unnoticed, however, the analytics tool that is based on business rules will be able to spot evidence of possible fraud.

Steps for implementing analytics for fraud detection

- Perform SWOT analysis: Insurance companies need to do a SWOT analysis of existing fraud detection frameworks and processes in order to identify gaps. This will help them align a fraud solution with the company's strengths and weaknesses.
- Build a dedicated fraud management team: Much like credit risk or enterprise risk, companies need to have internal staff whose priority is fraud detection and prevention. This team would be made accountable for all things related to fraud and would report to senior management.
- Whether to build or buy: Insurance companies need to determine how they want to implement analytics by assessing whether they have the right skill set to build an in-house model or if there is need to hire external consultants to implement the solutions. External consultants should be evaluated on their cost, ease of integration, ability to add new data sources, and the user interface.
- Clean data: Insurance companies need to assess the data that they have and remove any inefficiencies from the data sources. This would ensure that the analytics solution is deriving meaning from correct data.
- Come up with relevant business rules: It is important that insurance companies look into their history and experience when coming up with business rules. Some business rules may be used at an industry level to detect fraud, however, there is little impact unless they have a relation to the company's history with fraud.
- Come up with pre-determined anomaly detection thresholds: Insurance companies should provide inputs for threshold values for different anomalies, for example claim amounts. It is important that statistical analysis is carried out to determine whether the threshold is representative of the historical experience. Thresholds that are too high may result in many fraudulent claims going undetected while those that are too low will result in resources being spent where they should not.
- Use predictive modelling: Data mining tools would be employed in order to determine the likelihood that a claim is fraudulent. These tools would give a score to each of the claims and rank the claims in order of fraud propensity. The results can then be made available to management for further analysis.
- Use of SNA: SNA is effective in modelling relationships between various entities involved in the claim. For example, it can identify relationships with policyholders that have filed claims in the past or provide linkages between locations, which would be useful to assess against a pre-determined threshold for a certain location.
- Build an integrated case management system leveraging on social media: Insurance companies should capture all key findings that are relevant to an investigation. Social media carries with it a lot of information that may be useful, for example one may be able to identify the physical location of the policyholder at the time the insured event occurred or assess disability through videos and photos posted.
- Forward-looking analytics solutions: Insurance companies should continue adding new sources of data and updating their existing sources of data into their analytics solutions. This will ensure that the fraud detection system is able to address a variety of new frauds that may emerge in the future.



AI in underwriting and claims

The global insurance industry is adopting AI applications on a variety of business functions due to its access to a large volume of customer information. As a result, the industry will be highly sensitive, and particularly vulnerable, to the disruptive trends brought about by AI.

Evidently, the AI shift is resulting in far-reaching consequences, and insurers need to react accordingly:

- Customers need to be served differently. As customer demands lead to increased interactions, insurers will need to shift from transactional, low-touch customer interactions to more advisory, high-value, and high-touch customer interactions.
- Customers need to be targeted differently. Consumer data is a critical ingredient in the building of future value propositions - not just aggregated demographics or risk profiles, but highly individualized customer profiles. Insurers need to shift from offering segment-based products and promotions, to hyper-personalized offerings and engagements.
- Insurers need to play differently. Today, as most insurers are still experimenting with these technologies, they are largely viewed in isolation. However, in the future, the continued convergence of data and technologies will allow insurers to "do a lot more with less", causing a step-change in operational efficiency and customer engagement, and enabling secure data sharing at a scale that was not possible before.

While there are other areas in insurance that could benefit from AI, it is clear that claims and underwriting are the two core insurance tenets where the traction is with AI.

AI enables an insurer to define the probability of a loss occurring, and automatically compensates the policyholder if the loss occurs, therefore eliminating the exhausting claims process.

In the East African region, we have seen some companies adopting AI in managing their claims and underwriting processes. For example, regional underwriter Kenindia Assurance has invested heavily in incorporating AI into its operations to detect fraud. The insurer also uses AI to fast-track claims resolutions using anomaly detection, sentiment detection, text analytics and a self-service portal.

Jubilee Insurance in Kenya is also leveraging AI capabilities through their Digital Virtual Assistant named Julie. Clients who interact with the company's Facebook page and website, receive real-time services that include end-to-end purchase of insurance products without any human intervention.

In the global markets, companies such as Hippo Insurance provide premium quotations within 60 seconds of a policyholder submitting the relevant underwriting details online.

AI in underwriting

Historically, premiums were and still are priced based on previous experience. Technology may well be the answer to addressing these issues through dynamic pricing tools that take real-time data into consideration.

In underwriting and service management, insurance companies could leverage technology for the following uses:

- Extract insights from multiple data sources. For example, data on claims and driver behavior can be used to personalize policies each with their corresponding premiums.
- Enhance pricing, policy rating, and personalization. This knowledge helps scale insurance companies upwards by performing real-time evaluations on policies and moving towards profit-making business classes and modifying loss-making ones.

Insurance of today

Transational
It's mostly focused on tactical low touch customer interaction

Reactive
Actions are mostly initiated by customers; the insurance companies then react

Segment-based
Products, promotions and pricing are based on aggregated risk profiles

Product-based
There is a defined set of product features with standardized pricing and placement

Insurance of tomorrow

Advisory
It's mostly focused on high-value, high touch customer interactions

Proactive
Better tracking and predictive capabilities pre-empt customer actions.

Individualized
Offerings are hyper personalized and customer engagements are individualized

Solution-based
Offerings are customized based on individualized customer needs and preferences

- Automate demand analysis and generation of new product offerings. Insurers can focus on specific industries, products, and customers to provide products that meet their needs

The benefits of using AI in the above ways include:

- Efficient and lean underwriting processes: Robo-advisers streamline the process of customer interaction and data gathering, while data analytics helps insurers to make better-informed decisions.
- Improved hit and retention ratios: Owing to better insight derived from data analytics and machine learning.
- Increased risk evaluation quality: Smart technology increases not only the quantity of information that underwriters and risk managers need to make decisions, but also the quality of the decisions. Market participants with this information are better placed to be the most profitable and productive as they can capitalize on the most dynamic products before their competitors.

AI in claims management

The claims process is most often the client's second interaction with the insurer after the uptake of cover. This is a critical stage and often the insurer's reputation is imprinted by the way they handle claims.

The claims process entails reviewing immense data including but not limited to, policy reports, claim forms and statements, driver/ insurer details, and policy details and exceptions.

An AI system can scan through this data, surveyors and assessors reports and then issue a repair authority based on the estimated damage or a discharge voucher.

This data can also be run through an intelligent software that can capture anomalies and inconsistencies in the claim report thus help detect fraud.

In order to achieve efficient claims management, insurers can use the intelligent technologies in the following ways:

- Enable a real-time question-and-answer service for first notice of loss.
- Pre-assess claims and automate damage evaluation.
- Enable automated claims fraud detection using enriched data analytics.
- Predict claim volume patterns.

Cybersecurity

Raised stakes for cybersecurity

As insurers increasingly step outside their own infrastructure borders, depending on data repositories, application hosts, and external partners to conduct businesses, they may be losing a measure of control over cybersecurity as well.

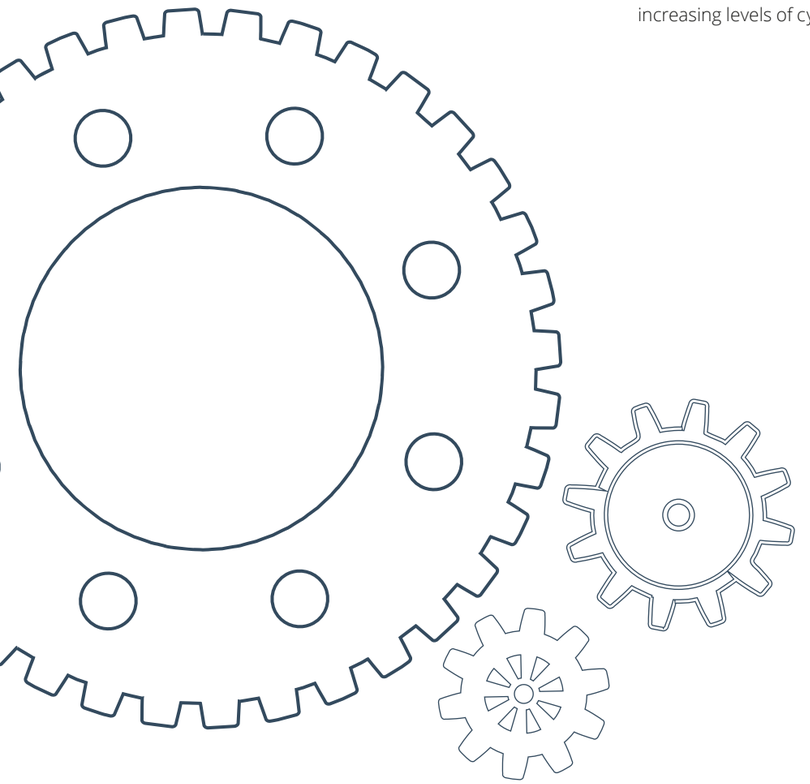
This seems especially troublesome because the human factor remains perhaps the weakest link in cyber risk management. Rather than dealing with just their own personnel - who can be directly trained, monitored, and managed - insurers often rely on individuals, platforms, and systems beyond their supervision to protect digital assets.

Cyber risks are also rising with expanded use of connected devices, forcing insurers to defend against attacks via remote sensors in smart cars, homes, wearables and commercial buildings. While these technologies help insurers better engage customers and enable new products and service capabilities, they can make it more difficult for the cybersecurity function to keep pace. Therefore, as insurers increase their business maturity with AI, they should be aware their adversaries are likely taking advantage of the same advanced technologies to discover new vulnerabilities and propagate malware to exploit them.

As we head into 2021, insurers need to consider taking the following actions about cybersecurity:

- Incorporating cybersecurity into development of new systems, applications, and products right from the start. However, they also cannot afford to neglect regular patchwork for existing infrastructure, systems, and applications, which may often go unpatched for long periods because insurers are concerned about budget or the impact on operations.
- Putting in place proper governance to ensure carriers are effectively aligning and collaborating across lines of business and operational silos. Part of that process is risk management triage-determining where the insurer's "crown jewels" reside and how such data and systems might be protected. Another key element is empowering chief information security officers (CISOs) to weigh in at the executive level about prioritization and cybersecurity strategy.
- Adopting a "cyber everywhere" mentality, in which cybersecurity is an enterprise wide responsibility and at the center of digital transformation efforts.

According to a survey conducted by Deloitte Center for Financial Services, the three distinctive traits displayed in the figure below were identified, which set more mature cyber risk management programs apart, particularly the prominent role cybersecurity should be playing in overall business strategy and its execution.



Reshaping the cybersecurity landscape

Most financial institutions have been moving steadily toward digitization for some time now. Operations across companies large or small in all financial sectors have been going digital, driven by the need for efficiency as well as rising customer expectations.

Over the last few months, the COVID-19 pandemic has forced many companies to accelerate their digitization efforts. As office closures and restricted movement compelled everyone and everything that could go virtual to do so, many institutions had to more fully embrace a digital transformation in operations, distribution, and customer engagement.

This sudden shift, however, has compounded problems for many CISOs and cybersecurity teams charged with securing the digital fortress at their firms. Hackers and cyber scammers are trying to take advantage of expanding technology footprints and new attack surfaces, with most employees working remotely. In April 2020, the New York Department of Financial Services highlighted the significant increase in cybercrime related to the COVID-19 outbreak.

The imperative is clear across the board: Organizations should be digitally enabling the cybersecurity function to keep pace with rapid IT transformation and protect critical assets against increasing levels of cyber threats and attacks.

Spending rises to meet increased demand

One of the most important components of a financial institution's cyber risk management operation is the level of resources allocated to cybersecurity programs. The average annual cost of cyberattacks has been ballooning for many organizations.

According to a survey conducted by Deloitte, the insurance sector cybersecurity spending rose in 2020 as compared to 2019. Respondents to the survey spent about 11.9% of their IT budget on cybersecurity on average, up from 9.3% a year earlier. This equalled about 0.4% of company revenue on average, again up from 0.3%.

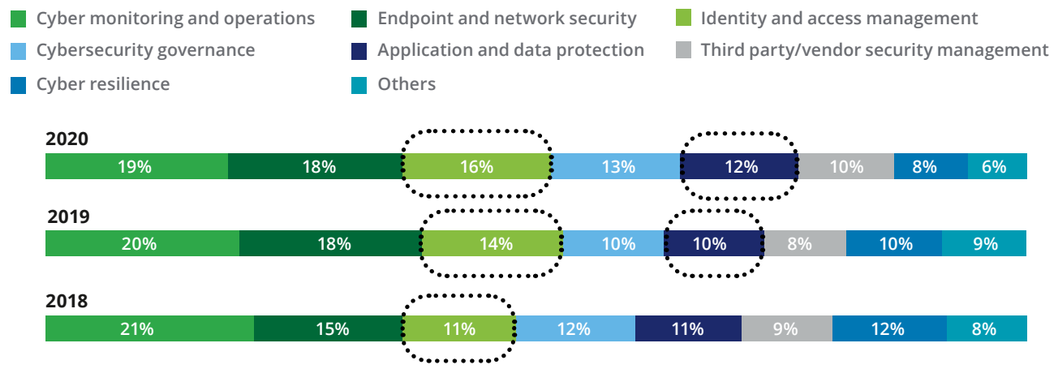
Despite increased spending, budget allocations have remained largely consistent over the three years of the survey. Cyber monitoring and operations, endpoint and network security, and identity and access management collectively received more than 50% of the spending pie (See Figure 1).

Another reason for increased cybersecurity spending is increased pressure on boards and executive management teams, which has heightened their interest in cybersecurity. According to the survey, board engagement was not limited to strategic or operational areas. Security technologies rose from number nine among respondents in our prior survey to number seven in the most recent survey, indicating that boards are becoming more interested in understanding the technical aspects of cybersecurity. Similarly, boards were more interested in reviewing roles and responsibilities of the security organization than in the past. This likely validates the growing emphasis around the notion that cybersecurity is everyone's job and not just the CISO's responsibility.

Maintaining the strategic importance of cybersecurity
Cyber threats and attacks are no longer just a technology risk, but a business risk as well. That is why the cybersecurity function should have sufficient independence and prominence. This can help ensure that decisions related to risk management are given due consideration and are not influenced or overshadowed by other IT considerations or constraints.
If cybersecurity is part of IT, it may not have enough visibility and ties to actual lines of business. At the same time, with CISOs reporting to chief information officers (CIOs), other stakeholder relationships may matter even more to balance risk and business priorities.

Companies should therefore consider specific measures to create linkages among lines of business, risk partners, and cybersecurity. This can be accomplished by creating steering committees and hiring business information security officers (BISOs). These actions could also help align cybersecurity with future business plans.

Finally, companies should work on ensuring that boards and management committees place cybersecurity high on their agendas. As noted earlier, having an engaged board can help the entire organization focus on the challenge of managing cyber risk while ensuring that adequate resources are allocated. And board oversight should be ongoing, rather than only at the initial stages or when there is a cyber-incident.



Note: Percentage totals may not equal 100% due to rounding

Source: Deloitte Center for Financial Services, "Reshaping the Cybersecurity Landscape"

Regulatory environment

In March 2020, the International Accounting Standards Board (IASB) announced the deferment of the IFRS 17 Insurance Contracts implementation for another year with an effective date of 1 January 2023.

The deferment of the Standard's implementation enables insurers worldwide to regroup and reflect on their IFRS 17 agenda. Insurers now have the opportunity to tackle the implementation of IFRS 17 over a longer period. However, insurers need more granular data and extensive calculations, going beyond the information required for current IFRS compliance.

Most insurers underestimate the effort required for the Standard's implementation. In the East African region, a large number of banks waited until the closing weeks to the deadline to implement IFRS 9, which led to a rushed and possibly inadequate execution. As a learning lesson, insurers need to start now if they are to use this IFRS not only for compliance but as an opportunity to drive better analytics and understanding of their data for decision-making.

Recognising the key drivers of the implementation journey will give insurers an indication of their IFRS 17 readiness.

Budgeting

Budgets have a significant role in determining the success or failure of a project. IFRS 17 is a budget intensive investment for the insurers, given the complexities inherent that involves people, processes, data, and systems.

Ideally, insurers spend their budgets relatively evenly between four key categories: buying and building technology solutions, engaging external consultants, expanding and upskilling internal teams, and engaging contractors for the development and implementation of technology solutions. However, the level of the overall budgets vary depending on the size of the insurer.

Learnings from the global implementations suggest that insurers locally are likely to underestimate budgets for their IFRS 17 agenda. Therefore, insurers should develop a sufficient budget by performing adequate gap assessments that provide an indication of the gaps that need to be covered to reach compliance.

Resourcing

IFRS 17 brings aboard a new corporate culture that will transform the traditional reporting language for insurers. Insurers need to ramp up their internal training efforts to ensure that critical team members are aware of the upcoming changes that are required in their systems, data, finance, and IT and operations environment.

Deloitte has developed an end-to-end online e-learning platform to support its clients in understanding the standard including key implications and business considerations. Insurance firms will need experts to document key decisions, knowledge, and capable of training and mentoring new team members as needed to keep the project on track.

Acquiring the right talent to drive the implementation agenda will facilitate a smoother transition into IFRS 17. However, insurers seeking to delay their implementation efforts will experience resourcing strains due to a shrinking talent pool.

It is also important to realise that the IFRS 17 project will not run in isolation because businesses as business as usual activities will need to continue. This poses tough decisions on how to allocate the available scarce resources and may require firms to put their best resources in implementing IFRS 17 as they look for alternative resources to handle the day-to-day activities. Generally, IFRS 17 implementation projects have taken longer than expected, and insurers who have invested in a dedicated IFRS 17 project management team have been able to complete milestones earlier than companies that do not have dedicated project managers.

Data requirements

Implementing IFRS 17 will bring significant changes to an entity's process and systems, requiring significant coordination between many functions of the business – notably between finance and actuarial. These changes can also create a fundamental shift in the way data is collected, stored and analyzed, and can significantly affect business operations, financial systems, and forecast methodologies as they adjust to the new standard.

Companies will need to come up with an efficient way to process large volumes of data, and this may require them to review and refine their data infrastructure from end to end. This will form a critical component of the IFRS 17 gap assessment with a focus on the historic data maintenance and storage, which is dependent on the retrospective reporting approach chosen by the company. Insurers can identify the current data gaps through deliberation with internal and external stakeholders.

There is no "one size fits all" solution, and each company will need to develop its unique Data Management System (DMS). Investing in a DMS is critical to a successful IFRS 17 implementation, enhancing automation and integration to work with the specific needs of the company.

The clock is ticking

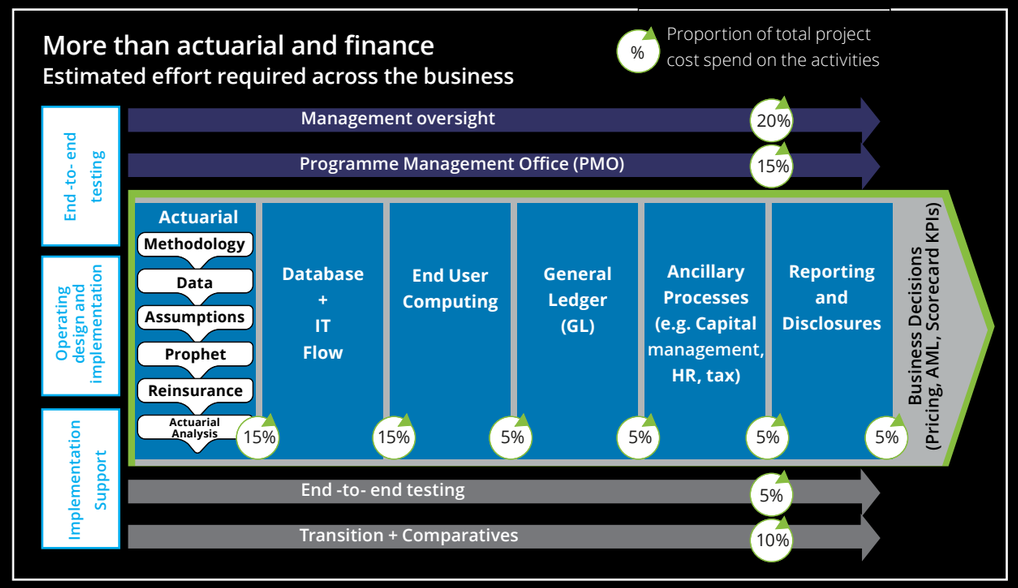
The experience from early implementations has indicated that a large number of insurers have underestimated the effort that is needed to reach full compliance. We have assisted several insurers in their readiness for the implementation phase by performing time and financial cost estimations of each sub-phase.

More than actuarial and finance

The IFRS 17 implementation program will be more than an actuarial and finance initiative. Deloitte's estimated effort required across the business, below, indicates the level of integration and collaboration required by different teams in the organization. A steering committee will be required to oversee the initiatives, ensuring the effort and cost is distributed across each of the key areas of organization as indicated in the gap and business impact assessments.

The key immediate challenges that we see our clients facing are:

- Making the standard practical through interactive learning sessions for finance and actuarial teams.
- Assessing and choosing the different design and methodology options.
- Developing a robust IFRS 17 Programme inception and management plan with limited resources.
- Freeing up business as usual team to focus on IFRS 17 implementation.



Deloitte has developed accelerator tools to assist its clients in the journey of implementation from a pragmatic standpoint:

01. Training programmes - These include an interactive e-learning platform that includes our popular T-account training, attended by individuals from finance, actuarial, and operations functions.

02. Deloitte Financial Impact Assessment tool - A tool developed in-house that can be linked to the insurer's current cash flow output to estimate the IFRS 17 balance sheet, income statement, and projected revenue profiles, including Best Estimate Liability (BEL), Risk Adjustment (RA), and Contractual Service Margin (CSM) components.

03. Deloitte gap analysis – Deloitte's gap analysis approach translates the standard into 200+ functional gaps across the insurer's financial reporting, modelling and other core capabilities. This allows translation of the standard requirements into a practical, implementable programme of work.

04. IFRS 17 project implementation plan – We have developed a pre-packaged implementation plan and detailed roadmap that covers the following key work streams: Governance, actuarial models, reporting systems, transition, and other business areas. Each work stream is subdivided into project steps that can be tailored to the insurer's specifics.

05. Methodology and design options - The IFRS 17 standard contains numerous areas of interpretation and design choices that insurers need to make. Deloitte has a comprehensive list of the key areas of interpretation and design options in the standard that we can apply to your business.

06. Prototype roll-forward engines – Deloitte has developed a suite of prototype spreadsheets that perform initial recognition and subsequent measurement computations for each of BEL, RA, CSM, and reinsurance components.

07. Deloitte T-account model – This model identifies all the necessary elements required from the modelling environment and illustrates the respective accounting entries at initial and subsequent measurement points. The T-account model can also be used to test design decisions around unit of account, income volatility, and others.

08. Insurance reporting architectural frameworks – Deloitte has developed this framework to support systems and data decisions to meet the related systems and data requirements. We are engaged with various vendors who offer commercially available technology solutions.

09. IFRS 17 disclosures - A complete set of disclosures including supplementary note has been developed and mapped to a data dictionary, showing the granular data feeds required from different finance and actuarial systems. The model disclosures can be used to understand and train your finance community and aid in the design.

With the implementation date looming, insurers need to start assessing the gaps in their current reporting infrastructure and the potential solutions that will get them to IFRS 17 compliance in the most efficient way possible.

Capital requirements and mergers and acquisition activity

Capital requirements

The Insurance Regulatory Authority of Kenya (IRA) conducted a review mid this year on companies that met the new capital requirements that were introduced in July 2020. According to IRA, out of 56 licensed insurance companies, 20 firms failed to meet the capital requirements.

The new requirement was meant to reduce cases where companies are unable to pay claims, increased the standard capital for general business from KES 300 million to KES 600 million or 20 percent of the net-earned premiums of the preceding financial year, whichever is higher. The capital for long-term business also increased from KES 150 million to KES 400 million or five percent of the liabilities for the financial year. Firms that have not met these capital requirements have up to December 2020 to shore up their capital or lose their operating licences.

IRA has been pushing for movement to the risk-based pricing regime, which will see companies adopting robust systems to measure the risks they take on and make payments on time. The risk-based pricing system is also expected to increase capacity to pay claims whenever they occur.

The mergers and acquisition (M&A) activities will certainly be affected, as the companies that have not complied with the new capital requirements are pushed to seek mergers or acquisitions in order to comply.

The same trend is likely to be experienced in the region, with regulators already expressing their intentions of moving towards risk-based capital regimes.

M&A drivers and trends

The far-reaching influence of COVID-19 has caused M&A headwinds in the form of the economy, interest rates, and financial market uncertainty. A post-pandemic world may unleash structural and systemic changes across multiple industries, and it is widely expected that recovery will be highly asymmetric across regions and sectors. Most industries, including insurance, will need to reinvent themselves in order to thrive and M&A activities are expected to have a strong influence in shaping the "next normal" environment.

Several factors have risen since the outbreak of the pandemic, which companies should consider how to respond to as they move forward with their strategic growth plans. These include:

Portfolio optimization

COVID-19 has forced many insurance carriers to hit pause on new M&A activities and focus on preserving capital. As such, this may be an optimal time for carriers to reevaluate their product and service portfolio and plot the path of greatest organic growth. However, in considering the history of a hard market, this may exist over a limited time period, so carriers should continue to strategize how to achieve profitable growth.

Insurance carriers may be forced to make strategic choices in terms of evaluating their core offerings and disposing non-core operations.

Customer experience

Due to the economic slowdown, customers may be more likely to reduce or cancel coverage. As a result, a carrier's ability to retain existing customers will be an increasingly important driver of financial results. As a result, insurers might look for consolidation opportunities in order to get back to scale quickly.

InsurTech market

As insurers move into late 2021, there may be an increase in insurance carriers acquiring and partnering with InsurTechs. This is because InsurTechs may have a greater willingness to partner or be acquired due to the uncertain economic outlook, and carriers seeking to quickly respond to a rapidly changing world (such as an increased need for virtual or touchless claims) may find InsurTech investment a more appealing allocation of capital than investing in the current low-interest-rate environment.

On the other end of the M&A spectrum, InsurTechs may become acquirers of small carriers. For example Hippo Analytics Inc., a property and casualty (P&C)-focused personal lines broker, announced on 3 June 2020, its acquisition of the carrier Spinnaker for an undisclosed sum. Another example is the workers' compensation InsurTech Pie Insurance, which raised $127 million in May 2020, in a new round; of this, $100 million was earmarked to purchase a licensed insurance company or start a new one. While these InsurTechs may decide to vertically integrate, it remains to be seen if this type of M&A will gain momentum in 2020 and 2021.

Role of private equity

Private equity investors (PEIs) are playing increasingly important roles as managers of insurance company assets, which has implications for both the insurance M&A market and the private equity fund investment space. For Life & Annuity (L&A) insurers especially, the average time period between the receipt of premiums and the payouts of claims can be many years, meaning that an insurer's profitability will be driven in large measure by its success in investing the premiums it collects. PEIs may utilize their investment expertise to mitigate the effect of low interest rates and improve net spreads. With the relatively recent success of this asset management play, whereby the PEI assumes the role of asset manager for the insurance company, it is expected that there may be an uptake in this type of relationship.

Offensive and defensive moves

Unprecedented times create opportunities—which may explain why M&A could play a critical role in post-pandemic business strategy. Yet, even as their company's business model may be changing, insurance leaders need to evaluate prospective deals based on their strategic fit, as opposed to bargain pricing. Companies can deploy a revised set of strategic choice options and scenario-planning tools to help identify the new capabilities they require and prioritize the markets where they need to operate in order to safeguard their future and drive growth (See Figure 4).

	Priority	Potential responses	M&A deal archetypes
Defensive M&A	Salvage value	Identify ways to raise capital	• Divest non-core or distressed assets • Wind down underperforming businesses
		Improve operational efficiency or increase business flexibility	• Identify rapid turnaround situations to optimize portfolio • Explore JVs and alliances with suppliers and partners
	Safeguard markets to maintain competitive parity	Adjust operating models in response to competitive dynamics	• Pursue deep synergies from recent acquisitions • Develop partnerships for non-core capabilities
		Prepare the business for the "new world order"	• Pursue co-investment opportunities for capital intensive projects • Pursue opportunistic deals to safeguard core markets
Offensive M&A	Transform the business to safeguard the future	Rebalance your portfolio	• Pursue acquisitions to facilitate vertical integration • Close gaps in portfolio through strategic acquisitions
		Capture additional revenue in adjacencies	• Acquire distressed under-performing peers and early stage companies • Acquire capabilities to accelerate digital transformation
	Change the game	Define the "new world order" through the power of networks	• Orchestrate a web of multilateral partnerships and alliances • Capture new opportunities resulting from sector convergence
		Invest to scale at the "edge"	• Acquire high-growth businesses from the innovation ecosystem • Curate a portfolio of investments on the "edge" of your core business

Moving forward in the era of COVID-19

Amidst the uncertainties and challenges brought about by the pandemic, insurers must relook their operating business model and the impact the pandemic has cast on their future.

Low insurance penetration in the region and increased claims and losses due to fraud, particularly in the motor and health businesses, have strained the industry's performance over the past few years. Although the extent of the financial impact on insurers is uncertain, societal and structural changes in the economy are expected to bring long-lasting effects to how insurance companies operate.

The new norms of work and social interactions will only accelerate the pace at which the insurance industry will be disrupted.

How should insurers respond?

In response to the changing market, insurers need to redefine their business operating models, digitalize their systems and change their market approach to become more customer centric.

Identifying ways to improve data analytics across the entire company will become relevant, not only to ensure a customer-centric approach but also to optimize operations such as underwriting and claims management.

With virtual operations and remote work becoming the new normal across the industry, special focus will be on building digitally enabled distribution models to ensure a seamless customer experience. Insurers need to reassess recruitment, workforce, workplace (physical office space), and training policies and cater to work-from-home technology needs; effectively transitioning from "return to work" towards "future of work".

Insurers will need to look to start-ups and InsurTechs that they can partner with to speed up the pace at which they develop data-based enhanced customer experience.

Understanding the evolution of the insurance industry will help insurers identify their current state and future possible outlook and take the necessary steps to achieve recovery.

Customer preferences:

Customer loyalty may be challenged as individuals are more sensitive to poor experiences and prioritize usage of funds to savings and investments. To ensure customer retention;

- Focus sales force efforts on online advisory.
- Shift focus away from capital-intensive, rate-sensitive products towards fee-based accumulation products.
- Design data-driven, customer-centric, and customized offerings, focused on overall financial wellness and life-stage needs.
- Modify underwriting guidelines to include pandemic-related exposure disclosure.

Thriving in the new "normal"

In order to thrive in the post COVID-19 environment, insurance companies need to move far more quickly to create truly digital organizations if they are to compete in a market that is set for rapid transformation.

The insurer of the future is one who is willing to critically think of how to protect their current market share and create sustainable growth.

Although the market is largely yet to face disruption, it would be against the insurers interests not to start preparing for change.

Key areas of focus going forward

Digital transformation – Insurers need to improve end-to-end process efficiencies, enable customer or agent digital capabilities, respond to changes in buying behaviors, drive new tech and data ecosystem partnerships, and adapt to changes in working models.

Product offerings – Carriers should evolve their current products and value propositions to more hyper-personalized policy types.

Customer retention – As new client acquisition becomes increasingly difficult, retention becomes the core driver for growth. Insurers need to move from product-push to a customer centric solution-based approach.

Changes in regulation – As insurers adjust with the changing times, they should also keep in mind critical Insurance regulations such as IFRS 17 that will impact their business reporting and financing framework.

Cybersecurity – Insurers need to adapt or reinvent security models to prevent fraud and phishing as digital channels increase. In addition they should also customize products that insure their clients' against the risk of cyber-crime.

Adopting a digital strategy

None of these areas can be transformed without an innovation and digital strategy that underpins the company's business model.

Therefore, insurers need to start thinking of business models that could be used to facilitate innovation across the key focus areas. Deloitte has worked with several insurers in possible business models. One of these options includes the innovation "speedboat", which runs adjacent to the main organization and is driven by a customer-centric mandate.

The business model embraced by insurance companies should encourage and motivate experimentation, "fail fast and fail early" and agile learning environments, to succeed in making innovation a strong pillar of the organization's strategy.

InsurTechs will become an increasingly important piece of the puzzle if insurers want to accelerate their growth in innovative solutions. These partnerships will be key in enabling insurers to reimagine their business operations, product offerings, and back-end processes as the insurer of the future emerges.

The insurance sector has an opportunity to capitalize on the current situation and set themselves up for success. It is crucial that insurers develop a cultural shift in thinking, which also implies that the talent and human resources driving these changes needs to be aligned with the ideal picture of the future.

Conclusion

The COVID-19 pandemic has significantly disrupted financial institutions and the ways they operate globally. Remote working and decentralized decision-making has increased significantly. Companies should digitally enable their cyber function to improve agility and ability to adapt to rapid changes in business operating models. Weaving security-by-design principles into IT service development and embedding cybersecurity requirements into the architecture and design stages of the software development life cycle could help companies get ahead of evolving threats.

While most insurers may be understandably focused on doing what they already do, only faster and cheaper, longer-term competitive threats are looming that will likely require far more differentiating innovation down the road. An increasingly aware and modernized consumer is putting pressure on the industry to customize products and services and make them available on demand, in real time, over multiple platforms.

Incremental innovations to maintain status quo systems, distribution options, and business models are not likely to suffice in the face of such dramatic changes in the society and economy. Fundamentally changing how insurers operate and provide value is becoming a make-or-break necessity. That means most insurers can no longer afford to merely dabble in innovation. They should be reimagining their value proposition to serve consumers for a very different future and start taking more substantial steps to get there before others beat them to the punch, whether from within or outside the industry.

Insurers are not victims of circumstance, or at least do not have to be. They still have time to raise their game through innovation and disrupt themselves before others disrupt or even displace them.

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Our insights can help you take advantage of change. If you're looking for fresh ideas to address your challenges, we should talk.

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