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HOW INSURERS CAN BOUNCE BACK FROM COVID-19

The COVID-19 crisis has left a deep mark on the insurance industry, with many insurers suffering a rapid 50 percent loss in market value, increased operational strain, and capital and solvency pressures. In this whitepaper, we share why the industry will never be the same again, and why the businesses that are quick to evaluate the lessons from the current crisis and implement changes now, will be able to be more successful over the longer-term.

AN INSURANCE EVENT LIKE NO OTHER

The very nature of insurance is to deal with the unpredictable, but no amount of preparation would have allowed insurers to both foresee and respond to the sheer scale and propagation of COVID-19.

As Chubb's general counsel Joe Wayland recently said, "Unlike other catastrophic events, like hurricanes or tornadoes, pandemics are not limited geographically and extend over long and uncertain time periods."[1]

Of course, the insurance industry has had to navigate epidemics and pandemics in the past; from HIV, Asian flu to Severe Acute Respiratory Syndrome (SARS), however none of these have had the widespread economic impact or business complexity as COVID-19, which has spanned all continents and countries, with no obvious end date for when the resulting losses will cease.

Every insurance customer segment has suffered, from retail customers and small to medium enterprises (SMEs), through to large and global corporates. The impact has extended to all industry segments, a broad range of insurance products, and third parties (such as brokers and managing general agents). The economic impact has been exacerbated by the hit to the investment portfolios of insurers which forms a significant component of the estimated total cost to the industry which stands at $203 billion globally.[2]

A full recovery will not be quick. Indeed, in this COVID-19 context, growth opportunities won't be available in the usual places, so new paradigms must be found, as well as insurers revisiting their budgets, implementation plans and project portfolios.

1. https://uk.news.yahoo.com/why-pandemic-insurance-is-impossible-205944685.html
2. https://www.cnbc.com/2020/05/14/lloyds-of-london-coronavirus-will-be-largest-loss-on-record-for-insurers.html

A COMPLEX GLOBAL LANDSCAPE

Insurance firms all over the world have been impacted by the pandemic, and those with a significant property and business interruption book, especially relating to SMEs, have experienced uncertainty and are under significant government, regulatory and public pressure to make payments to insureds. We've also seen legal proceedings commence against insurers, and understandably insurers want to make sure they pay valid claims, however, there is significant resistance to paying claims that were never intended to be covered and setting a precedent for the future.

Here is a selection of how the global insurance industry is being affected on different national levels:

United Kingdom: In mid-May, the Financial Conduct Authority (FCA) in the UK told insurers to halt dividend payments to allow them to pay claims. It had already told insurers it expected them to treat customers fairly[3]; however, back in March the Association of British Insurers had also warned the UK Government's Business Committee that few companies would be protected for their losses by their insurance policies.[4] On 1st June 2020, the Financial Conduct Authority (FCA) stated it will progress a test case to provide guidance for the interpretation of business insurance policies.[5]

United States: Across the Atlantic, in late March, President Donald Trump told a briefing with the Business Interruption Group (BIG), a recently formed non-profit aimed at pushing for insurance payouts, "When they [businesses] finally need it, the insurance company says, 'We're not going to give it.' We can't let that happen."[6] While this statement was not legally binding, eight U.S. states have now introduced legislation that would require insurers to pay claims, despite exclusions. Many of the bills would let insurers seek reimbursement from the states, however.[7]

Canada: In April, a class action lawsuit in Quebec and Saskatchewan was filed against a leading indemnity insurer for breach of contract in their refusal to pay business interruption claims from the COVID-19 crisis.[8]

France: In April, President Emmanuel Macron said that insurers "must be there" to help stabilize the economy. The Federation Francaise de l'Assurance meanwhile said "almost all" commercial insurance policies exclude claims due to epidemics. However, French insurers are reportedly in talks with the government to find new solutions to support the corporate sector and donating 3.2 billion euros to the government's business aid fund.[9]

China: In mid-April, Fitch Ratings reported that the recent launch at the direction of the Chinese government of insurance policies to cover Chinese enterprises against losses due to business interruption from the coronavirus outbreak could pose risks to the underwriting stability of property insurers.[10]

3. https://www.theguardian.com/business/2020/apr/12/uk-insurers-face-legal-action-from-small-firms-over-covid-19-claims
4. https://www.insuranceage.co.uk/insurer/7503051/covid-19-abi-admits-few-will-be-covered-for-bi
5. https://www.fca.org.uk/news/press-releases/update-fca-test-case-validity-business-interruption-claims
6. https://www.ft.com/content/025a7f41-d05c-4fbd-afb0-825c50215b42
7. https://www.insurancejournal.com/news/international/2020/04/28/566595.htm
8. https://www.insurancejournal.com/news/international/2020/04/06/563476.htm
9. https://www.insurancejournal.com/news/international/2020/03/20/561842.htm
10. https://www.fitchratings.com/research/insurance/business-interruption-insurance-poses-new-risks-to-chinese-insurers-16-04-2020

DAY-TO-DAY CHALLENGES

Aside from external pressures facing insurance firms, the enormity and unprecedented impact of COVID-19 has operationally challenged firms, including the effectiveness of business continuity plans that have previously been signed off. The operational challenges that insurers have faced include:

- Complete closure of all office and site locations across the world, with no available and viable back-up location, which has resulted in the immediate working from home for all employees

- Increased infrastructure and data security concerns due to the remote working of employees, including an initial insufficient availability of laptops and VPN connections, and an increased level of phishing attacks

- Servicing of new business and renewals has often relied heavily on agents and human interaction, as a result many insurers had to temporarily pause new business and automatically extend policies due to the limited availability of call centre employees

- Significantly increased interaction with policyholders and agents who have had queries on policy wordings, sought to notify of a claims event, or register a complaint about service or the denial of coverage

- Inevitable reduction in productivity, many employees have endured longer working days however it has often been combined with managing domestic situations and 'firefighting' at work, this has been exacerbated by a reduction in productive capacity due to furlough arrangements; and

- Managing outsourced relationships, with the outsourcing provider often struggling under their own operational constraints and unable to meet their contractual service level agreements.

Despite these challenges, it is encouraging that insurers, brokers and agents have continued to operate during the crisis, and inevitably there will be many lessons learned that will need to be incorporated into operational resiliency plans in the coming months.

FINANCIAL LOSS

It is the financial loss for the industry that many are obviously focussing on right now. While it is still early days, we have seen a number of industry loss estimates being published, as well as individual insurers outlining their initial financial loss for COVID-19 as part of their quarterly earnings announcements.

Here's what we have learned to date:

- High volatility in both equity and fixed income markets, resulting in realised and unrealised losses, has eroded balance sheets, and compounded the losses on the liability side of the balance sheet

- Solvency ratios have reduced due to both a reduction in asset values and an increase in insurance liabilities

- Rating agencies have warned that downgrades could occur which in turn will reduce choice for corporate risk managers operating in-line with tightly defined security parameters and an increase in borrowing costs for some insurers

- Capital raising will be required, some insurers have already tapped the markets to raise equity to take advantage of a favourable rise in insurance rates, and it's expected more will raise capital to address solvency concerns and fund future growth initiatives.

Income, cost and profitability challenges are inevitable, with 2020 budgets being re-forecast and companies re-modelling their five-year plans including targets for subsequent discussion with investors.

HOW SHOULD INSURERS RESPOND?

We believe that insurers will need to focus on three areas: (1) their strategy and business model (2) operating model and digitization and (3) financial and risk management including the regulatory impact from the crisis. Leading insurers will learn from their experiences to date and take heed from the evolving world around them.

1. STRATEGY & BUSINESS MODELS

Strategy functions across the industry will be busy working with their board and executive committees to understand how their organization's strategy needs to evolve. The following initiatives should form a significant part of any business strategy refresh.

Create pandemic pools (backed by governments)

This will help ensure that individuals and companies benefit from a risk transfer solution that allows them to manage through any new pandemic event. It will require insurers, reinsurers, regulators and governments, to collaborate and create a pandemic pool, and for wording, process and system changes to be implemented. In the UK, a Pandemic Resteering Committee has been formed and six working groups mobilized, with the project collaborating with Pool Re, in order to develop a strategic response for the industry.[11]

Invest in e-trading platforms

New e-trading strategies will need to be developed with investment prioritised. The biggest barrier to e-trading has been cultural, with the excuse of complexity often cited. However, UK government restrictions in light of COVID-19 such as social distancing, have forced underwriters and brokers to adopt e-trading to ensure renewals have been completed, and the feedback from the crucial 1/4 renewal date has been positive. Many insurers have experience of extranets and software house solutions; however, innovative insurers have adopted new platforms such as Whitespace to write complex subscription / co-insurance business. Even the complex (re)insurance market has seen an adoption of e-trading solutions, with Aon seeing an increase in use of its ABConnect platform and receiving accreditation for Lloyd's electronic placing mandate for end-to-end processing back in April.[12] New capabilities have been implemented, such as video booths with features to schedule slots and chat with brokers face-to-face.[13]

Form new revenue streams

These will offset any decline in gross written premiums that will result from an economic recession. We see opportunity for new innovative products to be created that close the protection gap, new distribution channels being accessed to increase insurance penetration, and new services being launched. However, this will require partnerships, a change in culture, design-led thinking, and addressing legacy technology challenges by using new technologies including SaaS platforms, microservices and APIs.

Insurers are already showcasing just how interesting and innovative collaborations in and out of the sector can be.

Last year, Chubb and ZhongAn together launched income loss and protection products on Grab, a ride hailing service similar to Uber. Grab sees itself as a platform, and the platform has a loyal following, therefore users of the platform will be able to buy insurance on the platform, even when they are sitting in the back of a taxi.[14]

Ping An, the world's largest insurer, is committed to spending $22 billion on new technology such as AI and blockchain in order to offer comprehensive insurance products including related services, and a best-in-class customer experience.[15] The insurer is so confident in its approach that it has publicly stated that the technologies it develops using its considerable investment will be available for licence by western Insurers who are seen more as followers.

The large tech titans, who have ambitions on large markets, have indicated that insurance is indeed ripe for disruption. With Google, Apple, Microsoft and Facebook reportedly targeting the health industry[16], we can construe that this focus area can easily be extended to insurance solutions too. Meanwhile car maker Rivian reportedly has plans to offer its drivers insurance products that it underwrites itself like Tesla[17], and Amazon already provides significant financing to SMEs that use its platform, and it will not take much to extend to insurance for SMEs.

11. https://www.reuters.com/article/us-health-coronavirus-britain-insurance/uk-insurance-industry-working-with-pool-re-to-develop-pandemic-cover-idUSKCN223191
12. https://www.insurancejournal.com/news/international/2020/04/22/565764.htm
13. https://www.whitespace.co.uk/
14. https://www.global-benefits-vision.com/singapores-grab-enters-insurance-market-with-chubb-and-zhong-an/
15. https://www.insurancejournal.com/news/international/2019/10/24/546474.htm
16. https://www.mobihealthnews.com/news/new-cb-insights-reports-says-facebook-could-be-digital-entry-point-health-future
17. https://www.cnet.com/roadshow/news/tesla-rivian-insurance-program-collision/

Re-build relationships with small to medium enterprises

Many have suffered extensively, and it's important that insurers launch initiatives that actively regain the trust of these vital businesses so that they can continue to thrive and spearhead future economic growth. In May, it was heartening to read that the COVID-19 Support Fund, which is supported by insurers including the ABI, BIBA, Lloyd's and the London Market Group, has so far raised £82.5 million for charities affected by the pandemic.[18]

2. OPERATING MODEL AND DIGITIZATION

The operational strain that has been experienced in light of COVID-19 has outlined a number of opportunities for improvements within organizations; these include operating models, outsourcing arrangements, automation and other digital transformation tools.

Optimize the current operating model

It is likely that the economic consequences of COVID-19 are going to persist far longer than the hoped for 'V shaped' recovery.[19] This means that the profitability of insurers is likely to be pressured for the foreseeable future. The current crisis emphasizes that the considerable fixed cost base of the industry needs to become more variable in order to deal with the economic shocks that are inevitable in the globally connected and complex world of today.

Insurers therefore need to review their end-to-end customer journeys and identify opportunities to transform the underlying cost base without compromising the customer experience, with the objective to have a cost basis that is variable based on the level of premiums written by the organization.

Strengthen third-party agent servicing performance

Insurers should conduct a detailed review of how outsourcing providers (underwriting, claims, operations, technology, etc.) have performed during the current crisis, form recommendations for discussions, and implement changes which may include increased automation, re-thinking sourcing strategies and formalising new performance requirements.

Accelerate the shift to digital servicing channels

Central to any automation strategy is the digitising of information. Insurers are notorious for capturing information in an unstructured data format e.g. medical records, Lloyd's market slip etc. There is an abundance of new technologies to automate the end-to-end policyholder experience. These technologies include optical character recognition (OCR), digital workers (RPA), chatbots, next generation portals, and machine learning and artificial intelligence. It's important to use the current crisis to identify new use cases that have emerged that can benefit from digital servicing. For example, increased segmentation of underwriting and claims interactions that can result in a higher throughput for digital workers to process.

We've seen this approach work recently in parts of Asia - the first continent to succumb to coronavirus – insurers are being particularly innovative in light of social distancing measures. For example, in Singapore, AIG have been adopting the use of video to communicate with policyholders and telehealth solution

18. https://www.insurancetimes.co.uk/news/aviva-and-zurich-uk-among-insurers-contributing-to-new-industry-wide-coronavirus-support-fund/1433433.article
19. https://www.weforum.org/agenda/2020/05/z-u-or-nike-swoosh-what-shape-will-our-covid-19-recovery-take/
20. https://www.aseantoday.com/2020/05/covid-19-pushes-healthcare-technology-transformation-in-asia/
21. https://www.asiainsurancereview.com/News/View-NewsLetter-Article/id/50012/Type/eDaily/Etiqa-introduces-new-video-claims-service-for-motor-policyholders

provider DoctorAnywhere to help doctors remotely assess the health of their patients suffering from coronavirus symptoms.[20] Meanwhile in Malaysia, Etiqa launched a new video-assisted claim service that enables the insurer's motor surveyor to interact with the claimant or work directly and remotely via an audio or video call.[21]

Embrace distributed remote working at scale

So far, insurers and brokers have done a phenomenal job in adapting to remote working in a very short space of time. Inevitably, there have been issues, including backlogs, shortened hours for contact centres, a lack of clarity on who is responsible for servicing (e.g. agent, broker or insurer), however, COVID-19 has been an excellent global use-case for remote-working and proven that distributed working at scale is possible. After all, the 'new normal' will evidently be with most of us for many more weeks - and potentially months - to come, and insurers must prepare accordingly.

The industry has suffered from a presenteeism culture and the evidence is that distributed teams do work effectively, however, this requires the adoption of new ways of working based on agile principles[22], and teams benefitting from the roll out of collaboration tools.

Technology firms are typically at the forefront of change. After two months of lockdown, Shopify, Twitter, Square and Facebook are offering the choice of remote-working permanently, and this sentiment has been mirrored by other firms for at least the end of 2020.[23] Given the ongoing war for talent, and insurers increasingly competing for technology and data resources, it is likely that they will have to offer the same flexibility as other industries, and the recent experience shows that working from home is possible even for front-office employees.

3. FINANCIAL & RISK MANAGEMENT, AND REGULATORY IMPACTS

The effects of COVID-19 on the insurance industry have been far-reaching, highlighting improvement opportunities in firms' risk and data management processes that require action but should enable significant benefits over the longer term.

Reduce policy coverage ambiguity

Regulatory intervention may require insurers to do this, however, proactive insurers should seek ways to easily communicate the implication of wordings, for example through gameification or video. Insurers can learn from digital financial services providers such as Monzo, who pride themselves on 'solving problems, rather than selling financial products' and offer a transparent customer-provider relationship and onboarding process, including easy-to-understand terms and conditions (T&Cs), which they even rally for on their website.[24] Furthermore, with website browser add-ons like Terms of Service; Didn't Read[25], whose software breaks down the jargon of T&Cs for popular apps, it's just a matter of time before we see more sophisticated tools integrated into insurance price comparison websites for individual policies.

Timely exposure management data

This has always been a challenge for insurers with sizeable exposures strewn across the world and often moving. Telematics

22. https://www.capco.com/Intelligence/Capco-Intelligence/The-secret-sauce-of-the-scaled-Agile-framework
23. https://edition.cnn.com/2020/05/22/tech/work-from-home-companies/index.html
24. https://monzo.com/blog/2019/05/03/writing-clear-terms-and-conditions
25. https://tosdr.org/

and the internet of things provides a significant opportunity for insurers to utilize technology embedded in assets for real-time tracking, this will require insurers to re-think their data strategy and understand how they will ingest this information real-time and deploy data science to develop meaningful insights for decision making.

Re-evaluate the approach to global operational resiliency

COVID-19 has shown how previously 'unthinkable' scenarios must be considered and planned for. While it is supposedly impossible to predict 'black swans' such as the coronavirus pandemic, organizations now have the hindsight of what protocols need to be in place to maintain a reasonable level of business continuity during a global shut down.

CONCLUSION

The insurance industry may be facing its largest loss in its 300-year history. However, it has always demonstrated that it is resilient and there is nothing to suggest that this time will be different. Given the level of public interest in seeing reparations, it is important that the industry manages its reputation and is sympathetic to the needs of its policyholders, by ensuring that appropriate effective risk transfer mechanisms continue to exist beyond COVID-19. But this will only go so far – insurers must also make themselves more responsive to disruption in the future by diversifying into new products and services, and investing in technologies that automate and provide a better customer experience, whilst improving the bottom line.

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ABOUT CAPCO

Capco is a global technology and management consultancy dedicated to the financial services industry. Our professionals combine innovative thinking with unrivalled industry knowledge to offer our clients consulting expertise, complex technology and package integration, transformation delivery, and managed services, to move their organizations forward.

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