Clyde & Co

Searching for growth

M&A and other strategies

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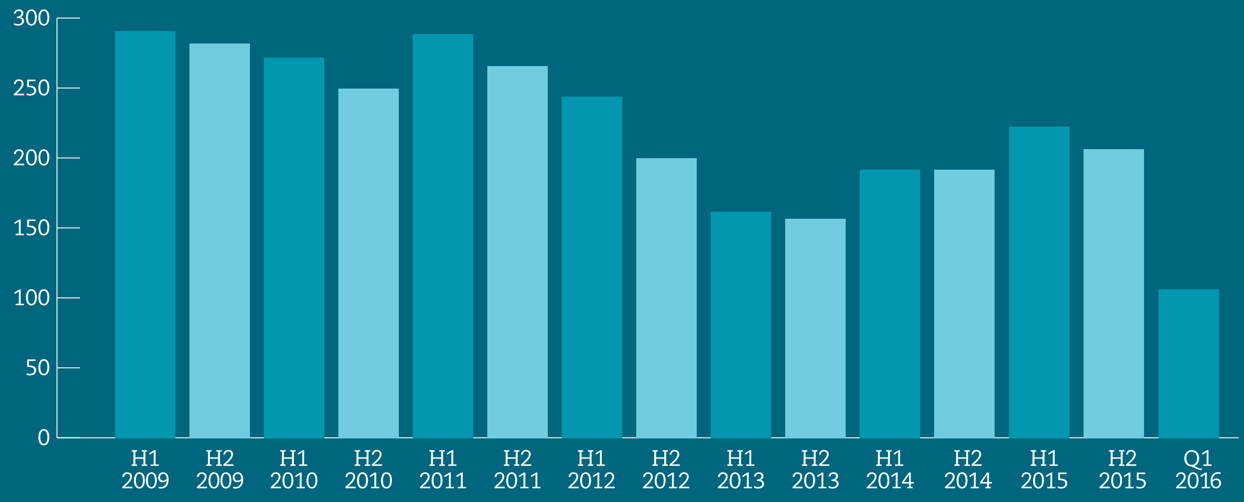
Introduction

The insurance industry faces some of the most testing market conditions since the turn of the 21st century – impacting brokers and carriers wherever they are located. Interest rates remain low, albeit with some possible upward adjustment in the US, while levels of competition in the market are keeping premium levels depressed – a fact exacerbated by the inflow of alternative capital into the reinsurance market. The recent vote by the UK to leave the European Union also means that that, in this region, there will be a sustained period of uncertainty. With thin investment returns, insurance businesses are having to focus very keenly on their underwriting results, and on strategies to reassure investors that that there will be sufficient returns on equity.

Almost every public statement from carriers and brokers alike talks about their search for growth, so we decided to use our annual report to examine this trend. M&A as a route to growth has certainly seen considerable popularity as a strategy in the last several years – "achieving scale" has been quoted by many a CEO. Market executives have been deploying excess capital, and the ability to borrow cheaply, to look for inorganic growth – seeking out deal activity that can deliver consolidation, diversification and geographic reach.

Although 2016 has not yet seen the announcements of any of the mega-mergers that typified the deal landscape last year, there is no doubt that general M&A activity was buoyant in the last nine months and, with no change in insurance market conditions forecast, few businesses would rule out some transactional activity in the next year.

Volume of insurance deals completed globally: January 2009 – March 2016



The appeal of M&A in achieving scale has clear advantages, but the challenges of finding a suitable target and, significantly, at a suitable price, may cause insurance businesses to consider more organic routes to growth, depending on location and the characteristics of the market.

Over the last several years we have seen a desire to enter new markets through the establishment of a branch or subsidiary. South East Asia is a particular example of this trend, where low insurance penetration rates present an attractive proposition for insurers in mature markets experiencing modest growth levels. However, many jurisdictions in the region are characterised by a lack of obvious or appealing targets. Singapore is one such market where we have seen a significant uptick in interest from international re/insurers looking to set up shop and establish a base for wider access to markets across the region. In another example, Miami is emerging as a regional hub for Latin American and Caribbean re/insurance business – attracting a number of international players who are drawn by its deep connections with and accessibility to the wider region.

Joint ventures (JV) with a local partner have long been a popular route to growth, especially in countries where there are limitations on the level of foreign participation. Overseas investors in the past have been prepared to take minority positions in a JV as a means of establishing a foothold in the market with the expectation that they would be able to build out their position at a later date. In some significant markets, such as China and India, the foreign direct investment limits have been raised and, as a result, there has been considerable activity in the last year by international insurance businesses to increase their shareholdings.

Lloyd's of London also offers joint venture possibilities, which are seen as an increasingly attractive way to enter a market that has a decreasing number of acquisition targets. Last year Beazley and Korean Re established a special purpose syndicate (SPS) at Lloyd's, which is supported by a two-way programme of reinsurance as well as employee secondment. Another recent example was Patria Re of Mexico teaming up with Pembroke. We expect this to be a continuing trend.

The other development we have seen this year is that, in response to the on-going difficult trading conditions, a number of larger insurers have taken a long-term bet to deploy venture capital into technology start-ups around the world. According to recent data from Accenture, insurance technology start-ups attracted USD 2.6 billion of investment in 2015, up sharply from USD 800 million the year before.

By expanding the scope of this report to go beyond M&A, we have explored some interesting trends in how insurance businesses are seeking expansion. With market conditions not expected to improve in the foreseeable future, there can be little doubt that we will see more businesses looking for creative answers to the issues they face in the next few years.

Andrew Holderness
Global Head of Corporate Insurance

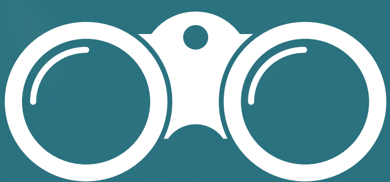
Top ten facts

Consolidation, disposal & entering new markets = key drivers of M&A activity

8 of the **Top 10** deals in H2 2015 involved Asia insurers

1 in 5 P&C insurers have yet to apply big data advanced analytics to any function

50 percent Maximum stake international partners can now take in Chinese JVs since April 2015, up from 25%



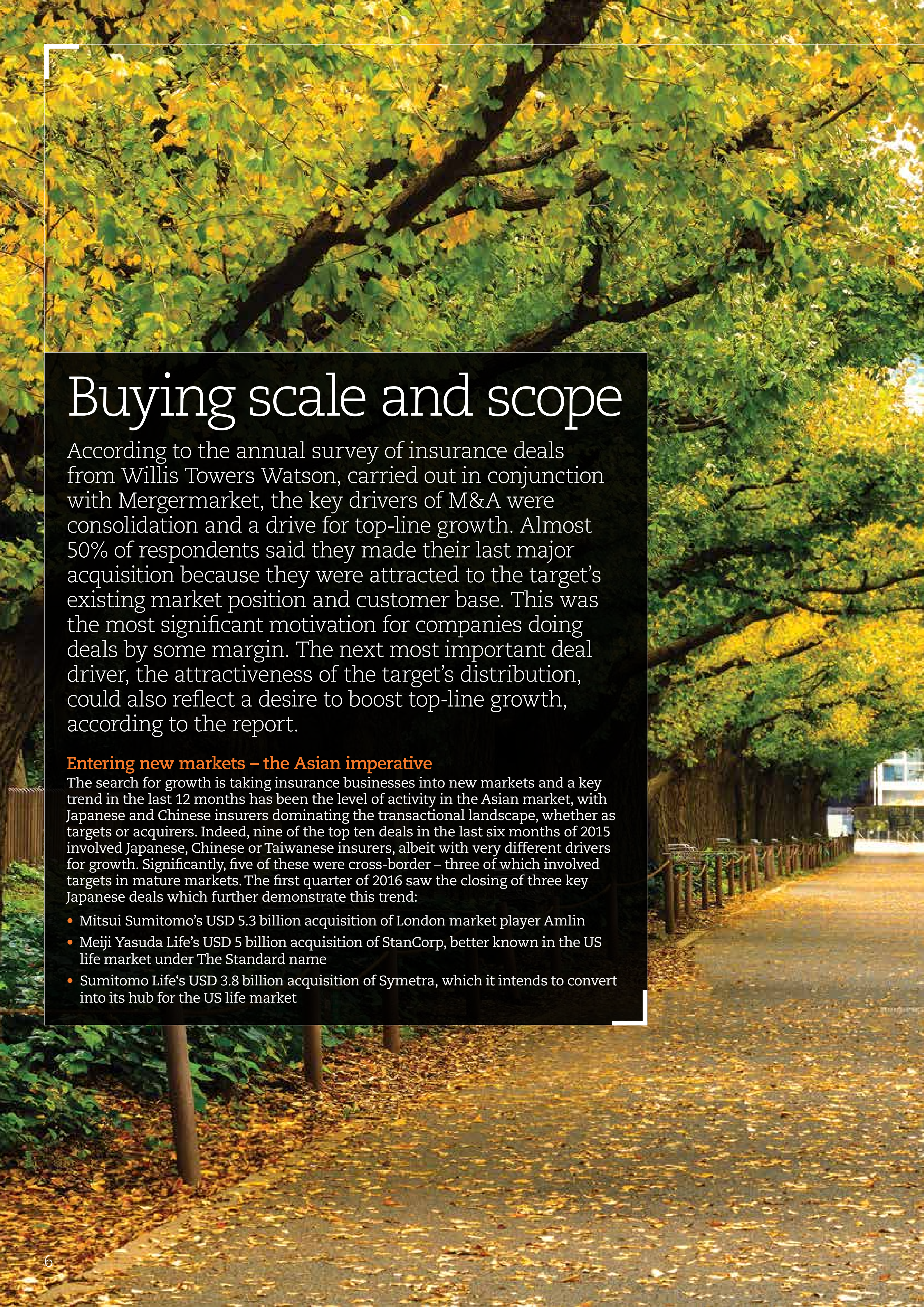
The sharing economy will generate **USD 335 bn** in global revenue by 2025

14 Number of **completed deals**
in Q1 2016 with a value over USD 1 bn

Insurance penetration rates in SE Asia are **half** the global average

444
Number of deals **worldwide** in 2015 – highest level since 2012

USD 2.6 bn
invested in insurance technology start-ups in 2015, up sharply from USD 800 m the year before



Buying scale and scope

According to the annual survey of insurance deals from Willis Towers Watson, carried out in conjunction with Mergermarket, the key drivers of M&A were consolidation and a drive for top-line growth. Almost 50% of respondents said they made their last major acquisition because they were attracted to the target's existing market position and customer base. This was the most significant motivation for companies doing deals by some margin. The next most important deal driver, the attractiveness of the target's distribution, could also reflect a desire to boost top-line growth, according to the report.

Entering new markets – the Asian imperative

The search for growth is taking insurance businesses into new markets and a key trend in the last 12 months has been the level of activity in the Asian market, with Japanese and Chinese insurers dominating the transactional landscape, whether as targets or acquirers. Indeed, nine of the top ten deals in the last six months of 2015 involved Japanese, Chinese or Taiwanese insurers, albeit with very different drivers for growth. Significantly, five of these were cross-border – three of which involved targets in mature markets. The first quarter of 2016 saw the closing of three key Japanese deals which further demonstrate this trend:

- Mitsui Sumitomo's USD 5.3 billion acquisition of London market player Amlin
- Meiji Yasuda Life's USD 5 billion acquisition of StanCorp, better known in the US life market under The Standard name
- Sumitomo Life's USD 3.8 billion acquisition of Symetra, which it intends to convert into its hub for the US life market

> Although the USA is not a high growth market like emerging economies, it remains the largest insurance market in the world offering solid business opportunities and a range of targets for potential acquirers as well as the opportunity to increase market share for existing players. This, combined with an increasingly robust economy, means that the conditions for insurance deal-making in the USA will persist for the near-term.
>
> **Vikram Sidhu, Partner, New York**

In 2015, the Chinese insurance market grew by

20%

The motivation for these deals is clear. More than a quarter of Japan's population is aged over 65 and its birth rate is among the lowest in the OECD. The Japanese insurance industry has been one of the first to feel the full impact of this demographic shift, which is why it has been a very active purchaser of overseas assets. There is also a sense that Japanese insurers are using overseas M&A to secure their position so that they do not become targets themselves.

These acquisitions are typical of the Japanese strategy – identify the right target and then commit sufficient capital to secure it, often paying what is seen as a high price. For example, Mitsui Sumitomo's offer for Amlin was 2.4 times book value, which was perceived as a generous multiple. Even with these deals, it is likely that Japanese insurers will continue to be on the acquisition trail to achieve their stated targets for international businesses over the next few years.

The fact that the Japanese have been keen acquirers of Lloyd's businesses in recent years – Tokio Marine and Sompo have both bought Lloyd's managing agents – illustrates the continuing attraction of a platform that gives immediate global reach as well as having a sizeable presence in US speciality markets. Conversely, other Japanese insurers are cementing their position at home before looking internationally. For example, Nippon Life spent USD 2.3 billion to purchase Mitsui Life, increasing the size of its domestic sales base as Japan's population shrinks.

Activity in China has also been lively. As with Japan, recent deals have been mostly outbound, with major Chinese acquirers such as Fosun and Anbang targeting developed markets for expansion through takeovers. In April 2016, Anbang agreed to take over the life insurance and investment operations of Allianz in South Korea to add to its purchase of Tong Yang Life. It also looked to Europe with its acquisition of Vivat in the Netherlands. Fosun committed more than USD 2.7 billion to insurance acquisitions last year and promised more activity, although we expect these 'ad hoc' acquisitions by non-insurance groups to draw to a close with traditional insurers instead picking up the baton and increasing their outbound investment through M&A.

According to Chinese rating agency, Dagong, there are several reasons behind these developments. The first is that Chinese insurers need to expand their technical expertise and diversify their assets from a "relatively shallow and volatile domestic financial market". With the local economy already cooling down, opportunities in foreign markets become more attractive. Secondly, the government is also encouraging a more global outlook – regulatory changes now allow companies to invest up to 15% of their entire assets internationally, translating to a maximum total of USD 202 billion.

The last year has seen some activity from foreign participants looking to enter or increase their participation in the Chinese market, some of whom have started preparatory work for applying for reinsurance licences, including setting up representative offices, underlining the fact that China is a highly attractive investment destination. Although it is already the world's third-largest insurance market, the Chinese market grew 20% in 2015 and its strong savings culture and the rise of the middle class will clearly drive further demand for both life and non-life protection.

> Activity in China has been lively, reflecting the country's dynamic expansion, and has seen domestic and foreign interests look to develop their position in an insurance market offering great potential.
>
> **Carrie Yang, Partner, Shanghai**

However, the last four months have seen the biggest upsurge in interest ever from domestic and foreign participants in M&A in China. While there does not seem to be one definitive cause, it would appear that factors include a combination of changes in regulatory landscape; foreign players deciding that it is now or never to enter the market; and a renewed interest from investors with an existing involvement in the Chinese market. The result is a strong sense of anticipation for lots of M&A activity to come. Markel International president, William Stovin, articulated this trend when he said that China had to be viewed as a long-term business opportunity. "You are in China now to be there in years to come. If you don't put roots down now you will miss the boat," he said.

Looking over new horizons

According to Willis Towers Watson, relatively few takeovers take place in markets that are completely new to acquirers. Nevertheless, the search for growth does mean that a wider range of strategies are being deployed to give insurers some foothold in a range of developing markets. Latin America has been just such a region, with a robust stream of activity by the international re/insurance industry. Major players in the primary insurance market are Zurich, which has an important distribution arrangement with Santander, and Mapfre. Last year Ace Group (now Chubb) became one of Latin America's largest commercial property/casualty insurers after acquiring Itaú Unibanco's corporate insurance business. Until about two years ago, this stream of investment activity was fuelled by strong economic growth across the region and rapid development in the insurance sector in several countries. More recently however the region has struggled economically, and the forecast tightening of monetary policy by the US Federal Reserve is likely to compound the challenges due to the resulting effects on the currencies and economies of the region.

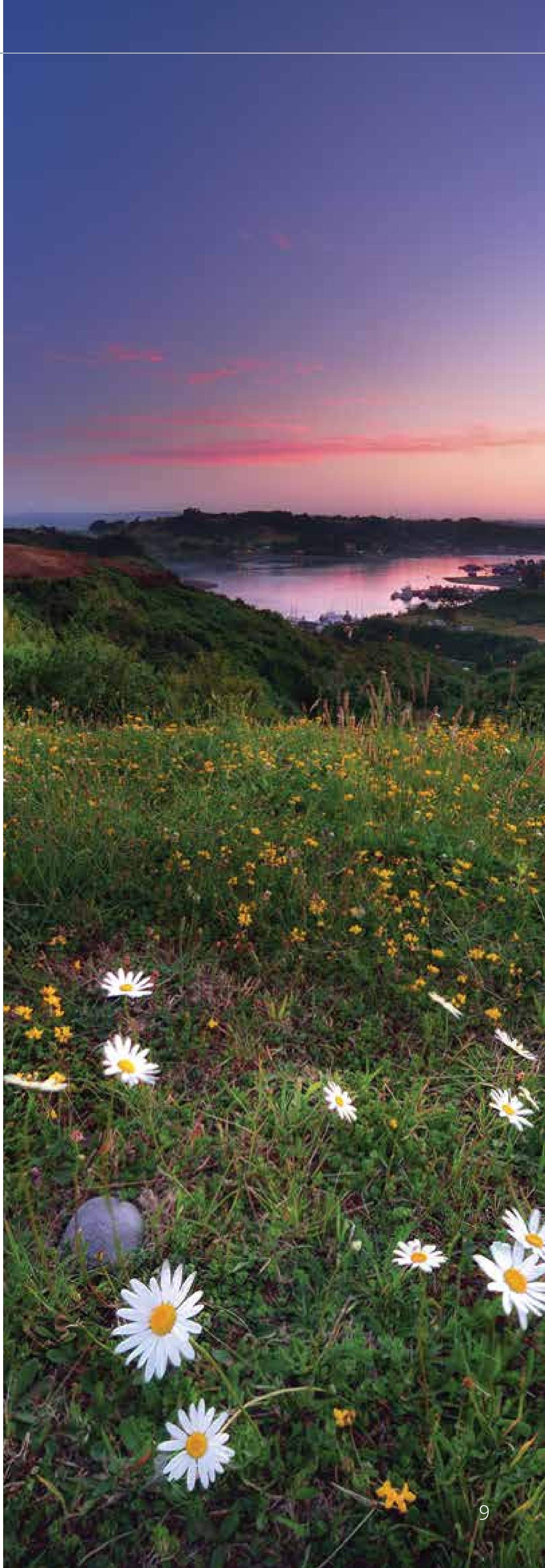
> Insurers are looking for a foothold in a range of developing markets. Latin America remains highly attractive to established international players looking for growth opportunities outside their often stagnant domestic markets; there has been double-digit life insurance premium growth in every major market in the region over the past five years.
>
> **Stirling Leech, Partner, Sao Paulo**

Brazil, Latin America's largest economy, is a focus of interest for insurance groups, and today it represents nearly half (48%) of Latin America's gross written premiums, according to Lloyd's. Despite the fact that the Brazilian economy has faced significant difficulties in recent years, insurers such as Axa, Chubb and QBE are investing in the development of their business lines in the country. In early 2016, French group CNP entered into exclusive discussions with BTG Pactual in Brazil to acquire 51% of insurance subsidiary Pan Seguros and broker Pan Corretora, and Axa completed the takeover of the commercial lines subsidiary of Brazil's SulAmérica in December 2015.

Chile is especially attractive because it is one of the most sophisticated insurance markets in the region. The sector is open to foreign players and is very competitive, partly because its high catastrophic loss exposure has forced it to deal extensively with the international industry for many years. The last six months has seen a series of deals that underline the appeal of this insurance market.

Mutua Madrileña – a Spanish insurer, completed its first international acquisition with the purchase of a 40% stake in Chilean insurer BCI Seguros for EUR 209 million (USD 221.1 million), and Mutua Madrileña's President, Ignacio Garralda, said the deal achieved one of the key objectives of the company's strategic plan – international expansion and the opening of new growth avenues.

Early 2016 saw US insurer Liberty Mutual acquire 99.6% of Penta Security, the fourth-largest non-life player in the country, writing premium of around USD 322 million in 2014. Another US insurer, Prudential Financial, announced it is to take between 34% and 40% in Chilean retirement provider Habitat at a cost of between USD 430 million and USD 510 million, and UK health insurer Bupa has paid about USD 129.8 million to buy an additional 26.1% in Cruz Blanca Salud, subsequently renamed Bupa Chile.



Into Africa

While Africa has lagged other emerging regions in terms of insurance interest, there is no doubt that the continent's potential is starting to be recognised. However, deal activity is low since the number of targets is small and many insurers are looking at alternative routes to grow across the continent.

Axa remains a key player; taking steps to build its account across the region and across a number of lines of business – both retail and wholesale. It paid EUR 54 million to acquire a 7.15% stake in African Reinsurance Corp, following its previous acquisition of Assur Africa, a holding company that owns 77% of Nigerian insurer Mansard. Axa also entered into partnership with Lloyd's group Chaucer to set up Axa Africa Specialty Risks, covering business such as political risks, energy and infrastructure in the continent.

In February, 2016, Axa also reached agreement to be the exclusive provider of insurance through Africa Internet Group, including its Jumia online retail subsidiary which is active in 11 African markets. The French group also increased its stake in MicroEnsure, a microinsurance specialist targeting Africa and Asia, to 45%.

Old Mutual in May 2016 announced that it had launched Old Mutual Specialty Insurance, a Lloyd's coverholder, to offer coverage in nine product areas: commercial property; energy; construction; political risk and trade credit; mining; kidnap and ransom; terrorism; cargo, transit and delay in start-up; and general aviation across sub-Saharan Africa.

> "We expect that there will be a marked increase in deal activities in South Africa as a result of proposed regulatory changes, such as the introduction of Solvency II and the regulation of insurance groups.
>
> **Ernie van der Vyver, Partner, Johannesburg**

They are not alone however in their interest – and other investors see insurance as a significant growth area. LeapFrog Investments, a specialist in emerging markets, demonstrated their interest by taking a majority stake in UT Life Insurance, one of Ghana's largest life companies. The former owner, UT Holdings, has banking interests and will continue to support the insurer and co-operate in the area of bancassurance. In addition, pan-African investor, African Capital Alliance bought a 49% stake in Continental Re, acquiring the holding from Saham Finances, which retains 51% of the reinsurer's shares.

India offering genuine investment potential

One geographic market that saw an acceleration in deals over the last 12 months has been India. 2015 saw the most significant change to the Indian insurance market for decades with an increase in the Foreign Direct Investment limit in the insurance sector from 26% to 49% – opening up to foreign investment a market with huge potential.

According to a report issued last year by the India Brand Equity Foundation, the country's insurance industry will grow from USD 66.4 billion in 2013 to about USD 350 billion by 2020, driven by greater life expectancy, an increasingly affluent middle class and a general increase in the awareness of risk.

In response to the changes in legislation a number of international insurers have raised their stakes in Indian entities to the newly permitted maximum of 49%, including:

- Japanese insurer Nippon Life in Reliance Life
- Asian life group AIA in Tata AIA Life
- French group Axa in Bharti Axa Life and Bharti Axa General
- Tokio Marine Holdings Inc. in Edelweiss Tokio Life Insurance
- Canadian group Sun Life in Birla Sun Life

In addition, German group Ergo, the primary insurance centre for Munich Re, will increase its stake to just short of 49% in HDFC Ergo General, in partnership with the Housing Development Finance Corp of Mumbai. HDFC Ergo has also acquired L&T General Insurance, a wholly owned subsidiary of Larsen & Toubro, a move which will turn HDFC Ergo into India's third biggest private-sector non-life insurer. The transaction, an all-cash deal, is valued at USD 82.5 million.

In two other deals of note, UK group Standard Life and Fairfax Financial Holdings increased their stakes to 35% in joint venture partners HDFC Standard Life and ICICI Lombard General Insurance respectively.

There can be little doubt that last year's regulatory change will act as a catalyst to help the insurance industry rediscover growth. Active foreign participation will also improve standards, implement best practice, better quality products, improved customer experience and choice. A note of caution however has been sounded by AM Best who said that the poor underwriting performance of the Indian non-life sector could delay expansion plans for foreign investors.

The FDI limit in India has increased

26% 49%

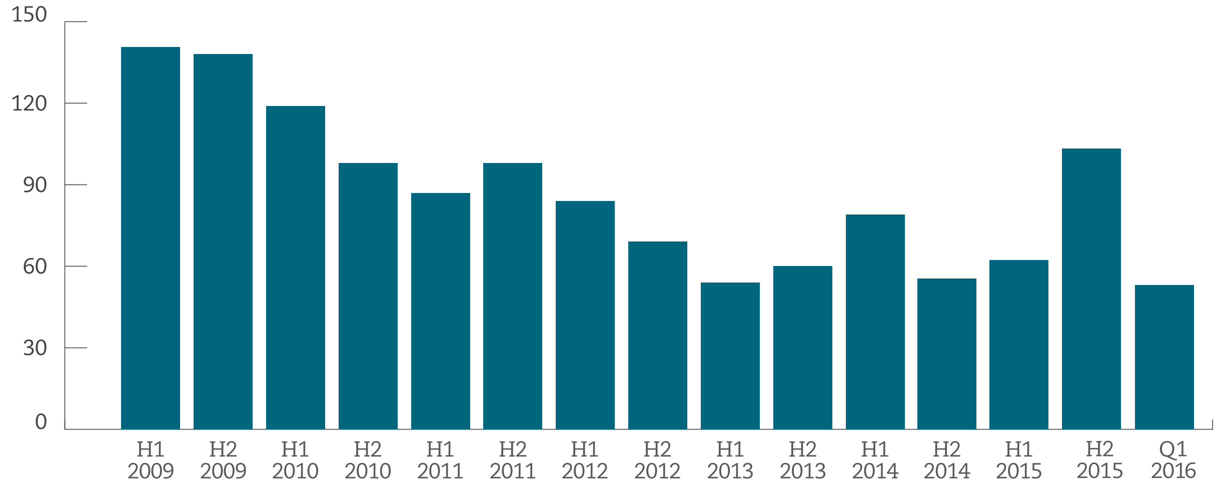
In addition, Lloyd's announced in April 2016 its intention to apply for a reinsurance branch based in Mumbai following the Insurance Regulatory and Development Authority of India's publication of the regulations governing the Lloyd's market.

> "The regulatory change will act as catalyst to help the Indian insurance industry rediscover growth. Foreign participation will also improve standards, products, customer experience and choice.
>
> **Vineet Aneja, Partner, New Delhi**

Growth through consolidation

For many insurance businesses the route to growth has been consolidation – particularly for smaller or medium sized insurers – and a particular driver for this in Europe has been the introduction of Solvency II. The new regulatory environment has changed the way insurance groups are structured, the way they operate and how they fund and utilise capital within their business.

Volume of insurance deals in Europe 2009 – March 2016



Many smaller and medium sized insurers have looked for a strategic merger or acquisition as a means of defending their position in the market. In France for example, the mutual-dominated health sector has become increasingly concentrated. Over the last 15 years the number of mutuals has reduced by a third and is expected to drop by a further 50% by the end of 2017. The first quarter of 2016 saw a number of deals between French insurers that reinforce this trend.

A key driver of this shift has been a new French law which requires every company to offer health insurance to its employees. Historically, the bulk of business underwritten by French mutuals has been individual health policies so this shift in the market requires a change in strategy which can be difficult for smaller players to execute. Additional pressure on these businesses is coming from the requirements of Solvency II, especially the disclosure requirements of Pillar 3, as well as the changing tax environment.

> “The introduction of Solvency II has had a significant impact on insurers' perception of how they need to manage their capital requirements, in turn driving deal activity.
>
> **Yannis Samothrakis, Partner, Paris**

Regulatory change driving disposals

The other sector of the market affected by Solvency II has been the legacy market where an increasing number of firms are looking to dispose of books of business – either live or already in run-off, in order to manage their capital requirements more effectively. According to Willis Towers Watson, 77% of Lloyd's businesses are considering the disposal of a legacy portfolio, and 53% of firms based in Western Europe expect to make at least one sale in the next three years. This provides a range of opportunities for those looking to achieve critical mass or diversification. The impact of M&A activity is also expected to drive further run-off opportunities, with companies seeking solutions for non-core portfolios once integration has been completed.

For example, in October 2015, Charles Taylor announced the disposal of its non-life insurance subsidiaries, Cardow Insurance and Beech Hill Insurance, as part of its strategy to reduce exposure to non-life companies in run-off and instead acquire life insurance firms. "We are focusing our strategy on acquiring life insurers, which offer attractive opportunities and generate cash releases for the group," Charles Taylor group CEO David Marock said in a statement.

A handful of well-capitalised legacy business acquirers are still demonstrating an active interest in deals including Enstar, Catalina Holdings and Swiss Re. The latter agreed to acquire Guardian Financial Services in September 2015 for GBP 1.6 billion, as a means of expanding its role in the management of closed books of UK life policies. In a statement, the reinsurer said Guardian Financial Services presented "an attractive opportunity to deploy part of excess capital above the Swiss Re Group's profitability hurdle rate of 11% [return on equity]; in line with the group strategy." In March 2016, Catalina signed an agreement to acquire AGF Insurance from Allianz SE subsidiary AGF Holdings. Catalina CEO and chairman Chris Fagan said: "We have been developing our expertise in this class of business over several years and retain an appetite to acquire more of this class and related legacy risk."

Regulatory changes were also behind the merger of Partnership Assurance and the Just Retirement Group last year. In March 2014, the UK Chancellor announced a liberalisation of pension laws, which caused the sale of annuities to drop sharply, devastating the prospects for insurers in this sector.

There have been a range of examples of insurers looking for expansion by entering into new lines of business or building on an existing footprint. In the US, Zurich announced the planned takeover of crop insurer and agency Rural Community Insurance Services in December 2015, a business that wrote a gross premium of USD 2.1 billion in 2014. In the UK Beazley acquired the UK open market medmal business from Marketform. Adrian Cox, Beazley's head of specialty lines, added: "Healthcare liability is one of Beazley's core specialty lines offerings and the addition of this team continues our strategic expansion in the international arena."

Growing organically

The appeal of M&A as a route to growth has clear advantages, but it is by no means the only option available to insurance businesses. Neither is it always the most appropriate or available, depending on the location and the characteristics of the market. The challenges of finding a suitable target and, significantly, at a suitable price, may cause insurers to consider other avenues. These might include establishing a branch or subsidiary in a new location, entering into a joint venture agreement or investing in new distribution channels.

> Acquisition targets aren't always popular as they often come with baggage – there is an attraction to starting with a clean slate and setting up your own platform to act as a base for regional expansion.
>
> **Ian Stewart, Partner, Singapore**

Insurance penetration rates in SE Asia are **half** the global average

Starting afresh

One region where there is considerable interest in creating start-up operations is South East Asia. As with many developing economies, the region is an attractive proposition for insurers in mature markets experiencing modest growth levels. Insurance penetration rates are low – 3.1% in the region compared to 6.2% globally; while a middle class (that has expanded six-fold in the past decade) has a range of new assets that it is looking to protect. At the same time an ageing population is putting extreme pressure on health care provision.

While regulators in some markets such as Malaysia are actively encouraging consolidation in order to create fewer, stronger, better-capitalised insurers, other jurisdictions in the region are characterised by a lack of obvious or appealing targets. Singapore is one such market; under-represented in terms of obvious businesses to acquire but still very much an attractive destination for investment and expansion.

Much of Singapore's appeal is due to an ambition by the government to become a predominant South East Asian hub and a global market place, which has resulted in a welcoming regulatory regime. This has led to a significant uptick in interest from international re/insurers looking to set up shop and establish a base for wider access to markets across the region. PartnerRe, W.R. Berkley and Canopius are just three examples of international players who have been granted new licences by the Singapore Monetary Authority recently, and anecdotal evidence suggests there have been more applications in the last six months than in the previous decade.

Significantly, Singapore is increasingly becoming a destination for outbound Chinese expansion. China Re is in the final stages of establishing a branch office in Singapore, which is expected to become operational in the second half of 2016, as it continues to internationalise its business. Singapore will be China Re's second foray overseas; it first established a special purpose syndicate at Lloyd's of London to write a whole account quota share of Catlin's book in 2012.

Close but not too close

In addition to M&A in Latin America, the region also remains another market with huge potential for organic growth, but those looking to enter the market must be prepared to make a substantial investment. Start-up operations can be quite costly due to the need for registration and approval processes in a number of countries. Meanwhile, those looking at acquisitions will find bargains few and far between with local insurers tending to demand a high multiple of their book value.

Miami is emerging as a regional hub for Latin American insurance and reinsurance business attracting a number of international players, including Allied World, Beazley and loss adjuster Cunningham Lindsey, who have set up their Latin American hubs in the city. Miami offers a well-skilled bilingual workforce with growing expertise in insurance and reinsurance as well as deep connections with and accessibility to Latin America. From this regional hub the next step is to establish local entities under the hub or to enter into fronting arrangements with local insurers as well as intermediaries in target markets. Miami also serves as the ideal gateway to markets in the Caribbean. With the prospect of continuing easing of US sanctions against Cuba and eventual normalisation of economic relations between the two, Miami is also likely to become the vital hub and link for doing business in and into Cuba.

Taking the reinsurance route

Another market with appealing growth prospects that has long been touted as ripe for M&A activity is the Middle East. However, historically a number of barriers to transactions have existed, including structural issues, mismatched price expectations between buyers and sellers and the difficulties of due diligence. Those looking to enter the market have also had to contend with foreign ownership limits that have restricted their participation.

Today, those looking to do business in the region are looking at a widening range of options. Draft regulation published last year will create a new financial free zone in Abu Dhabi, which will provide an alternative route into the market. Meanwhile, international players have been continuing to come into the Dubai International Financial Centre (DIFC), where 100% foreign ownership of reinsurance entities is permitted. Partner Re, XL Catlin and Markel are just some of the big international players that have opened an office in the DIFC to serve as a staging post from which to access the region. "London still has a major role to play but regional hubs such as Singapore and Dubai have started to grow their level of expertise and grow their market share because ultimately clients want to trade locally if the expertise is there," Crispin Hodges, head of Beazley's Dubai office, said.

> "The Dubai International Finance Centre is becoming a hub for reinsurance in the region – 'the Singapore of the Middle East.' Activity is increasing among International players attracted by a favourable regulatory environment.
>
> **Peter Hodgins, Partner, Dubai**

Last year Lloyd's of London officially opened its specialist underwriting platform in Dubai, providing another route into the market. There are now 14 entities writing on Lloyd's paper in the Middle East and more are set to follow. With the regulator itself having set the ambitious target of doubling the number of the insurance entities by 2018, for those looking for growth in the Middle East – either by acquisition or start-up – these are exciting times.

14 entities now writing on Lloyd's paper in the Middle East

Finding the right partner

As with the recent spate of activity in India following the raising of the foreign direct investment limit described above, entering into a joint venture (JV) with a local partner has long been a popular route to growth, especially in countries where there are limitations on the level of foreign participation. International players in the past have been prepared to take minority positions in a JV as a means of establishing a foothold in the market with the expectation that they would be able to build out their position at a later date. Recent regulatory changes in key markets have enabled international players to revisit their agreements and attempt to re-negotiate more favourable terms.

In China, foreign equity holders have historically usually sat with a stake at around 24.9% to prevent a company from tipping into foreign ownership, which would make it subject to tougher regulations and penalties. Under new rules which allow higher levels of foreign direct investment, international partners in JVs are now pushing for 50% arrangements under which they would be treated on the same terms as domestic underwriters. Those not able to achieve that may review their options in China, which could include considering an exit from the market entirely.

Advent Insurance Management is a good example of how a joint venture can be used to create a global footprint. In September 2015, it entered into a JV with Sydney-based regulatory outsourcing services firm Littlewoods Services to create a new company in which Advent holds a controlling stake. It also formed similar partnerships with AmeriClaim and Canadian Claims Service to establish presences in its key markets the US, Canada, UK and Australia, giving Advent access to more than 80% of Lloyd's coverholders.

Elsewhere, Markel International is exploring an entry into Latin America by way of joint ventures with primary insurers in Brazil and Colombia to write specialty insurance. Markel International president, William Stovin, said a joint venture was attractive as it would enable the re/insurer to use the brand and distribution of local carriers. "You have to be part of the local market if you want to write the business…the potential of the market is huge," he said.

Lloyd's of London also offers joint venture possibilities. Last year Beazley and Korean Re established a special purpose syndicate (SPS) at Lloyd's. The SPS, which is supported by a two-way programme of reinsurance as well as employee secondment, gives Beazley experience of the Korean market and Korean Re of Lloyd's. This type of SPS arrangement is becoming more and more popular in the market – another recent example was Patria Re of Mexico teaming up with Pembroke – and will continue to be so going forward.

In a further development, Beazley has since announced it is going to extend the relationship further in 2016 and is looking at developing products together with Korean Re this year. Andrew Horton, chief executive of Beazley, said: "We are also looking at opportunities in relation to whether we can write more of their reinsurance and similarly can they write more of our reinsurance, because the relationship is growing. If it works well then it is a blueprint for other parts of the world where we would like to do something similar."

Growth through technology

Technology is opening markets that have traditionally been difficult to access, offering new routes to growth. The most pertinent example is China, a key target for many businesses but one that has posed challenges due to a number of factors including stringent regulation for international entrants and restrictions on foreign investment.

However, the introduction of new rules has enabled underwriters to distribute products online – in all classes of business with the exception of motor – throughout China without the need to have a branch office in place. This development has opened a path to true national distribution throughout the country for foreign underwriters – encouraging international players to reconsider the Chinese market both in GI and life. Online distribution of products will remain an area of acute interest with one caveat; if you don't underwrite the products yourself, it's much more difficult to distribute through a third party due to a complicated approval process.

Elsewhere in the world insurers are looking at how they can utilise technology to enhance distribution and reach new customers. In Africa, for example, TV ownership is low but mobile phone penetration is high so insurers are looking at app-based solutions. One strong example of this is Kilimo Salama, a crop insurance scheme headed by the UAP Insurance Company of Kenya. The system works by supplying shop owners with mobile phones. When a farmer buys seed or fertiliser and wishes to purchase insurance, the shop owner scans the barcode on the products, collects an additional 5% of the retail price and the seed and/or fertilizer company chips in another 5%. The combined payment is sent to the insurance company via the phone.

Farmers do not have to file individual claims. The weather is monitored by 40 small weather stations that Kilimo Salama has installed throughout the country where the insurance is currently being offered. If the rains fail, or are too great, payments are automatically made to accounts that the farmers have installed on their cell phones. Following the success UAP has had with this product it is moving further into the digital realm, developing a mobile application for individual medical insurance customers.

> “Insurers are looking at how they can utilise technology to enhance distribution, deliver economies or reach new customers. They are also deploying venture capital into technology start-ups around the world.
>
> **Mark Williamson, Partner, London**

Maximising big data

Data, particularly big data, has been a hot topic for insurers for some time. Almost every insurer understands that the data they hold is a valuable asset and, if used correctly, can deliver powerful insights into business generation, underwriting and claims handling. However, thus far, only a few companies have been able to monetise its potential. According to a survey by Bain, most insurers have barely scratched the surface with around one in three life insurers and one in five P&C insurers yet to apply big data advanced analytics to any function.

P&C insurers have yet to apply big data advanced analytics to any function

Elsewhere, a similar revolution is underway in the world of health and life insurance due to the growing prevalence of wearable technology such as the Apple Watch and Fitbit activity trackers. Up to a third of insurers are now offering services based on the use of these devices, according to research by Accenture.

Insurers looking for growth will increasingly look at how to get more out of the data they hold, for example targeting new customers such as young named drivers on motor policies. In addition, they will look at where they might partner with other data-rich organisations like Uber, a company building up a vast reservoir of data on customers that has the potential to be mined more effectively than ever before in order to sell new products. Generali acquired 100% of MyDriveSolutions, a UK-based provider of data analytics for the motor sector. The Italian group has set up a new telematics hub in London to expand data analysis activities to various business sectors. Bain estimates that annual spending growth on big data analytics reached an average of 24% in life and 27% in P&C in 2015.

Investing in the future

In response to the on-going difficult trading conditions a number of larger insurers including Axa, AIG and Transamerica have taken a long term bet by deploying venture capital into technology start-ups around the world. According to recent data from Accenture, insurance technology start-ups attracted USD 2.6 billion of investment in 2015, up sharply from USD 800 million the year before.

Aviva is one of the latest companies to follow this trend, announcing in May 2016 that it had invested several million pounds in Founders Factory, a new technology incubator to support promising financial services start-ups that could help improve the insurance market.

Describing the rationale behind the move, Andrew Brem, the company’s chief digital officer said: “Insurance and financial services has been stuck in a bygone, analogue era when it comes to engaging with customers – we believe it’s high time to bring the industry into the digital age, for the benefit of customers and insurers alike.”

In April 2016, AIG and Hamilton announced plans to launch a joint venture, alongside hedge fund Two Sigma, which aims to "revolutionise" the North American small to medium-sized enterprise (SME) insurance market using predictive analytics. It will combine Two Sigma's proprietary data science and technology platform with Hamilton's technology and underwriting expertise in the SME market, as well as AIG's capabilities in the SME sector and its global presence.

Predictive analytics technology uses algorithmic models and data analytics to enable a more nuanced approach to underwriting, allowing for faster selection, analysis and pricing of risk. Describing the rationale behind the move, AIG President and CEO Peter D. Hancock said, "With this venture, we want to revolutionize the SME market through technology that creates a more tailored and compelling value proposition for clients in this critical segment."

> "The arrival of online aggregators almost two decades ago was the last big revolution in the market but that is set to change. In response to increasing market competition a number of insurers are investing in new technologies as an alternative route to growth.
>
> **Ivor Edwards, Partner, London**

Extending the boundaries

Another key growth area for insurers is to extend their offering by investing in new products. Some of these may be opportunities stemming from innovation and the application of new technology, others from the opening up of new markets to existing products.

> The market for protection against cyber threats presents significant growth opportunities but also challenges. As holders of significant amounts of customer data it is vital that insurers get their own houses in order, especially in light of new EU rules that represent the biggest change to data protection in over a generation.
>
> **Mark Williamson, Partner, London**

Demand for health insurance in emerging markets

Perhaps the product that offers the most significant growth prospects in the coming years is health insurance. This is particularly the case in emerging economies with growing and ageing populations coupled with rising levels of wealth and a burgeoning middle class. China is a prime example. Historically, health insurance has largely been provided by the state but this is set to change. The government has announced plans to pull out of underwriting health insurance, a move that will generate very high growth rates in the sector over the next few years and create a third major category of primary insurance in China, behind GI and life. Although there are currently only around 10 to 15 health insurance companies in the Chinese market, domestic and international companies are lining up to acquire new licenses in anticipation of capturing a share of what will undoubtedly be a fast growing market.

In the Middle East, regulations in Abu Dhabi, Dubai, Qatar and Saudi Arabia have made it compulsory to have private health insurance, a move which has led to significant interest from major international players such as Munich Health, BUPA, Aetna and Cigna who are looking further afield for growth opportunities due to high levels of penetration in their domestic markets. For those international health insurers who are not already present in the region, access is predominantly through partnership arrangements with local players. Although, the possibility of obtaining direct licenses where possible in order to position themselves to grow their market share is also being explored.

New risks, new opportunities

A number of relatively new insurance products are seeing increasing demand and present considerable growth opportunities. Chief among these is cyber insurance. As an ever-growing number of businesses rely on digital processes to drive their operations, incidents of data breaches, hacking, ransomware and other forms of cyber crime are on the rise and seemingly never far from the news headlines. Lloyd's of London has put cyber at the top of a list of five big risks the market faces in 2016.

While the market for cyber insurance in the US is already relatively mature, new regulations in Europe are likely to drive a significant increase in demand and a number of insurers are positioning themselves to take advantage. In one example earlier this year Beazley and Munich Re announced that they were teaming up to launch a major push into cyber insurance, offering tailor-made policies with double the amount of coverage that was previously available.

In another development, the boom in transactions – 2015 was the busiest year ever with deal volume reaching USD 4.7 trillion – has led to an increase in demand for M&A insurance. According to data from Marsh, the M&A insurance limit placed globally was up 45 percent in 2015 to USD 11.2 billion. The number of insurers offering the product on a primary or excess basis worldwide reached 25, a 30% increase on the previous year. Recent entrants to the class include QBE and Chubb.

Financial lines is another growth area, in both mature and emerging markets. In Brazil, the corruption scandal engulfing energy giant Petrobras centres on a bribe scheme which is believed to have moved hundreds of millions of dollars illegally into the accounts of company executives, public officials and political parties and has triggered payments of several hundred million dollars in legal costs covered by D&O policies. As a result, demand for D&O insurance is soaring not just in Brazil, but in other markets across Latin America.

Tomorrow's world, today

Looking to the future, a number of developments are set to open revolutionary growth channels. The rise of the sharing economy is set to be a game-changer. Today, its principal sectors generate around USD 15 billion in global revenue according to PwC, but this is forecast to reach as much as USD 335 billion by 2025.

The sharing economy will generate
USD 335 bn
in global revenue by 2025

French insurer Axa is one company that has moved quickly to position for the opportunities that the sharing economy may offer, entering into a partnership last year with BlaBlaCar to provide innovative insurance products tailored especially to long-distance ridesharing. This looks to have been a prescient move. BlaBlaCar has since gone from strength-to-strength, launching in a further nine countries in 2015 (it now operates in a total of 22) and raising a further USD 200 million in funding that pushed the company's value to USD 1.6 billion. In a similar move in early 2016 Allianz announced that it would offer insurance cover to drivers who rent out their vehicle to strangers via the car sharing app RideLink.

Elsewhere in the industry the arrival of peer-to-peer (P2P) insurance – essentially a new twist on the established mutual structure utilising new technology – is most likely to appeal to the younger generation who are not as accustomed to the traditional ways of transacting insurance, are more open minded and creative and, crucially, more comfortable with social media.

Start-up Lemonade, set to launch around mid-2016 as an online P&C insurance carrier built around a P2P business model, has raised USD 13 million in initial funding and received the backing of reinsurers at Lloyd's of London and Berkshire Hathaway's National Indemnity among others. In a media interview, the company's president, Shai Winniger, said: "We're challenging the way insurance companies work, with a peer-to-peer business model fueled by self-serve technology. We've seen this kind of combination breathe new life into other industries, and we're determined to do the same for insurance." The market is watching the progress of P2P with interest.

Elsewhere, a number of products and processes enabled by the application of new technology, such as 3D printing and small unmanned aircraft systems – also known as drones – are reaching a tipping point at which their use will become increasingly widespread, bringing with them a changing liability landscape and opportunities in abundance.

However, the arrival of driverless cars is arguably the single development which will have the biggest transformation on the insurance industry. Personal lines motor insurance will likely cease to exist and be replaced by product liability policies which will have a dramatic impact on underwriting, distribution and claims handling. Those insurers who can move quickly to adapt and evolve their product offerings to seize first-mover advantage will have a head-start in the race for future growth.

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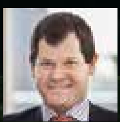

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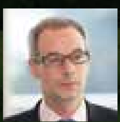

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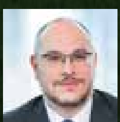

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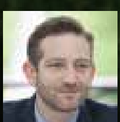

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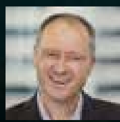

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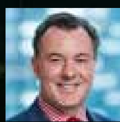

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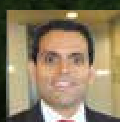

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