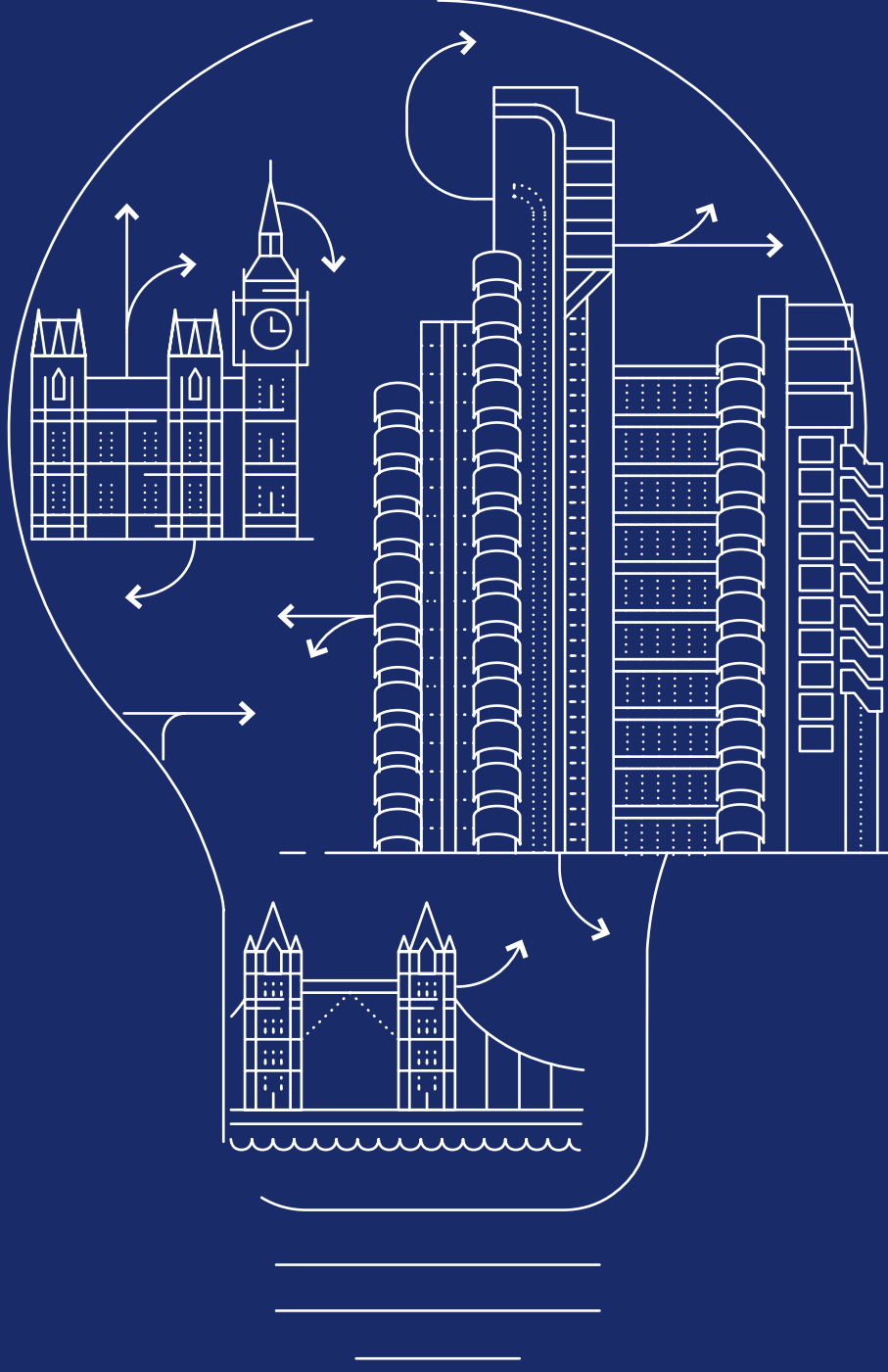




Which way now? Is the UK MGA market at a crossroads?

A survey of MGA and insurance carrier opinion
on the state of the sector





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Which way now? Is the UK MGA market at a crossroads?

A survey of MGA and insurance carrier opinion on the state of the sector.

The UK Managing General Agent (MGA) sector has seen significant growth in recent years. The prolonged soft market has acted as an incentive for carriers to seek to diversify income streams and remove fixed costs, and an MGA offers the potential of access to cost-efficient new distribution channels and specialist markets beyond the scope of an insurer's appetite or expertise.

Historically, London has been the ideal location for this type of business; it has long been home to a community of international, entrepreneurial and agile underwriters with specialist skills looking for a chance to create value and build reputation. In recent years MGA incubators have been set up by a number of the larger brokers and underwriters looking to capitalise on that skills base. However, the appeal of the model has broadened and more recently the UK regions have seen significant growth in the number of new MGAs being set up.

But the path ahead is not clear cut. Pricing uncertainty, Brexit negotiations and a tougher regulatory environment are just some of the significant headwinds facing the sector.

The drive for efficiencies in the company market, combined with regulatory hurdles and a lack of capacity at Lloyd's, has seen MGAs come under increasing scrutiny to ensure that they are delivering on their promises to efficiently reach new customers in new markets in a way that delivers profitability for all parties involved.

Against this backdrop, we surveyed more than 100 insurers and MGAs to better understand the issues and challenges facing the sector, and to shine a light on its future direction.

Methodology

The research that formed the basis of this report involved a survey of over 100 UK-based insurers and MGAs, seeking their views on the current state of the MGA market, how they see it developing, and the state of the insurer-MGA relationship. The survey was conducted during March and April 2019.

The research was supplemented by a number of interviews with insurers and MGAs which delved deeper into the issues identified by the survey in addition to insight from the Clyde & Co MGA team.

Thanks to the Managing General Agents' Association for their assistance distributing the survey to their members and arranging interviews.

Key findings

- Vast majority of carriers expect to increase or maintain MGA capacity
- But insurers and MGAs agree that market is more complicated than ever – with regulatory compliance a key reason
- Frustration at lack of progress made in standardising processes – which is driving cost, complexity and delay
- Lloyd's under threat as best place to set up an MGA – principally from the London company market
- Market divided on who should provide tech capability and investment, and the importance of claims handling services



Riding the storm

In part as a response to the longest soft market the industry has known, the use of MGAs has become a popular route for carriers to generate top-line growth. As a result, the size of the MGA market in the UK has grown to £4.7 billion – around 10% of the country's general insurance premiums.

Despite widespread speculation that an MGA “bubble” has formed that is ready to burst, our research shows that only 21% of insurers expect their MGA capacity to reduce in the coming year – the vast majority expect it to hold steady or increase. However, market conditions have undoubtedly become much tougher for MGAs in the past 12 months, with the sector increasingly under scrutiny.

In May 2018, Danish insurer Alpha, which provided capacity to several MGAs, collapsed – the fourth unrated insurer operating in the UK to go into liquidation in three years. Then in August, the FCA sent a notice to brokers emphasising the need to perform due diligence on the insurers they use, especially those providing capacity to MGAs.

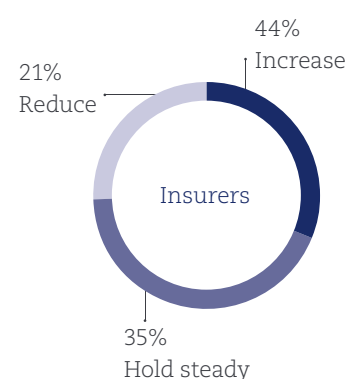
Lloyd's too, a significant source of capital, put the spotlight firmly on performance and, in the January renewal of delegated authority business, syndicates were forced to be more discerning in their distribution partnerships. Those that were underperforming in terms of loss ratio or were not deemed specialist enough were hardest hit, but even some high-performing relationships came to an end.

The trend of re-evaluating MGA relationships is spreading. In May 2019, for example, Aspen put its UK SME MGA into run-off, despite the profitable performance of the business, which had a COR of just under 90%. This follows the completion of the \$2.6 billion acquisition of Aspen by Apollo in February and the results of a strategic business plan review.

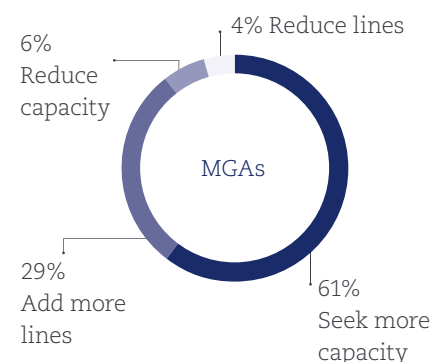
As we look ahead, the findings of our research indicate a heightened sense of awareness of the need to drive value among both MGAs and capacity providers, who are evenly split over whether there will be more or fewer MGAs in 2019. There is, however, a strong consensus that the market is becoming more competitive and that it is now much harder to set up an MGA than at any time in the past.

While there is no evidence to suggest that a bursting of the bubble is imminent, we expect these pressures to lead to a re-balancing of the MGA market.

How do you expect your MGA capacity to develop in the coming year?



How do you expect your business to develop in the coming year?



53%

of insurers

believe there will be more MGAs in 2019

51%

of MGAs

67%

of insurers

believe the market is becoming more competitive

69%

of MGAs

78%

of insurers

agree that setting up an MGA is much harder now than at any time previously

67%

of MGAs

“At their best, the entrepreneurial spirit of MGAs adds tremendous value to the market. They are a source of proactive and innovative underwriting and are an important channel for insureds and brokers to access capital, and for carriers to access new markets, experiment and diversify. But the performance of a number of MGAs has been sub-optimal. It is quite right that we are seeing them come under scrutiny – challenge and choice are features of an effectively functioning market. This is a chance to refresh and modernise the MGA model.

Jennette Newman, Clyde & Co Partner, London

No safe harbour

Lloyd’s may be under challenge as the MGA market of choice; but the rising regulatory burden is part of a universal threat that makes establishing, and more particularly, running, a successful MGA business a challenging prospect in any jurisdiction.

Our research shows that Lloyd’s is viewed as the best location to develop MGA business by fewer than one-third of respondents, with the rising regulatory and compliance burden cited as a primary factor behind the decision to look elsewhere.

Overwhelmingly, MGA players believe that the London company market offers the most opportunities, but interestingly, carriers show greater interest in the US and other geographies.

However, a change of location does not mean that the challenge of regulation is going to be any easier. It is becoming progressively tougher for MGAs to get established – wherever they choose to set up – due to the rising regulatory and compliance burden, the FCA’s systems and control requirements and more particularly, the new Senior Managers and Certification Regime which comes into force in December 2019.

Carriers have a responsibility to control the MGAs they work with from a regulatory, capital, reserving and conduct perspective. As the requirements become more complex, so the burden on the MGA and the carrier to monitor and control operations becomes greater.

The challenge lies less in the initial set-up of a relationship between an MGA and a capacity provider but more in terms of on-going operations – maintaining good governance and compliance with the carrier’s rules and regulations. This can be very difficult particularly if MGAs are working with multiple carriers, all of which do things differently. Theoretically this means separate management information, reserving, capital, service level agreements (SLAs), confidentiality and data protection, reporting and audit for each carrier.

In our research, around three-quarters of respondents agreed that a lack of standardisation between capacity providers adds cost, complexity and delay.

Where provides the best opportunity to develop MGA business?

Location	Insurers	MGAs
Lloyd’s	33%	27%
London company market	42%	63%
USA	11%	2%
Other geography	13%	8%

91%

of insurers expect more regulatory and legal scrutiny over MGAs in Lloyd’s in 2019

75%

of MGAs are looking at competitors to Lloyd’s due to its rising regulatory and compliance burden

79%

of insurers

68%

of MGAs

believe there has been little or no progress in standardising processes in the last year

“ The contraction in capacity at Lloyd’s is a necessary evolution for it to return to profitable underwriting. There will be a concern that the business it loses should not be the profitable business. But while carriers are keen to focus on new opportunities outside the UK, Brexit has thrown a spanner in the works by creating issues around licensing. It has focused attention on where companies are licensed to do business and impacts how they conduct it.

Ivor Edwards, Clyde & Co Partner, London

“ The increased focus on compliance and regulatory actions has without doubt added to our workloads and impacts on speed of delivery. However it is right that we demonstrate professionalism and act in a way that delivers products and services that are fit for purpose and protect the needs of the customer, capacity and regulator. This does also present us with numerous opportunities to distinguish ourselves in a crowded market by demonstrating our underwriting/product governance expertise in building propositions which have the customer needs at the heart of the offering.

Kevin Donoghue, Underwriting Director,
Accelerate Underwriting



Maps do not always align

Good MGA-carrier relationships are built on common areas of interest and complementary skillsets.

Insurer priorities

Our survey findings indicate that the majority of insurers prioritise ease of doing business (cited by 53% of respondents), good customer service (51%) and efficient access to new markets (49%). The first two could be considered baseline requirements for any business-to-business relationship, while the third is the *raison d'être* of many MGAs. Indeed, we have seen a plethora of MGA start-ups including C-Quence – set up by former AIG UK head Jackie McNamee – aimed at leveraging new technology to deliver on all three of these priorities.

Technical insight and capability is also a key requirement cited by almost half (43%) of insurers. In just one recent instance, Kersey Specialty was launched late last year with backing from Fidelis. Its sole focus is on delivering insurance to the upstream energy market, a prime example of an MGA offering niche market expertise.

Overall, capacity providers have become much more rigorous in their assessment of potential MGAs than they were a few years ago. They are increasingly looking to enter into longer-term relationships and the approval process is now often controlled by a binding committee, which expects to see serious underwriting pedigree and a proven track record for start-ups in terms of premium growth before they are offered the pen.

MGA priorities

From the MGA perspective, the responses were both more emphatic and more divided. Market reputation was cited by the overwhelming majority (77%) of respondents as the most important factor when choosing a capacity provider, regardless of location, ahead of experience in areas of specialisation, cited as key by around half of MGAs.

Reputation is what helps sell cover to retail brokers and their insureds, particularly in new geographic markets or where the cover being offered is innovative or meeting a new demand. A capacity provider's rating is a key factor in its reputation and an MGA may push for single capacity status, a rather more attractive proposition than a panel arrangement. From the carrier's perspective it is not ideal to encourage the possibility of channel conflict, but most will be reluctant to offer exclusivity to an MGA unless they can guarantee a very substantial book of business.

Experience in the class of business was also cited as critical by almost half (48%) of MGAs. This is an area where many MGAs seek to establish close collaboration and information sharing.

For example, Envelop Risk, a start-up MGA in Bermuda, uses machine learning tools to price cyber risks, with underwriting capacity supplied by MS Amlin. Collaborating across shared infrastructure to speed decision-making, Envelop models the cyber economy and enables assessment of individual risks within one data model.

So far so straightforward. Where relationships can become more complicated, however, is in the detail of how these critical requirements are met.

Market discussions suggest that carriers' demands can vary significantly. On one side, some can set very aggressive growth targets, the meeting of which is contingent to them offering capital. On the other, there are those that are attracted to the way that an MGA operates and expect it to maintain high quality service of existing customers as the top business priority. Often, the critical factor will be time – how long should a relationship be allowed to run before the two parties take stock of gaps in performance or customer expectation?

Another interesting issue uncovered by our research is the significance of claims performance. Although this was cited by considerably less than half of MGAs (38%) in terms of key criteria in selecting a capacity provider, this area was the focus of many of our discussions. This suggests that claims performance, while not a critical factor in initial selection criteria, is fundamental to the day-to-day relationship between insurers and their MGA partners.

MGAs that do not handle claims direct are particularly exposed to poor performance in this area as a bad claims experience has the potential to have a negative impact on their ability to grow and drive profitability.

As a result, they prioritise good relationships with brokers and the claims handlers at their capacity providers, and place great emphasis on the importance of doing thorough due diligence – not just around an insurer's financials but its claims record as well – before entering into any partnership.

What carriers look for in an MGA partner

Efficient access to new markets	49%
Volume of business	18%
Efficiency / ease of doing business	53%
Strong conduct / risk management record	39%
Customer service	51%
Technical insight and capability	43%
Cost	35%
Exclusivity	10%
BD / cross-selling opportunity	2%

Key factors for MGAs choosing a capacity provider

Market reputation	77%
Experience in your areas of specialisation	48%
Streamlined application process	17%
Help in navigating necessary regulatory approvals	21%
Collaborative approach on conduct risk management	21%
Ease of reporting and compliance	19%
Claims paying record	38%
Speed of approval	17%
Exclusive arrangement (no competition with other MGAs or capital provider on open market basis)	25%
Ability to leverage data	19%

“ For start-up MGAs there is often a tension between writing business to generate commission to cover overheads and writing business profitably. In many ways, how well a business manages the dynamics of these relationships is critical to its future success. It is impossible to over-emphasise the importance of open and frank discussions up front and of establishing clear SLAs so there are no surprises.

Toby Rogers, Clyde & Co Partner, London

“ Solid, effective MGA-carrier relationships take a lot of time and effort to set up and the fit needs to be right on both sides. Transparency and honesty are crucial shared requirements. We look for a long-term commitment from our capacity providers and in return offer them underwriters with true expertise, relevant experience in the lines of business that they write, and who are held in high regard by brokers.

Karen Williams, Underwriting Development Manager, MPR

“ One of the advantages of MGAs is that they can handle frequency claims on behalf of insurers. They’re closer to the client and can be more efficient. But insurers must understand the nuances in outsourcing claims handling to MGAs – that’s why we set up a dedicated MGA team in our claims division. We take the bigger claims.

We define the level of authority; beyond that, we step in to handle claims on behalf of the MGA. Meanwhile, MGA claims teams need to understand the insurers’ business model. We work with MGAs on an on-going basis to look at reserving and claims handling.

Enrico Bertagna, Head of MGA Network, Zurich



Bridging the gaps – is technology a panacea?

Looking forward to the coming year, around 60% of MGAs expect to develop their business by adding more capacity and 30% by adding more lines. But they perceive barriers in their way. Around two-thirds think that better sharing and analysis of KPI data would help them to grow their business faster, with just less than a half citing more rapid adoption of new technology, such as blockchain.

There is an interesting range of views among MGAs and insurers as to the role of technology in their relationships.

Around a quarter of MGAs say that they look for technology support and assurances from carriers with 45% taking the opposite stance – seeking to differentiate themselves on their technology capabilities. On the insurer side there is a roughly even split between those insurers who expect their MGAs to demonstrate technological strength and those who do not see technology as an important factor in their MGA relationship; for these players underwriting skill and customer reach are what count.

The type of MGA may be a factor here – those with a single product and a strategy based on generating volume may prioritise and invest heavily in technology while others may choose to emphasise their niche specialisms and customer relationships. But the over-riding factor is cost. Not all MGAs have the financial clout to invest on the scale needed to utilise technology as a service differentiator. They will likely purchase a suitable product from a third-party software-as-a-solution provider – attempting to invest in developing proprietary systems is too expensive. This means that for most MGAs, where technology is adding value is in terms of expense management; or in generating insight through data analysis (cited by 19% of MGAs).

“Speed of information transfer is critical – our systems need to be able to talk to each other effectively – so we expect the back-end processes of MGAs to be up-to-speed in terms of having the right technology. On the customer-facing side maybe one-in-a-hundred insurtech start-ups will be successful. Innovations need the ‘wow’ factor; it’s not just about impressing the underwriters – insurtechs need to persuade everyone along the chain of the value of their ideas.

Bill O'Malley, Senior Vice President,
Arch Insurance Europe

“We don’t see technology as a cost but as a significant benefit. We have invested in our own proprietary technology and proven that it works. Carriers can test their products with us without it costing either side lots of money. This makes us more attractive because we can flex to suit their specific needs and they can use us for what their own systems can’t handle.

Gary Johnson, Senior Underwriter, IPrism



Cost and technology are both factors in another area of frustration expressed by a significant number of MGAs: the lack of progress towards underwriters standardising their application and compliance procedures. Lloyd’s push to reform the requirements and processes for delegated underwriting to increase efficiency and reduce compliance costs could be a step in the right direction but there remains a broader need for market modernisation.

Significant progress has been made in some areas such as electronic placement but there is still some way to go – a plethora of different manual and digital systems endure. For MGAs, this is a problem which has no clear solution in sight. Capacity providers – especially the larger ones – will have invested heavily in their technology systems. They will also have their own governance and compliance systems that are complicated, extensive and well established; there is little incentive from their perspective to change and every reason to maintain the status quo.

Looking ahead, a number of MGAs regard insurtech start-ups as a potential – if not yet an immediate – threat, especially in terms of providing alternative distribution opportunities. This has precipitated some to realise the importance of technology and shift their focus. According to the MGAA, the percentage of its members developing an insurtech strategy jumped from 25% to 38% in 2018.

On the carrier side, most major re/insurers have already made some kind of foray into the insurtech world, whether through setting up a digital innovation lab, entering into an artificial intelligence underwriting partnership, having a division that identifies and invests in insurtech companies or simply underwriting insurtech products, such as “on demand” insurance sold via a mobile phone app. They are also aware that a huge percentage of insurtech start-ups do not survive their first six months and that crucially, they do not have the insurance expertise to pose a genuine standalone threat.



“ The application of technology to streamline processes and generate efficiencies is a no-brainer for both MGAs and capacity providers but its application to underwriting is where the greatest value is likely to be. The larger insurers have been investing heavily in insurtech for some time and with their deeper pockets they are always going to be ahead of MGAs. While an insurtech start-up may come up with a winning idea with the potential to disrupt the market, it still needs to rely on an insurer to make the concept a reality and gain critical mass.

John Eastlake, Clyde & Co Partner, Bristol



Importance of technology

45%	of insurers want MGAs who are strong in tech
45%	of MGAs offer support in this area
42%	of insurers see underwriting skill and customer reach as more important
25%	of MGAs seek tech support from insurers

Carriers: Is technology an important factor in your MGA relationships?

Answer choices	Responses
Yes – the MGAs seek assurances / skills / support from us in this area	7%
Yes – we seek assurances from our MGA partners that they are strong in this area	44%
No – underwriting skill and customer reach are what count	42%
Other	7%

MGAs: Is technology an important factor in your carrier relationships?

Answer choices	Responses
Yes – we seek assurances / skills / support in this area from insurers	26%
Yes – we offer support in this area	45%
No – underwriting skill and customer reach are what counts	27%
Other	2%



A positive outlook

It is clear that the MGA sector is in a period of change.

Over the coming year some MGAs will struggle – predominantly new start-ups and others without much of a track record or without transparent administrative and strong management information systems in place. But those which can demonstrate an underwriting profit and a sustainable business model will endure.

There is still plenty of surplus capacity in the market and, as a result of the remedial process, rates are going up in some areas, along with other signs of market hardening. We are also seeing moves by the insurance-linked securities (ILS) market to support MGAs, in areas including property catastrophe. ILS-backed MGAs could have a rosy future, not least due to the significantly lower expense base of ILS vehicles.

Although premium growth in the MGA sector in the next 12 months will broadly flatten out, in a reversal of the rising trend of the past several years, the overall level of premium written in the sector should hold steady, despite market exits. Indeed, the lifespan of an MGA tends to be quite limited - there has always been a steady flow of MGAs disappearing from the market and others coming in to replace them. MGA incubators have seen a surge in interest as senior underwriters who lost their jobs as part of the performance clampdown seek to re-enter the market.

What this survey shows is a market broadly aligned on the role it plays in the wider insurance sector and the challenges and the opportunities it faces. There is broad agreement on what needs to happen for it to endure with greater standardisation of processes, sharing of data and information, and investment in technology all key factors in the MGA model staying relevant. But how these improvements will be implemented and who is responsible for providing them is unclear. Ultimately, there is no one-size-fits-all solution. Carriers and MGAs alike have different priorities, strategies and expectations, even if they share common growth objectives.

The insurance market, particularly in London, is often seen as the home of specialism, innovation and entrepreneurialism. Whatever the weather, sentiment suggested that the market keeps moving forward.

“Some 80% of (re)insurers see their capacity for this channel holding steady or increasing and most agree that it will be harder to set up MGAs going forward. On that basis we could predict that those which survive the increased scrutiny and pressure to perform will emerge from 2020 as bigger, better run and more profitable businesses. These are the hallmarks of a maturing sector.

Jennette Newman, Clyde & Co Partner, London



Services for MGAs

Clyde & Co is the leading insurance law firm in the world. We are a proud founder supplier member of the MGAA, providing claims advisory, litigation and handling services, regulatory advice and corporate/commercial services to MGAs and capacity providers in the UK and globally.

We understand the MGA market and the issues an MGA will face in dealing with claims or commercial issues; we have experience of advising many MGAs on coverage, defence of third party liabilities, employment and corporate issues.

Please do get in touch if you would like to know more.

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