

Insurance Banana Skins 2019

The CSFI survey of the
risks facing insurers

TECHNOLOGY

CYBER
RISK



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Centre for the Study of
Financial Innovation

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Preface

This is the seventh Insurance Banana Skins survey that we have published since 2007 – the second in which the risks surrounding technology and cyber have come out on the top of the pile, and the first in which they are unequivocally the biggest upfront risk.

That is not to say that other risks have diminished. Indeed, the overall level of perceived riskiness within the industry is now at the highest since we began the series in 2007, and two old chestnuts (inappropriate regulation and poor investment performance) are right up there. But the risks associated with the take-up of modern technology and with cybercrime of one sort or another are way ahead of the rest – and both are rising.

This shouldn't be a surprise. After all, it is well known that many insurers are lumbered with legacy systems that need updating – and that integrating them is time-consuming, fiendishly complicated and, inevitably, very expensive. Equally, we are all aware of the risks around cyber – from simple hacking, from ransomware, from Trojans, even from malevolent state actors. We are less aware of 'silent' cyber exposure – but it is a real risk that is starting to take up much more C-suite time.

Of course, it is not all bad news. This latest survey, for instance, shows the industry (at least, the broader global industry) to be surprisingly nonchalant about Brexit. There is also, quite clearly, plenty of capital lying around, and corporate governance and management are not perceived to be big issues.

But the emphasis on technology and cyber ought to be a wake-up call. This survey produced 927 responses from 53 territories; it can hardly be dismissed as parochial or unrepresentative.

As usual, the CSFI's thanks go to our friends at PwC, who provided funding for the report, while allowing us complete editorial freedom. We are very grateful. I am also very grateful to my colleagues, Keyur Patel and David Lascelles, who have been responsible for the Banana Skins surveys for many years, and who have steered the series from an overwhelming concern with investment performance and equity markets to today's very different concerns around tech and cyber.

Andrew Hilton
Director

This report was written by **Keyur Patel** and **David Lascelles**

Sponsor's Foreword

Welcome to Insurance Banana Skins 2019.

We are once again delighted to sponsor this market leading publication detailing the risks facing the insurance sector across the globe in the next 2-3 years. We continue to work with the CSFI on this excellent survey, which began with its very first edition in 2007 and is now on its 7th edition.

The world has changed significantly since Insurance Banana Skins first began. In 2007, the iPhone had just launched, Twitter was in its first year, we had yet to experience the Global Financial Crisis and Solvency II was still under development. A lot has changed in this time, and the insurance industry has continued to work and develop to respond to the changing needs of its customers, shareholders and regulators. We have seen real growth in new ways of conducting business and reaching customers through a myriad of new channels. The external environment has also changed – economically, politically and socially. These changes of course bring risks and challenges – areas of focus for management and regulators alike.

Digitalisation

Operational risks continues to be the key category of risk occupying Insurers' Boardroom conversations. Whilst there is a pressing need for better and efficient technology, in the era of digitalisation, the threat of cybercrime has become ever more prominent. Linked to this is the risk of change management, questioning whether insurers are embracing such changes in technology and the virtual world. As always, the successful management of change is dependent upon how it is perceived - do these risks present an opportunity for insurers to proactively boot out legacy systems for a more customer centric innovation or cause a disruption that requires a reaction to remain relevant? Either way, the need to upskill the workforce to face these opportunities/challenges, however it is perceived, is in critical demand.

Regulation

In our last edition, we saw regulation drop overall with change management rising as the top risk. In this edition we see a rise of regulatory risk. This has been driven by new areas of regulation that we have seen introduced since 2017 (IDD and GDPR in Europe and various new Conduct standards across the globe) coupled with upcoming new accounting standards, particularly IFRS 17. The task of addressing and implementing these new regulatory standards, in the mandated timeframe, is proving to be a challenge for insurers everywhere.

Sustainable Development

As a big riser in 2019, climate change features high in this Banana Skins ranking, narrowly missing the top 5 position. We expect climate change and sustainable development to continue to impact the insurance industry, business and country agendas across the world. How will climate change impact the industry's financial risk and more so, how will insurers and regulators step up to address this?

Challenging the status quo and encouraging a move from traditional thinking, attitude and behaviours were suggested as the most effective ways in which these top risks can be managed. The transformation of the industry with this new wave of industrialisation requires diversity in thinking to best capitalise in this market. Despite the changes and risks highlighted however, the industry's response to preparedness as a whole has suggested greater confidence in their ability to manage and address these risks.

We have had an incredible year with almost 1,000 insurance practitioners responding to the survey globally. We are indebted to our global PwC network of clients for taking the time to participate in this initiative – we are also indebted to the CSFI for their perceptive analysis – thank you.

For further conversations on any of the issues raised, please do not hesitate to contact us.

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**927
responses
from 53
territories...**

About this survey

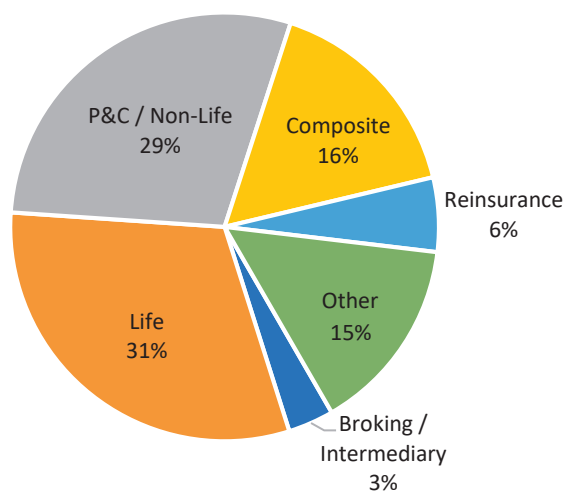
Insurance Banana Skins 2019 surveys the risks facing the insurance industry in early 2019, and identifies those that appear most urgent to insurance practitioners and close observers of the insurance scene around the world.

The report, which updates previous surveys in 2007, 2009, 2011, 2013, 2015 and 2017, was conducted in March and April 2019, and is based on 927 responses from 53 territories.

The questionnaire (reproduced in the Appendix) was in three parts. In the first, respondents were asked to describe, in their own words, their main concerns about the insurance sector over the next 2-3 years. In the second, they were asked to rate a list of potential “Banana Skins” or risks. In the third, they were asked to rate the preparedness of insurance institutions to handle the risks they saw. This report ranks and analyses each Banana Skin individually.

Replies were confidential, but respondents could choose to be identified.

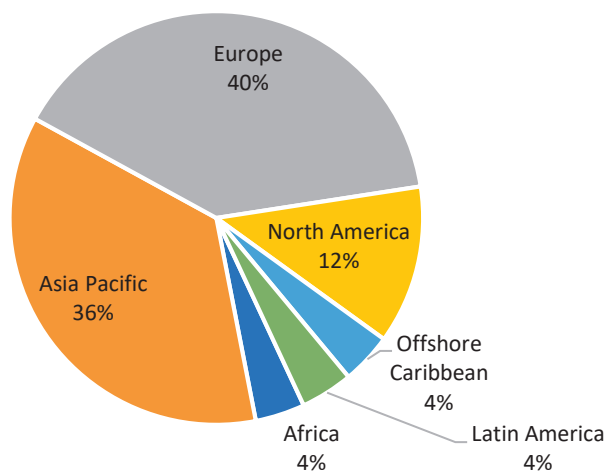
The breakdown of responses by sector was:



Three-quarters of the respondents were from the primary insurance industry¹. The remainder were from the reinsurance and broking sectors, and non-practitioners such as regulators, consultants, analysts and other professional service providers.

¹ I.e. the life and non-life sectors, or a composite. In this report we sometimes use the term non-life to describe what some markets call the Property & Casualty (P&C) sector.

The breakdown of responses by region was:



Three-quarters of respondents came from Europe and the Asia Pacific regions. The next largest group was from North America, with the remainder split evenly between Africa, Latin America, and offshore insurance centres in the Caribbean.

The breakdown of responses by territory was:

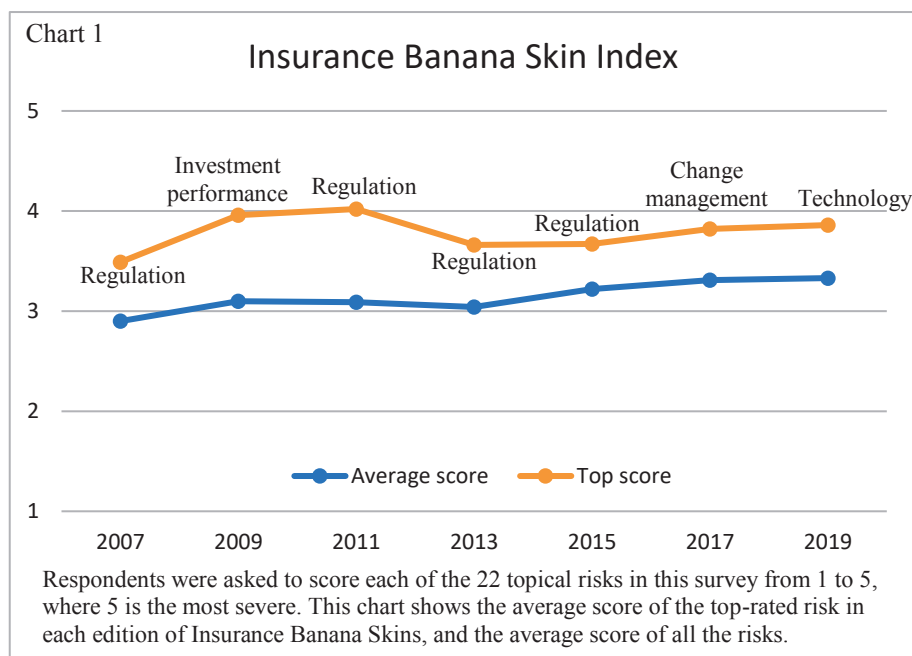
Angola	3	Greece	11	Philippines	23
Argentina	10	Hong Kong	19	Poland	3
Australia	33	Hungary	1	Portugal	22
Austria	30	India	11	Saudi Arabia	1
Barbados	3	Indonesia	28	Singapore	46
Belgium	33	Ireland	6	South Africa	28
Bermuda	32	Isle of Man	4	South Korea	18
Brazil	21	Italy	4	Spain	32
Canada	58	Japan	25	Sweden	4
Cayman Islands	2	Kenya	2	Switzerland	10
China	23	Luxembourg	27	Taiwan	40
Colombia	1	Malaysia	14	Thailand	13
Czech Republic	6	Malta	6	Turkey	27
Denmark	25	Mexico	5	UAE	1
Egypt	2	Netherlands	30	UK	66
France	6	New Zealand	33	USA	57
Germany	13	Nigeria	1	Vietnam	6
Gibraltar	1	Peru	1		

Summary

This survey identifies the risks, or "Banana Skins", facing the global insurance industry in the first half of 2019 as seen by a sample of 927 practitioners and close observers of the scene in 53 territories.

The most negative since the series began in 2007...

Significantly, the overall tone of the responses this year is the most negative we have seen since we began the series in 2007. This is largely due to the scale of the challenges facing the industry through technological and structural change, and concern about the industry's ability to manage them successfully. The results should also be seen against a background of growing economic uncertainty around the world, and heavier regulation.



Mounting pessimism is reflected in Chart 1, where the blue line shows the average score given by respondents to the basket of risks in our questionnaire. The red line shows the risk which achieved the highest score. This pessimism is due largely to a rise in operating risks, notably advances in technology which challenge the industry's traditional structures. The other source of rising anxiety is the public environment,

Chart 2

Major categories of risk* (Score out of 5)			
	2019	2017	+/-
Operating risks	3.46	3.39	+0.08
Economic environment	3.30	3.57	-0.27
Governance	3.12	3.18	-0.06
Public environment	3.20	3.14	+0.06

*The components of each category are listed in the survey questionnaire in the Appendix.

i.e. political and regulatory risk which could impose constraints on the industry. (See Chart 2) These shifting perceptions are reflected in the ranking of individual risks in Chart 3. The three highest risks form a cluster around the theme of technological change and industry response. The top position occupied by **technology risk** is rooted

Technological change is the biggest challenge...

...but note climate change, rising fast

in concern about the scale of the challenge facing the industry in this area, and is a pervasive theme in this report. Closely allied to it is the risk in No. 3 position, **change management** which exposes a high level of concern, even doubt, about the industry's ability to address the formidable agenda of digitisation, new competition, consolidation and cost reduction which confronts it. **Cyber risk** at No. 2 is a major issue for the industry as it adjusts to the digital age, both as an operational risk and an underwriting risk.

Technology risk was also responsible for the high position occupied by **human talent** (No. 8), where there is concern that the industry may fail to attract sufficiently able people to enable it to address change successfully. The challenges of new forms of **competition** ranked No. 7.

Regulatory risk at No. 4 is seen to be rising strongly, driven by initiatives such as IFRS 17 and stronger capital and consumer protection requirements. Another fast riser is **climate change** (No. 6) which had not featured near the top of this survey series since 2007. The spate of weather and natural catastrophe events now makes this an urgent industry concern.

The next cluster of risks, **investment performance** (No. 5), **macro-economy** (No. 9) and **interest rates** (No. 10), showed no overall change, but the responses suggested that the industry is uncertain about the direction of the global economy and interest rates.

The impact of **political risk** (No. 11) in the form of growing protectionism and populist policies could tax both the international and domestic insurance markets through trade wars and deeper interference. It could also aggravate **reputation risk** which has risen from No. 17 to No. 13 on the back of concerns about consumer rights, data security and the perception that insurance may be losing its "social relevance".

On the other hand, institutional risks such as **business practices** (No. 15), **quality of management** (No. 16) and **corporate governance** (No. 19) continued to be seen as low level, though possibly in a view tinged by complacency.

Low level risks include **capital availability** (No. 20) where the concern is about the surplus of capital in the industry, and **Brexit** (No. 21) which is seen as a non-event by

Chart 3

Insurance Banana Skins 2019

(2017 ranking in brackets)

- 1 Technology (3)
- 2 Cyber risk (2)
- 3 Change management (1)
- 4 Regulation (6)
- 5 Investment performance (5)
- 6 Climate change (-)
- 7 Competition (8)
- 8 Human talent (9)
- 9 Macro-economy (7)
- 10 Interest rates (4)
- 11 Political risk (11)
- 12 Cost reduction (13)
- 13 Reputation (17)
- 14 Guaranteed products (10)
- 15 Business practices (12)
- 16 Quality of management (14)
- 17 Credit risk (-)
- 18 Social change (16)
- 19 Corporate governance (19)
- 20 Capital availability (20)
- 21 Brexit (22)

respondents outside the UK and the EU, most insurers being only distantly affected, or adequately prepared.

Big movers

This year's survey has produced striking changes in the ranking of some Banana Skins, reflecting shifting perceptions of risk in a difficult market. Here are some of the big movers.

UP

Regulation (No. 4). A heavy regulatory agenda including IFRS 17 and consumer protection increases compliance risk and implementation costs.

Climate change (No. 6). The spate of natural catastrophe events has increased the urgency of this risk, and could be undermining insurance pricing models.

Reputation (No. 13). Data security, populist politics and "declining social relevance" could all damage insurance.

DOWN

Interest rates (No. 10). The industry has learnt to live with low interest rates, and the next move may be up.

Guaranteed products (No. 14). For similar reasons, products which offer guaranteed returns appear less problematic.

Social change (No. 18). The industry is preparing for the challenge of meeting social demands created by greater longevity, growing medical and care needs etc.

Tech and cyber top the list for all sectors - and regions

Response by type of respondent...

The survey shows similarities as well as differences between the responses of various insurance sectors. The challenges of **technology** and **cyber risk** are at the top of the list for all sectors: life, non-life, composite, reinsurance etc. Concern about **regulatory risk** is also generally high and there is a common concern about the quality of **human talent** in the industry. Differences are found mainly in the assessment of **interest rate risk** which the life insurers ranked high along with **investment risk**, and **climate change** which ranked high with the non-life and reinsurance sectors. Concern about the **macro-economic** outlook was highest among life insurers and reinsurers.

...and by geography

A breakdown of responses by region displays similar risk priorities. The challenges of **technology risk**, **cyber risk** and **change management** ranked among the top risks for all regions. The rise in **regulatory risk** was also a common concern in all regions except Latin America. Concern about business conditions such as the outlook for the **global economy** and **interest rates** was highest in Europe. **Political risk** was ranked highest in the Americas, driven mainly by the rise in populist politics. **Climate change** featured highly in all regions except Asia Pacific.

Preparedness

Respondents were asked how well prepared they thought the insurance industry was to handle the risks they identified. On a scale of 1 (poorly) to 5 (well) they gave an average response of 3.11, an uptick from the previous survey's 3.02, suggesting greater confidence about the industry's ability to weather a difficult business environment.

Tech and/or cyber head the list by sector and by region...

Who said what

A breakdown of the results by respondent type and region shows a strong common concern with the impact of technology change and the industry's ability to manage it against a background of rising cyber risk, economic uncertainty and heavy regulation.

By sector

Life Insurance

1	Technology	The challenge of technological change and how to address it led the life insurance sector's list of concerns, as it did for most of the industry. More specific to the life sector were concerns about investment performance and the outlook for interest rates, both of them linked to the risk in No. 7 position: the economic outlook, which was judged to be shaky. The sector gave a higher than average score to regulatory risk, particularly because of the introduction of IFRS 17. Conduct and management risks were also noted as a higher threat.
2	Investment performance	
3	Regulation	
4	Cyber risk	
5	Change management	
6	Interest rates	
7	Macro-economy	
8	Competition	
9	Human talent	
10	Business practices	

Non-life

1	Technology	On the non-life side, the risk agenda is also dominated by concerns over technological change, specifically the entry of new forms of competition and distribution. Cybercrime features in a double capacity: as a threat to industry security and as an underwriting risk. Macro-economic risk did not feature in the top ten partly because some respondents saw recession benefiting insurance sales, while concern about interest rates and investment performance is also lower than average. For the first time, climate change ranks near the top.
2	Cyber risk	
3	Climate change	
4	Change management	
5	Regulation	
6	Competition	
7	Human talent	
8	Investment performance	
9	Cost reduction	
10	Political risk	

Reinsurance

1	Cyber risk	Cyber risk, both as a security issue and an underwriting risk, is the top concern of the reinsurance sector, as in the previous survey. However climate change came No. 2, marking a dramatic new entry to the ranking. The challenge of structural change in the industry, driven by new technology and competition, is also high on the agenda. The high position of political risk reflects worries about the threat of protectionism in this internationally oriented sector of the business.
2	Climate change	
3	Technology	
4	Investment performance	
5	Regulation	
6	Change management	
7	Macro-economy	
8	Political risk	
9	Quality of management	
10	Interest rates	

Composite

- 1 Cyber risk
- 2 Technology
- 3 Change management
- 4 Regulation
- 5 Investment performance
- 6 Climate change
- 7 Interest rates
- 8 Competition
- 9 Human talent
- 10 Cost reduction

Responses from the composite sector reflected those of the non-life side more than those of the life side, with a strong focus on cybercrime and technology risk, as well as on the growing risks posed by climate change. The rankings of investment and interest rate risk reflected the concerns of the life side. As with other sectors, the size of the regulatory agenda was a strong concern for the composites. The theme of the declining social relevance of insurance featured in a number of responses.

Brokers/intermediaries

- 1 Cyber risk
- 2 Change management
- 3 Human talent
- 4 Technology
- 5 Climate change
- 6 Regulation
- 7 Cost reduction
- 8 Business practices
- 9 Investment performance
- 10 Guaranteed products

Cyber risk headed the list of concerns for brokers and intermediaries, though their wider focus was on the challenges facing the industry in the areas of changing insurance markets and customer demand, and the development of human skills. Cost reduction was seen to be an urgent priority to address insurance affordability, seen by many in this sector as a growing issue with consumers. Business practices featured among top ten risks because of continuing concerns about questionable selling and reputational issues.

By region

Europe

- 1 Technology
- 2 Cyber risk
- 3 Change management
- 4 Regulation
- 5 Investment performance
- 6 Interest rates
- 7 Climate change
- 8 Macro-economy
- 9 Competition
- 10 Political risk

The threat of cybercrime challenged the necessity for business and IT modernisation for the top spot in Europe's response, the largest group in this survey by region. Interest rate risk, the No. 1 Banana Skin in Europe in the last two editions of this survey, receded to No. 6, but was still considered more urgent than in any other region – and was associated with higher than average concern about the broader macroeconomic climate and guaranteed products. Reflecting the rise in populism, political risk rounded off the top ten.

Asia Pacific

- 1 Technology
- 2 Cyber risk
- 3 Change management
- 4 Regulation
- 5 Investment performance
- 6 Reputation
- 7 Quality of management
- 8 Competition
- 9 Business practices
- 10 Human talent

The Asia Pacific response shared the same top five risks, in the same order, as both the European and global rankings. Beyond these, however, there was some divergence. As in the last edition of this survey, reputation risk was high at No. 6, and this year was linked to the threat of poor business practices at No. 9. Concerns about the quality of management and risk management at insurers were also notable. On the other hand, Asia Pacific respondents were more optimistic about economic conditions, ranking macroeconomic and interest rate risk significantly lower than average.

North America

- 1 Technology
- 2 Cyber risk
- 3 Change management
- 4 Human talent
- 5 Regulation
- 6 Investment performance
- 7 Climate change
- 8 Political risk
- 9 Competition
- 10 Macro-economy

Concern that the insurance industry could struggle to attract and retain talent was strikingly high in North America, a trend we also observed two years ago. At the top of the table, technology risk received the highest score of any region surveyed, while the industry's ability to respond to changing insurance markets was marked as a concern. Political risk was also prominent. Elsewhere, North America's response was broadly in line with the global rankings, with a slightly lower emphasis on previous years' top risks such as regulation, the macro-economic environment, and interest rates.

Latin America

- 1 Technology
- 2 Change management
- 3 Cyber risk
- 4 Climate change
- 5 Competition
- 6 Macro-economy
- 7 Cost reduction
- 8 Political risk
- 9 Human talent
- 10 Regulation

The response in Latin America was characterised by high concern about changing insurance markets and distribution channels, in an environment where cost reduction is a priority. It was particularly attentive to structural changes to the industry coming from big technology firms and Insurtechs. The threat posed by climate change ranked higher than in any other region, while there were also significant concerns about the macro-economic climate. However, investment performance, the top risk two years ago, has fallen out of the top ten, and regulatory risk was also seen as less urgent.

But are we better prepared to handle those risks?

Preparedness

We asked respondents how well prepared they thought the industry was to handle the risks they identified.

On a scale of 1 (poorly) to 5 (well), they gave an average response of 3.11, an increase from 3.02 last time. Breakdowns by region and sector are shown below, with 2017 scores in brackets.

Preparedness by region		Preparedness by sector	
Africa	3.31 (2.93)	Reinsurance	3.20 (3.06)
Offshore Caribbean	3.27 (3.12)	P&C / non-life	3.16 (2.99)
Europe	3.16 (3.06)	Composite	3.08 (3.10)
North America	3.11 (2.86)	Life	3.05 (3.04)
Asia Pacific	3.03 (3.00)	Brokers/intermediaries	2.90 (2.88)
Latin America	2.91 (3.00)		

Views on preparedness

Spain, non-life (2/5): "Insurers in general have benefited from living in a reasonably profitable and stable sector, which has demotivated change, innovation and transformation. The players not willing to transform and not fully aware of the challenges and opportunities arising will be at risk of disappearing."

Canada, broking (2/5): "The greatest obstacle is not the will to change or the ability but the willingness for all players to come together and work out the solution for the whole. If they fail to change, change will happen to them."

UK, non-life (3/5): "Business and underwriting risks attract a lot of attention and resources. Legacy systems or other drains on time and expense, comparatively less so."

Australia, life (3/5): "Awareness and action on these risks may be increasing but the effectiveness may be offset by a herd mentality, short term thinking and competing priorities."

USA, non-life (3/5): "The industry has the tools and the money, but adopting new practices in an industry with aging leaders will be hard."

Thailand, consultant (3/5): "Large local insurer and international insurers are quite well prepared to handle main risks while small to medium size insurers are not quite ready."

South Africa, composite (4/5): "Risk management is our business; significant planning, skill and capacity is focussed on the key strategic risks."

Australia, health insurance (4/5): "My feeling is that it is a mixed bag. Insurers need to question in a fast-paced changing world, do they have the frameworks in place to address emerging risks. If they are not willing to challenge the status quo the likelihood that they will be disrupted is significant."



1. Technology (2017 ranking: 3)

2019 Score: 3.86 (2017 Score: 3.75)

The urgent need for business and technology modernisation poses the greatest threat to the global insurance industry over the next 2-3 years, according to this survey's respondents.

First year that tech tops the list...

This is the first year that technology risk has topped our rankings. As a risk in its own right, it received the highest score of any Banana Skin we've surveyed since 2011. It is also a pervasive theme throughout this report, underpinning other high-ranking risks including cyber risk (No. 2), change management (No. 4), and competition (No. 7). By sector, it was ranked No. 1 for both the life and non-life sides of the industry; and by geography, in Europe, Asia Pacific and North America.

At the heart of responses was the view that many insurers are encumbered with legacy business models and IT infrastructure that are poorly equipped to handle the changing demands of the industry. But modernisation requires capital and skills that are in short supply, and an ability to forecast future needs that are far from certain.

The director of risk at a life insurer in The Netherlands said: "Old business models are dying/dead, and are only partially being replaced by new models. It's very likely many insurers will not succeed in wrestling themselves from legacy business, resulting in declining profitability and take-over". The treasurer of an insurance company in the US warned that: "The insurance industry as a whole is woefully behind other financial services firms in implementing technology".

Many respondents made the point that this challenge cannot be met simply by throwing money at it; that upgrading technology systems creates significant opportunities, but is also a "significant strategic risk if you bet on the wrong horse". The chief executive of a composite insurer in Belgium said: "The key is to make the right choices, i.e. which technologies do you want to give priority. When it is for process improvement, the choices appear to be quite clear. When it is for a commercial approach to end customers, the certainty to invest in/launch successful projects is much lower".

The consequences of making the wrong decisions could be wide-reaching. They include missing opportunities that are essential for keeping pace with competition, both from inside and outside the traditional insurance industry; increased vulnerability to potent threats such as cybercrime; and huge wasted investments in systems that are quickly obsolete.

The industry is highly likely to select large "industrial" systems to replace current legacy systems. This could well lead to today's legacy systems being replaced by tomorrow's legacy system. The industry should look to new ways of using proven technology to provide modern, flexible, adaptable systems.

Chris Powell, managing director and chief executive, Integrity Life, Australia

An actuary in the UK said: "Inefficient insurers risk being left behind, early adopters may end up wasting lots of money on the wrong solution, and new green-field entrants without legacy issues will continue to eat into the value chains of incumbents". The chief financial officer of a composite insurer in Poland said: "Potential failure would result from missed predictions on distribution and customer behaviour changes".

Do techies understand insurance?

In an environment of low returns, ensuring systems are brought up to date to enable use of big data, process efficiency, security and agility [are] the cost of legacy against niche new entrants.

Non-executive director, insurance broker, Australia

A further worry is that the pressing need for technology modernisation increases dependence on IT specialists, often from external vendors. The head of risk management at a Swedish life insurer said: “IS/IT and other support functions, with little or no knowledge of the core business, sit in the driver seat”. Another respondent warned that “Given current business models, the reliance on third and fourth party suppliers and the risks involved in managing them are far more prevalent.”

A few respondents were more sanguine. Jordi Calbet, Head of Digital Acceleration at Zurich Insurance in Spain, said: “Some players are not only adapting but leading the change, so the risk is not for the industry but for some incumbents”. Others noted that sluggish insurers might be sheltered by their size and position. The chief financial officer of a reinsurance company said: “Large organizations will struggle to implement technology changes quickly but may be protected by the barriers to entry in this industry, which include know-how, capital and regulatory restrictions. It is not cheap to operate in this space”.



2. Cyber risk (2)

Score: 3.85 (3.80)

The threat posed by cybercrime to insurers narrowly misses the top spot in our rankings for the second survey in a row. It received the most 5/5 scores of any Banana Skin, and was the leading risk for the broking, composite and reinsurance sectors.

Concerns from past surveys have intensified: the insurance industry faces a barrage of attacks from criminals and state-actors, many which are extremely sophisticated, and is an enticing target because of the volume of valuable data it holds and its often outdated and piecemeal defences.

Cyber attacks are real, sophisticated and malicious. The risk is exacerbated by the growing dependence on the internet and connectivity, not just our corporate IT systems that may be exposed.

Martin Mulcare, Independent Director, SCOR Global Life Reinsurance, Australia

A respondent at a life insurer in Canada said: “Insurers tend to have a large amount of data valued by cybercriminals who are politically motivated or wish to turn a profit by selling their services/private data on the black market. Most of the industry seems to have the appropriate framework in place to somewhat mitigate this risk, but cybercriminals are continuously using more and more sophisticated approaches to stay one step ahead. Even with the most advanced security team and technology, this risk will always persist”.

The harm to insurers from a breach could include material losses from outages, loss of records, and the theft of intellectual property. An even bigger fear is the hefty fines and potentially “huge and severe” reputational damage and loss of trust that may follow a data breach.

Compounding this risk was widespread uncertainty around how to manage it. A respondent from the P&C industry in the Philippines said: “Cyber risk is present but

Cyber risk increasing...

Do we understand cyber-insurance?

the understanding about what we can do as insurers is still in its infancy, especially in the country. We don't have the expertise in the country and the market is not fully aware of the risks that they might be exposed to". Many respondents pointed out the imperative for insurers to collect data to remain competitive, even as the difficulty of keeping it safe rises.

We also received many comments that focussed on the industry's exposure to risk as a result of underwriting cyber insurance. "Insurers don't know how bad this can get – limited cover is the only option as disruption by digital crime is still not clearly understood", said the president of a general insurance company in Indonesia. A respondent in Hong Kong said: "Lots of insurers are trying to write cyber policies, but the potential impact of cyber insurance claims is still very much unknown (even if cyber itself isn't new, the scale of potential impact is unimaginable)". Another in the UK observed that: "Cyber coverage/exclusion contracts are yet to be really tested".

There was a minority of comments, however, that suggested cyber risk is being overblown. "It's topical, but the impact is no worse than a material insurance loss, e.g. a CAT event", said the vice president of risk at a life insurer Canada. A regulation specialist in the UK said the threat was: "High but maybe not as high as the amount of time and money people are spending on it".



3 Change management (1)

Score: 3.76 (3.82)

Though it has been overtaken at the top of the table, the risk that inadequate response to change will damage insurers continues to be seen as urgent.

Perry Thomas, chief risk officer at Scottish Widows & Lloyds Banking Group Insurance, said: "In today's market this is the main determinant of survival of current market participants and the pace of that change has increased very substantially. The technology/digitisation arms race... between incumbents with their customers, and fintechs with their superior customer engagement experiences [is] a race between economies of scale versus cost efficiency."

These are changes driven by technologies such as artificial intelligence and the internet of things that are overhauling insurance markets, radically different customer expectations (see box), and modern distribution channels. Several respondents cited the example of driverless cars. An audit committee member at an insurer in Brazil said: "If people 'buy' mobility rather than vehicles, insurers will have to negotiate much more with mobility service providers and much less with people who buy vehicles. The bargaining power will decrease considerably and the margins may fall. I do not see this in three years, but in the longer term, the threat is very large."

The world has been built on insuring the value of physical goods, such as property, but less so on insuring and measuring the value of non-tangible digital goods. There is therefore a protection gap in how we have thought of losses and insurance to date and how we will need to deal with them in the future. Take the debates of how autonomous vehicles would be insured, or how to protect against terrorism when the main damage may be consequential loss (e.g. Gatwick being shut by drone activity or a denial of service attack crippling an entity's access to markets), rather than building damage which is included in traditional policies.

Non-executive director, property and casualty insurer, UK

Change is accelerating...

... and is harder to predict

A persistent theme in the responses was around the industry's immobility and recalcitrance, with comments including: "too big, too slow, too much internal politics", and "passive resistance to change is the norm in the insurance industry". The chief compliance officer at a life insurer in Canada said: "Our industry's greatest risk is a failure to become truly customer-centric. This could lead to growing irrelevance, through digital disruption, and/or harsher regulatory intervention. Our products remain overly complex, too expensive and often do not meet the real needs of our customers. The quality of advice through our agency and other distribution channels is spotty, and our interactions with customers are more often than not driven by a sales culture and ripe with conflict of interest".

A risk of not changing fast enough is that insurers could find themselves side-lined into unprofitable parts of the business. The chief risk officer at a life insurer in Belgium warned of the: "risk of ending up as the manufacturer in the insurance value chain (where the customer is in the hands of a third party), and a squeeze on margins".

Taking a more optimistic view, a respondent in Singapore observed: "Sales continue to be strong with insurance penetration growing in most markets, suggesting that things are not changing as quickly as some might expect. Furthermore, insurers are investing in change". Another respondent argued: "The scare of massive disruption of just a few years ago has not materialised. Technology is making insurers more nimble and cost efficient".

What kind of insurance do customers want?

How is demand for insurance changing?

A widespread observation in this survey was that younger consumers in particular have very different expectations from insurance providers than past generations – if they feel that they need insurance at all.

The head of risk and compliance at a life insurance company in the UK said: "The received wisdom is that life policies are sold not bought. There is an increasing trend for consumers to complete their own research and a lack of willingness to pay for advice. I suspect there is therefore a risk that life companies will not adapt to changing patterns of distribution". Others noted that: "The dependency of current generations on social media creates an expectation of 'online all the time'" and "convenience and price are all that matter".

A senior vice president at a mutual insurer in the US said: "In the life/disability income protection markets we continue to see growing customer apathy – 'I don't need it' and 'it is too expensive'. Customer ignorance of the facts is clouded by indifference".

The feeling is that to reach these less engaged markets, the industry needs to fundamentally reassess the risks that consumers care about, rather than simply banking on what has been historically profitable. A main risk to the industry is whether service providers can: "create a more comprehensive value proposition, in order to broaden the ecosystem not only to basic coverage, but also protection (to prevent issues) and additional services (related to the main coverage) ", said Christian Balatti, Director, Strategy & Transformation, at MetLife in Argentina. The chief risk officer at a Belgium insurer said: "Customer behaviour towards new mobility, self-diagnoses, and connected ['smart'] homes is totally switching the way we have to think and design coverage, anti-selection, guarantees and responsibility".



4. Regulation (6)

Score: 3.62 (3.53)

A continuing heavy agenda of regulatory change is driving regulatory risk up the rankings. Respondents expressed frustration with the cost and distraction of compliance, and warned of the potentially damaging effects that disproportionate requirements could have in areas such as capital, consumer protection and product availability.

A London-based actuary said: “Recent changes in regulation have achieved little in giving added protection to insurers and/or policyholders. This not only does not reduce risks but also causes a loss of confidence in the industry and regulations themselves.”

A particular bugbear is IFRS 17, the new worldwide reporting standard which requires insurers to use a current discount rate to value liabilities. Many respondents described the measure as costly and unnecessary. A sector head at a P&C insurer in The Netherlands said: “The very large investment in IFRS 17 adds little benefit but needs major investments by the insurance industry.”

A specific concern is the risk that new regulation will tilt the playing field away from traditional insurers with their heavy legacies towards more lightly weighted new entrants. Regulation might hamper older companies’ ability to adapt at a time when the industry is striving to transform itself. David Perez Renovales, director general of Linea Directa Aseguradora in Spain, said: “Regulators and supervisors do not seem to be aware of or aligned with the challenges and changes that the sector has to face in technology developments and the evolution of demand, habits and behaviour of consumers”. The chief risk officer of a Belgian composite insurer said: “The risk is mainly that such measures will slow down our transformation and limit our agility.”

Insurance supervision and regulation and the way it is applied across the board has already resulted in squeezing smaller companies out of the market as these companies find it increasingly difficult to digest the related bureaucracy and cost. This is particularly so in jurisdictions where rules are applied strictly (e.g. Germany, Austria). The ultimate goal of protecting policyholders is somewhat counter balanced by fostering concentration in the market and the creation of oligopolies. It is fine to have national (European) champions but there should be competition from local smaller insurers.

Chairman, P&C insurer, Austria

However, a number of respondents said that regulatory reform would ultimately benefit the insurance industry by improving its strength and reputation – even if change might take a number of years. A respondent from the Philippines said: “I think this is good for the industry and also for clients. Only reputable and stable companies will be able to comply”. Robin Low, a non-executive director of AUB Group, said of the recent Australian Royal Commission reforms: “[They] could have quite a high impact, but it is also an opportunity for those companies which want to show leadership.”

Is IFRS 17 worth it?



5. Investment performance (5)

Score: 3.52 (3.60)

Difficult investment markets feature heavily in the outlook for the insurance industry, and concern on this front remains high, though the risk score has slipped slightly because insurers are taking action to mitigate it.

Many respondents made the point that investment income is a key contributor to profits, though the low returns of recent years have forced insurance companies to earn more from their underwriting activities. Andreas Bachofner, director of Shires Partnership in the UK, said that “investment returns will not make up for poor underwriting. There should be more pressure on quality underwriting with a more long-term view.”

Respondents were concerned that low investment yields were encouraging insurers to take greater investment risks to raise their returns. The head of life and health products at a Canadian life company said there was still “over-investment in high risk assets. We are in bubbly times.”

For many respondents, the risk of a further downturn in the markets remains high. Owais Ansari, deputy chairman of FWU AG in Germany, said that “frequently recurring periods of high volatility in the global stock markets (driven by a variety of factors i.e. trade wars, Brexit, political uncertainty) [are a high risk]. For a long-term-focused life insurer, these repeated market shocks result in planning uncertainty and loss of confidence of the policyholders.”

In Japan, the deputy manager of a large life company said: “In the past, most of the cases where life insurance companies went bankrupt in Japan were [caused by] losses on asset management, and it is believed that the impact will continue to be significant.” But there was greater optimism in other quarters. The chief financial officer of a UK non-life company said: “I think this is a lower risk after the financial crisis especially for P&C companies, who have taken on low risk assets. Returns have also been lower, but the risk of loss is also lower.”



6. Climate change (-)

Score: 3.45 (-)

Climate change is seen as a much more urgent threat to the insurance industry than four years ago, when it ranked in the bottom half largely because it was considered a long-term risk. This year, it would have placed even higher up the table but for the perception that it has little impact on the life side of the industry, which had it at No. 19. It was No. 3 for P&C insurers and No.2 for reinsurers – and many respondents saw it as the top threat beyond the near future.

A common theme was the growing economic destructiveness of extreme weather events, including hurricanes and typhoons, floods, droughts, and wildfire. The president of a P&C insurer in Canada said: “The frequency and severity of events has more than doubled in the past 10 years and is expected to continue to increase as global temperatures continue to rise. New flood products have not been fully tested for price adequacy and wildfire risk is growing as well without models to assist in measuring exposure”.

**Low yields
driving a
higher risk
appetite**

**Climate
change - big
for P&C and
reinsurers**

“A 3 degree world may not be insurable”

Christoffel van Riet, board member and chief operating officer of Klaverblad Verzekeringen in The Netherlands, said: “It is not just about an unexpected hail storm. It is about a possible substantial change of the fabric of our societies as a result of potential massive migration driven by climate change invoked food shortages”.

Several respondents made the point that as a consequence of climate change, some risks will become very difficult or impossible to insure. Lisa Guglietti, chief operating officer P&C Manufacturing at The Co-operators in Canada, said: “The escalation in trends and volatility will challenge the sustainability of traditional insurance products unless we start putting more focus on prevention as opposed to indemnification. Many clients are unable to afford the risks that they are exposed to, and more alarmingly many of these same clients are unaware that they have this exposure”. The chief actuary at a P&C insurer in New Zealand said: “In the short term this looks like greater use of risk-based pricing; however, as the response evolves there will be more restrictions and potential withdrawal of cover”.

Massive over the long-term. A 3-degree world may not be insurable.
Chief executive, P&C industry, New Zealand

Moreover, the additional uncertainty about the frequency of catastrophic events is “breaking actuarial models”, as one respondent put it, particularly in the reinsurance industry. A respondent in India said: “If Global Warming increases the number of disasters, reinsurance pricing could produce shocks for the insurance industry”. A regional chief executive of a Chinese reinsurer said: “Many P&C insurers are not taking out adequate reinsurance protection as they want to reduce the cost of protection. This may result in sizeable financial impact to their capital”.

Respondents who ranked this risk lower were overwhelmingly from the life insurance industry, which had it close to the bottom of the table. One said: “There’s no direct risk for the life insurance industry. Indirect risk as it may impact financial markets”; and another: “As we are life insurer, our primary risk from climate change is in our investment portfolio”.

Another question which affected its ranking is how much time insurers have to prepare for climate change. A respondent in the UK said: “In the next few years, it will continue to worsen extreme weather events, but to a manageable extent”. But others were already seeing notable impacts on their business. A respondent in the Philippines said: “Change in weather has greatly affected the way we underwrite risks. We have seen a shift in the direction of typhoons lately. We have had to change some of our business modelling because of this”.



7. Competition (8)

Score: 3.44 (3.49)

The question of whether the insurance industry will be able to meet the challenge from disruptive competition is one that probably attracted more comments than any other in this survey, and much disagreement.

Many respondents argued that the primary threat of disruption comes from the large technology companies rather than the Insurtech industry. “Digitization of distribution access is allowing powerful new entrants in... we should fear the technology giants”, said a respondent from the life insurance sector in Japan. The chief executive of an insurance broker in Canada said: “Current insurtechs are too small and too inexperienced to impact the industry. Bigger players like Amazon, Google and such

Where does competition really lie?

could do it. Insurtechs have little capital and only provide one piece of the solution. They get bought out by current industry players with capital. Not too scary for now”.

Respondents noted other significant barriers to gaining scale. “Regulatory mastery is a high hurdle. Most innovation is focusing on processes not entire business models”, observed a sectoral chief executive at a large US insurer. Greg Tacchetti, chief information and strategy officer at State Auto Mutual Insurance in the US, said: “In the next 2-3 years, I see a popping of the current Insurtech bubble; there's too much money chasing too many good but not profitable concepts”.

But others argued that technology-driven start-ups pose a considerable threat to incumbents. The managing director of a P&C insurer in Belgium said a main risk to the industry is “new entrants supported by private equities or huge corporates willing to diversify their businesses. Data will make the difference, and the companies holding them are able quite easily to develop their own predictive models and propose very adaptative products (financial institutions sliced & on-demand).” For many respondents, the question was not whether some Insurtechs will succeed, but whether it would be as competitors to or partners with traditional players. (see box)

One of the reasons this risk does not rank higher is that, on balance, many see new competition as a net benefit to the industry. The chief executive of a pension company in Denmark said: “Margin pressure and competition from non-industry players and disrupters are challenging the old established industry, but also keeping us on the toes and forcing the old industry players to be more innovative and agile, which will benefit customers”.

On the other hand, the chief executive of a P&C insurer in the UK said: “Disruptor competition at uneconomic price points = more medium-term pain until they exit or have to raise prices to profitable levels”. A respondent in Hong Kong said: “Business models are deeply flawed in many cases (how much term assurance do they think they will sell?), with the risk of detriment to customers and undermining the sector as a whole”.

Will Insurtechs partner with incumbents?

“I don't believe that insurtech industry is a very large threat for insurers. It is still all about transferral of risk. Insurtech does not replace insurance, it is a tool used by insurance.” **Actuary, Netherlands**

“We see Insurtech more and more focusing on parts of the value chain and looking for distribution capacity (to be found at insurers). So less a disruptive force, more as partners.” **Chief executive, composite insurer, Belgium**

... Or compete with them?

I think some insurers will dismiss insurtechs as not having the "all in" ability to perform. And that would be a mistake. **Chief financial officer, composite insurer, Canada**

The insurtech industry will become the insurance industry for risks that can effectively use public data for underwriting. **Chief executive, life insurer, US**



8. Human talent (9)

Score: 3.44 (3.40)

Shortage of talent in the US?

The risk that insurers will have difficulty attracting and retaining talent continues to climb the table, up from No. 15 four years ago. It was particularly high in North America, at No. 4.

A persistent concern was that insurance is being shunned as a career destination by talented graduates in favour of alternatives such as banking and technology. Comments about the industry included: “conservative and old fashioned”, “old hands at the wheel [and] failure to make the business interesting to the young”, and “bureaucratic institutions which stifle personal initiative”.

The chief financial officer at a P&C insurer in Malaysia said: “Millennials are impatient and may find the regulatory constraints in the industry limiting their ability to innovate and speed to market”.

A particular worry is that demand is most urgent for the types of technical roles where there are skills shortages – such as data scientists, actuaries, and regulatory specialists. The vice president of audit and risk at a Canadian insurer said: “Most people fall into insurance, not by choice. The image of the insurance industry presents challenges to attraction and recruitment of talents, particularly in fast-paced field such as technology, data science and quantitative risk management”. A respondent in Hong Kong asked: “Have you tried hiring an IFRS17 expert?”

Another factor seen to be weighing on the industry is the loss of experienced people. An executive director at an insurance broker in the UK, said: “Pressure on costs is weighing more heavily on individual employees with increased risk of burnout without any commensurate material compensation. Years of ‘soft markets’ have also seen a drain of experience as ‘more expensive individuals’ are culled and with them irreplaceable knowledge”.

We have been operating for decades with a shallow bench and it is starting to take its toll. We have an aging pool of experts that is fast dwindling.
Michael F. Rellosa, Executive Director, Philippine Insurers and Reinsurers Association

Rating this risk lower than most, the chief executive of a life insurance company in South Africa said: “The problem is not attracting and retaining talent in the industry. The problem is retaining talent in a particular individual business”.



9. Macro-economy (7)

Score: 3.40 (3.49)

The level of concern about the world economy has fallen slightly since the last survey two years ago: respondents see plenty of potential threats to growth but these have yet to materialise.

The dominant concern is that political tensions will set off trade wars at a time when economic conditions are fragile. Burcin Arkut, chief actuary at Aviva Turkey, said that the “global economy will face its biggest test since the last financial crisis leading to headwinds for the insurance industry.” Respondents saw signs of fragility in

overvalued markets and in the strong growth of credit and leverage in the banking system.

A particular concern was that softer conditions would force central banks to hold down interest rates, prolonging the low yield environment which has bedevilled the insurance industry for several years. “The maintenance of returns is a risk given the current interest rate scenario, the uncertainty about economic growth, and commercial tensions that do not seem to decrease”, said the Finance Director at an insurance mutual in Spain.

But would a more difficult environment be good or bad for business? Although many respondents saw a downturn hurting premiums, others were less pessimistic. The chief executive of an insurer in Luxembourg said that “the current environment is bad from an economic / political perspective but the fear factor is good for the insurance sector as clients are looking for secure / safe solutions”. A respondent from India said that “Safety as a virtue assumes maximum importance during times of macro-economic uncertainty. Hence I feel it actually could serve as a good environment for insurance and hence do not see it as a stress.”

The level of concern about economic risk varied with geography. The region with the highest concern was Africa where it ranked No. 2. Ian Visagie, chief financial officer at Sanlam Personal Finance in South Africa, said: “Locally the uncertain political and economic climate will in all likelihood continue and have a negative impact on investment business, as well as the return earned on assets.” Despite anxiety about China, the Far East region was the least concerned, placing macro-economic risk at No. 14. The senior director of a Hong Kong-based life insurer said that “life insurers are typically quite sturdy and can cope with economic change pretty well.”

Other regions gave this risk a middle score, including North America. A respondent in the US said that the economy “is on a good path, but global macro is introducing risk”. In Canada, a chief risk officer reported that “the current economic environment is a positive one for our business.”



10. Interest rates (4)

Score: 3.36 (3.65)

Concern about interest rate risk is receding, mainly because the insurance industry - in particular the life side - is learning to live with a low interest rate environment. The risks have historically lain with excessive dependence on investment returns to sustain profitability, and on savings products that offer a guaranteed return.

A regional chief executive at an insurer in Luxembourg said that “insurers used to bank on making healthy returns, in order to make a profit. This enabled them to write to combined ratios of well over 100%. This has stopped and therefore I do not see much impact of continued low interest rates.” James Davenport, senior vice president, Finance, Mutual of Omaha in the US, said that “life insurers have gotten used to a lower rate environment and can now better operate with rate uncertainty.”

However, there are still areas of the market which are seen to be vulnerable, particularly if low interest rates persist or if there are sudden changes. Nelson Machado, CEO Life and Bancassurance at Ageas in Portugal, said: “A big change can be a significant risk, but today’s level is also a relevant issue.”

Learning to live with low interest rates?

Respondents were divided over whether the next move in rates would be up or down. If it is up, the pressure on insurers' balance sheets and P&L accounts would ease. There would also be a reduction in competition as new investment opportunities opened up for mobile capital. But if they stay low or even sink, market conditions would become more difficult. The chief financial officer of a Hong Kong insurer commented: "The pattern of gently rising rates may already be over. Time to put the champagne corks back in the bottles."

The head of risk management at a German composite insurer said: "The 'Japan scenario' of low interest rates for a very long time is becoming more and more probable for the European economy as well."



11. Political risk (11)

Score: 3.36 (3.29)

Concern about political risk is on the rise. Although the ranking remained unchanged, the risk score has risen. At the global level the risk of trade wars and protectionism is seen to be growing, particularly between the US and its major trading partners, with a potentially damaging effect on financial stability and market growth. The regions where concern about political risk is strongest include the Far East and North and South America.

President Trump's presidency was widely seen by respondents as a threat to economic and political stability, encouraging populist politics of a kind which often targets the insurance industry, such as mandated insurance and rate capping. Other risks that were mentioned included restrictions on foreign ownership of insurance companies, the politicisation of sensitive areas of insurance such as medical, and taxation.

Thomas C. Wilson, chief risk officer at Allianz in Germany, said that "Populism-driven political risks are challenging long-standing allegiances (WTO, NAFTA, NATO, the EU, Brexit, etc.). This is enough to disrupt the real economy and therefore is likely to be a strong contributing factor to the next systemic crisis."

Elections in major countries are also a focus for concern, including the US, India, South Africa and Indonesia where greater protectionism could be an outcome. Respondents from Australia were concerned about the recommendations of the recent Royal Commission on financial services which include an extensive overhaul of business conduct in the insurance industry. A non-executive director of an Australian insurance broking company said that political interference "is in full swing".

Political risk is, however, geographic and respondents from a number of territories said this was not a major factor. Philip Woo, chief risk officer at Tokio Marine Life Insurance in Singapore said: "Although geopolitical risks have risen, the situation in Singapore is still relatively stable. Of course, insurers will still be indirectly impacted by the broader changes in other countries, but I do not see the knock-on effects to be that large."



12. Cost reduction (13)

Score: 3.32 (3.26)

The challenge of reducing – or simply containing – costs continues to grow as new pressures bear down on the industry: competition, compliance, IT, rising claims etc.

Many respondents were sceptical of the industry's ability to meet this challenge, burdened as it is with legacy systems and a culture which tends to accommodate cost rather than confront it. Len Elikhis, chief officer, Product and Vitality, at AIA in New Zealand, said: "I expect to see unit costs rise across the industry, at least in the short to medium term, to respond to the regulatory agenda, the implementation of IFRS 17, and ongoing investment into technology."

Respondents feared that failure to contain costs would lead to further consolidation and the loss of competitive strength against new entrant businesses. A particular concern was that insurers would pass rising costs on to consumers and harden their growing resistance to insurance purchases. The actuarial superintendent at a Brazilian P&C insurer said: "The main concern is that the industry will not automate its processes and will not therefore reduce its administrative expenses. I believe this process is fundamental so that savings can be passed on to the policyholder and improve the customer experience. This means changing one's mindset from the self-centric to the customer-centric model."

Not all the responses were as pessimistic. The head of investor relations at a large French life company said: "Most insurers have implemented and continue to implement efficient cost reduction programmes." An Australian reinsurer was less complementary: "Collectively they all make such a poor job of it that all are shielded."



13. Reputation (17)

Score: 3.26 (3.17)

Though reputation risk remains in the bottom half, this is by some distance the highest ranking it has ever been assigned, and it reached No. 6 in Asia.

One reason is the growing fear that insurers' reputations could be seriously damaged by misuse of data, actual or perceived. A risk manager at an insurance company in The Netherlands said: "Definitely now that insurers are gathering more and more data, there is significant reputational risk fanned by scandals surrounding Facebook and Cambridge Analytica, Google, etc, and more broadly speaking the increasing suspicion towards 'surveillance capitalism'".

[A main risk to the industry is...] a breakdown in trust between customers and their insurers - driven primarily by pricing practices; which could be down to regulatory or other intervention on the issue of 'loyalty pricing', or because of a rejection of the amount and sources of data being used to price products in a way that is (at best) far from transparent, and (at worst) seen as being unfair.

Chief executive, P&C insurer, UK

While social media is no longer new, many respondents noted its ubiquity as a threat when the public is already inclined to view insurance negatively, and isolated incidents of bad behaviour could lead to a loss of confidence in otherwise credible providers. "We always look bad in public... it's impossible to explain insurance principles in a social media context", said the managing executive of a South African insurer.

But respondents also made the point that the industry is not helping itself by failing to respond to changing expectations and social values. "Social media could present a risk if, on a large scale, it started to put its focus on the actual quality (speed, accuracy, service) of the insurance industry, which as a whole and compared to other sectors remains poor", said the managing partner at insurance broker in Luxembourg. A

**Reputation
risk is still
low - but
rising**

respondent in Belgium said: “Public values are moving to more eco, more socially responsible behaviour, more fairness in customer treatment, so bad profits have to be revolutionized by the industry itself to prevent a poor reputation.”

This risk does not rank higher in part because social media is also seen as an opportunity for insurers. “Human need for protection of lives and assets will continue so consumers will increasingly move to more trusted insurers, enabled by more information and easier ability to change, in environments where brands are damaged by businesses not doing the right thing”, said a consultant in Australia.



14. Guaranteed products (10)

Score: 3.22 (3.37)

The difficulties created by insurance products which were sold with guaranteed returns are seen to be easing as insurers adjust their books and phase such products out.

A UK respondent said: “The risk was far greater when interest rates were falling and then stayed low. Nearly all insurers who were affected have now either fully reserved for the loss or suffered the loss.”

However, some respondents felt that risks were still present. The uncertain outlook for interest rates remained a threat for insurers who were still exposed, and for those who continue to depend on such products. A senior insurance director in Hong Kong said: “In Asia in particular many insurers do not fully understand the guarantees they underwrite and how damaging they can end up being. Industries in Korea and Taiwan have learned the lesson the hard way.” An actuary in Japan said that “generous guarantees have been causing problems for Japanese insurers for over two decades.”

In Europe, some concern was expressed about countries such as France, Germany, Portugal and Italy where exposure to guaranteed-return savings products remains considerable. The chief executive of a life insurer in Luxembourg said: “The risk will further increase, should the interest rates increase considerably over a short period of time”.



15. Business practices (12)

Score: 3.22 (3.28)

The risk that insurers will incur losses as a result of poor sales and other conduct of business practices has fallen down these rankings in recent years, since hitting No. 4 in 2013. The tone of comments we received suggests that this may hint at some complacency.

Some respondents though that insurers are improving in this area. A respondent in New Zealand said: “Insurers are responding to poor conduct and culture findings. This will take some time but will improve the situation”.

But others felt that as competition in the industry increases and squeezes margins, insurers might be increasingly tempted to gain an edge through questionable practices. The chief internal auditor at a life insurance company in Canada said: “Canada has historically had much better results in this regard than other countries... are we really

“... historical redress...”

that much different? Would increased transparency of advisors’ compensation start to surface issues? Will the drive to have more innovative products and increased risk appetites create conduct concerns?”

A key question is whether insurance business practices are keeping up with societal expectations and regulation. The chief financial officer of a life insurer in the Philippines said: “With increasing consumer activism and introduction of new regulations (e.g. data privacy), insurers may face more scrutiny and be subjected to larger fines and regulatory costs”.

More stringent regulation was seen by many as tempering this risk by curtailing future transgressions, but also increasing the risk of losses through historical redress. A number of respondents mentioned the Australian Royal Commission. An actuary in New Zealand said its consequences could include: “the cost of identifying and rectifying any cases where customers were not fully aware of any limitations in coverage or lifetime cost exceeds premiums paid, particularly if there was pressure selling to customers of limited means”. But another respondent said: “The resolution of the findings from this scrutiny and responding to this risk will force insurers to work out how to be more socially relevant and may even strengthen their customer value propositions in the medium term.”



16. Quality of management (14)

Score: 3.17 (3.26)

While there were areas of concern around business and risk management, these were generally not priorities for respondents to this survey. Nevertheless, this Banana Skin was ranked No. 7 in Asia Pacific, and No. 9 among reinsurers.

We received several comments that noted improvements to risk functions – for example, because of increased regulatory scrutiny around conduct and individual accountability. A non-executive director at a P&C underwriter in the UK said the industry was benefitting from: “Better internal and external regulation, and growth of chief risk officers – though there will always be the possibility of the odd ‘rogue’ company”. The chief executive of an insurer in Singapore said: “Multinational insurers have strong structures and processes in place which will not easily fail. New, smaller insurers might face the risk of short term thinking and insufficient controls in place”.

One potential area of conflict could be between the need for rigorous risk management and business innovation. William McDonnell, group chief risk officer at RSA Insurance Group in the UK, said: “Risk management in the sector is good, but the challenge is managing the tensions and trade-offs between tough business challenges and risks”. On the other hand, a departmental head of a reinsurance company in the US observed that: “some insurers staff their enterprise risk management departments with people who don’t pose a threat to the business”.

The chief executive of a Canadian insurance brokerage said: “With the new pace of change, executive teams must not be afraid to turn to younger generations to come up with more innovative strategies. Leadership teams still stuck in the old ways of thinking will fail, and not see the train hit them head on. Unfortunately, many young leaders are thinking ‘old-style’. It will take some time for the industry to change”.



17. Credit risk (-)

Score: 3.14 (-)

Credit risk is a growing concern so, for the first time in this survey series, we asked respondents to rate it. It came relatively low down the list, but the responses showed it to be a risk with many forms, all of which would be vulnerable to a downturn in the credit markets.

Some respondents felt that the uncertain economic outlook made credit risk one of the most important issues for the insurance sector. The head of audit at a Swiss insurer said: “The credit cycle is coming to the end of a rotation and accordingly we can expect an increase in credit spreads and deterioration in credit quality. This will have a direct impact on the balance sheet of insurance companies, particularly those exposed to long-term life business.”

The forms of credit risk mentioned included:

Counter-party risk: the risk that clients and agents will default on their obligations. A composite insurer in Malta said that “in a market that offers considerable credit to clients/intermediaries, companies could be faced with credit default risk especially if the economic environment takes a sudden downturn.”

Reinsurance risk: another aspect of counter-party risk. Many insurers have laid off their underwriting exposure with reinsurance companies. A Canadian respondent said that “credit concentration in the reinsurer presents the primary risk from a counterparty risk perspective.”

Underwriting risk: the insurance of credit risk is a growing business. How will it fare in a more difficult economic environment? A respondent from Australia said: “For those lines covering credit protection, clearly this would be big. But less so for other lines.”

Investment risk: Insurers have credit exposure to companies and public bodies through their investment in bonds and IOUs. The quest for investment returns may have driven them towards lower quality paper.

One concern is that that the new mark-to-market regulations would force insurers to take losses on their credit assets even if they were holding them for the long term, thus amplifying the risk.

The more optimistic view expressed by respondents focused on the prudence of risk management. A Dutch insurer said that “[credit] is a risk, but because of lessons learned in the past and the role of the supervisors, this threat is well being managed.” Others observed that the diversified investment portfolios of most insurers will help mitigate this risk.



18. Social change (16)

Score: 3.11 (3.17)

The insurance industry’s ability to meet the challenges of social change, such as the growing demand for health insurance, pensions etc., is viewed with some optimism. However this is a complex area where actual outcomes will depend on policies adopted by the state sector with which it is closely allied.

What will longevity mean for affordability?

The majority of respondents thought that the industry is keenly aware of these issues, and actively addressing them by designing products and preparing the market. Many even described this as an area of opportunity rather than risk. A Spanish mutual insurer said: “The sector is adapting and is becoming more agile in designing products to meet needs.”

The difficulty lies in devising an approach that ties in with services supplied by the state. An insurance regulator described it as “a big issue, but a risk to society rather than to the insurers.” There is also the risk that governments may oblige insurers to provide these services on stated terms.

A further issue is affordability: products based on a market of growing longevity will likely cost more than consumers are able or willing to pay. The risk officer of a UK insurer said: “The risk is not insurers failing to meet social pressure, the risk is unaffordability for a significant part of the population”.

Aging society and the pressure on current government-sponsored health and pension plans will create opportunity for insurers, but with products that will have longer tails that require additional reserves and put pressure on net interest income in a low to negative interest environment.

Head of distribution, Japan.

Many of the issues in this area are localised. A respondent in the Philippines said: “The Philippines is still a very young population. Therefore, social change may not have an impact as compared to other countries.” But the chief risk officer of a China life company said: “China faces the pressure of a population aging for the next decades, and this pressure is still increasing. Insurance funds may not be able to afford the growing pension and medical expenses under a low interest rate environment.”



19. Corporate governance (19)

Score: 2.98 (2.97)

Corporate governance ranks low down the table. The general feeling is that regulatory scrutiny and more focus on governance internally have led to significant improvements since the financial crisis.

The chief executive of a life insurance company in Japan said: “In terms of governance (control structures and oversight structures, lines of defence, avoiding conflict of interest, etc.) this time is better than any time before us. We remain dependent, though, on competent people”. In Bermuda, a board member at a P&C insurer said: “Demands on board oversight are greater than ever, with activism continuing to grow and risk evaluation expected to transcend the C suite”.

Some respondents were concerned that boards might be overly cautious, and consequently restrict innovation. Peter Beaumont, finance and operations director at Cornish Mutual in the UK, warned that: “Governance obligations can drive risk aversion. Boards are often quoted as the main barrier at innovation conferences.” The director of operations at a composite insurer in Brazil said: “All international companies have good corporate governance. The risk is to become more complex and have slow decisions, that could be crucial to compete with new entrants and start-ups”.

For some respondents the composition of boards was an issue, including a lack of diversity and specialist technology skills. We received comments about “an old boys’ network”, “products of a historical environment” and boards that are “ethically old-school”. The director of an insurance broker in UK said: “The skill base and mix of skills on boards of directors of insurers is sometimes inadequate, inappropriate and imbalanced. Some folks sitting on boards should not ever have been allowed to become an approved person”.

The regional chief risk officer of a composite insurer in Singapore highlighted governance risk in joint ventures. “The industry is partnering up with non-traditional players sharing very distinct governance principles with the risk of cultural and risk appetite conflicts”, he said.



20. Capital availability (20)

Score: 2.79 (2.91)

The continuing surplus of capital in the insurance market is among the least of the industry’s worries. While it creates soft conditions and encourages risk-taking, it is also welcome at a time when capital requirements are being tightened by regulators, and economic conditions are becoming more fragile. The chief auditor of a large Canadian life company said: “Excess capital will be beneficial given certain headwinds in the financial markets”.

Sloppy risk-taking and many factors that are hard to quantify and require prudent judgement are overlooked when capital is too easily available.

William Fischer, chief executive, Harrington Reinsurance, Bermuda

Some saw excess capital as a reputational rather than financial issue. The chief actuary of a New Zealand insurer said: “[This is] largely a reputational risk if capital is seen to be underperforming and therefore not providing value to investor or policyholders.” The chief risk officer of a US life company said: “[This is] a growing concern for our company; we need to put capital to work.”

The chief risk officer of a US reinsurance company was optimistic: “It will slowly erode away by fierce competition, in my opinion.”



21. Brexit (22)

Score: 2.66 (2.52)

Brexit - “a non-event”?

Despite all the noise made about it, Brexit is almost a non-event in the international insurance market. Most of the respondents outside the UK and the EU doubted that it would have much market impact, other than possibly causing ripples in the financial markets, though even here many said the event was well-anticipated and prepared for. Insurance is still overwhelmingly a domestic business.

The chief risk officer of a Bermuda-based insurer said that “the uncertainty has already been baked in and most organisations have had to make contingency plans; the downside risk is now contained.”

The greatest concerns came from the UK, where insurers said that the loss of direct access to the EU market would damage existing business and hamper growth. One respondent this “will be a disaster all round”. Others noted that Brexit would add a

layer of cost to companies in the affected businesses. A number of respondents noted that an important question would be the UK regulators' response. Would they, for example, water down or beef up Solvency 2?

Several respondents even saw Brexit in a positive light. A reinsurer in Bermuda said it was "both a risk and an opportunity", while the chief actuary of a Brazilian life company said that "I truly believe that the UK will be able to deal with this challenge."

Appendix I:

Insurance Banana Skins: The Top Ten since 2009

2009	2011	2013
1 Investment performance	1 Regulation	1 Regulation
2 Equity markets	2 Capital	2 Investment performance
3 Capital availability	3 Macro-economic trends	3 Macro-economy
4 Macro-economic trends	4 Investment performance	4 Business practices
5 Too much regulation	5 Natural catastrophes	5 Natural catastrophes
6 Risk management	6 Talent	6 Guaranteed products
7 Reinsurance security	7 Long tail liabilities	7 Quality of risk management
8 Complex instruments	8 Corporate governance	8 Quality of management
9 Actuarial assumptions	9 Distribution channels	9 Long tail liabilities
10 Long tail liabilities	10 Interest rates	10 Political interference
2015	2017	2019
1 Regulation	1 Change management	1 Technology
2 Macro-economy	2 Cyber risk	2 Cyber risk
3 Interest rates	3 Technology	3 Change management
4 Cyber risk	4 Interest rates	4 Regulation
5 Investment performance	5 Investment performance	5 Investment performance
6 Change management	6 Regulation	6 Climate change
7 Guaranteed products	7 Macro-economy	7 Competition
8 Distribution channels	8 Competition	8 Human talent
9 Natural catastrophes	9 Human talent	9 Macro-economy
10 Quality of risk management	10 Guaranteed products	10 Interest rates

Some risks come and go, some are hardy perennials, as this chart of the Top Ten Banana Skins since 2009 shows.

The last two editions of this survey show clearly that the industry has shifted its focus to risks related to technology – due both to rapid changes in the external environment and an urgent need to modernise internal IT systems and business models. These trends appear set to continue with the transformation of insurance markets by automation and modern distribution channels, and the pervasive threat of cybercrime.

Regulation – the top risk in 2011, 2013 and 2015 – continues to rank highly as insurers grapple with its volume and cost. Another major issue is investment performance, which burst into No. 1 position during the crisis in 2009 and has remained in the top five ever since. Initially driven by the market crash the concerns are now about the persistence of low yields. Concerns about the macroeconomic environment and interest rates, which have been high in recent surveys, have receded a little this year.

Among governance risks, the quality of management and boards started high but has gradually fallen down the list, and is now generally seen as lower order – reflecting the view that insurance companies are increasingly better run. Risk management was a significant concern in the aftermath of the crisis, but has since seen improvements.

Risks which are seen to be rising sharply – and ones to watch out for in future surveys – include climate change, with a growing perception that it is making some markets difficult or impossible to insure. Competition, both from technology giants outside the insurance industry and Insurtech start-ups, is attracting a great deal of discussion. The industry's ability to attract and retain talent – especially in technical roles – is also climbing up the top ten.

Appendix II: The questionnaire

Insurance Banana Skins 2019 A CSFI survey

Biennially, we ask senior insurers and close observers of the financial scene to describe their main concerns about the insurance industry as they look ahead. We'd be very grateful if you would take a few minutes to complete this latest survey for us.

Question 1. Who you are:

- Name
- Position
- Institution
- Country
- Which part of the insurance market do you represent?
 - Broking/intermediary
 - Life
 - P&C/Non-life
 - Composite
 - Reinsurance
 - Other (please state)
- Are you willing to be quoted by name?

Question 2. Please describe what you see as the main risks facing the insurance industry over the next 2-3 years.

Question 3. Below are risks in the insurance industry that have been attracting attention. Please score them on a scale of 1 to 5 where, in your opinion, 1 is a low risk to insurers and 5 is a high risk. Use the column on the right to add comments. Add more risks at the bottom if you wish.

Economic environment

1. Macro-economy: To what extent does the current macro-economic environment present a threat to the insurance sector?
2. Interest rates: How large is the risk that insurers will be damaged by movements - or lack of movement - in interest rates?
3. Credit Risk: To what extent does the risk of credit deterioration present a threat to the insurance sector?

Public environment

4. Political risk: How great is the risk that political pressures will damage insurers, e.g. through protectionism, populism, interference in business practices?

5. Brexit: How great is the risk that the UK's decision to leave the EU will harm the international insurance market?
6. Regulation: To what extent could the current wave of new regulation on conduct of business and capital requirements have damaging effects on insurers?
7. Reputation: How severe is the risk that the industry will be damaged by poor reputation or by social media?
8. Social change: How great is the risk that insurers will fail to meet social pressures such as greater longevity and the demand for health care/ pensions products etc.?

Operating risk

9. Capital availability: To what extent is the current surplus of capital a risk to insurance providers?
10. Investment performance: What is the risk that insurers will be harmed by poor investment performance?
11. Change management: How likely is it that insurers will be damaged by inadequate responses to change, e.g. in markets, products, customer demands, distribution?
12. Cost reduction: What is the risk that insurers will fail to achieve the necessary cost reductions to remain competitive?
13. Technology: What is the risk that the insurance industry will fail to address technology modernisation effectively?
14. Competition: What is the risk that the insurance industry will fail to meet the challenge from disruptive competitors such as the Insurtech industry?
15. Guaranteed products: With the low interest rate environment persisting, how much risk is there to insurers' capital and solvency from guarantees in products?
16. Human talent: How likely is it that insurers will have difficulty attracting and retaining talent in the present environment?
17. Cyber risk: How severe is the threat of cybercrime to the insurance industry?
18. Climate change. How severe a risk do you think climate change poses to the insurance industry?

Governance

19. Corporate governance: How likely is it that weakness at board level will lead to poor oversight and control of insurance companies?
20. Quality of management: How likely is it that insurance companies will be harmed by poor business and risk management?
21. Business practices: How high is the risk that insurers will incur losses as a result of poor sales and other conduct of business practices?

Please add other risks that you feel are significant to the insurance industry.

Question 4. How well prepared do you think insurers are to handle the main risks you identified in this survey, where 1 = poorly and 5 = well? Please add comments if you wish.

Thank you

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Aviva	Legal & General
Bank of England	LendInvest
Bank of Italy	Lloyds Banking Group
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