Insight and Intelligence on the 2019 *Rendez-Vous de Septembre*

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DAY 2

MONDAY

THE INSURANCE Insider

MONTE CARLO

Pricing momentum will be contained at 1.1 without fresh loss

Absent a major cat loss, reinsurance market conditions look set to be stable to steadily improving as we head toward 1 January, but will continue to lag the primary and retro markets.

Hurricane Dorian looks to have confirmed its status as a "near miss" for the US cat treaty market and is unlikely to disturb the dynamics at play in the mid-year renewals.

However, when a Category 4 landfall near Palm Beach was forecast market sentiment was fearful, with the ILS market's recovery appearing fragile in the face of a potential $10bn-$20bn event.

The lack of reinsurance capital depletion or major remediation exercises, along with rising capital as bond yields fall and the challenges of pushing price on diversifying risks, point to a likely failure to obtain meaningful across-the-board rate rises.

Instead, significant rate increases will be confined to underperforming lines and clients, or mismodelled perils – paralleling the 2018 reinsurer wins which came in the Florida, California and Japanese wind renewals.

Sentiment has been improving through the year and reinsurers are deploying aggregate in a more discerning way by both market and client. No doubt Monte Carlo will see a blitz of bullish sentiment among the reinsurers which dominate the public discourse at the *Rendez-Vous*.

But market fundamentals do not point to a rapid acceleration of pricing momentum.

Four key areas to watch are:

1. US casualty – Mounting concerns about loss emergence driven by social inflation could lead to accelerating excess-of-loss rate rises and ceding commission reductions to complement the primary pricing correction that has gathered pace through 2019.
2. Retro – The degree of tightness within the retro market as the ILS market struggles after two bad years and amid scepticism on modelling and due to climate change.
3. Wind/wildfire season – Meaningful dislocation in property cat looks possible with one more loss, and >50 percent of US windstorm risk remains at this stage, along with a menacing track that takes Typhoon Faxai near Tokyo, as well as some of the highest-risk months for California wildfire.
4. Continental big four – Swiss Re (+30 percent), Hannover Re (+20 percent) and Scor (+12 percent) all grew meaningfully in Q2, and together with Munich Re they could slow the market if they privilege market share over rates.

State of play

Retro pricing moved meaningfully following hurricanes Harvey, Irma and Maria (HIM) in 2017, and picked up pace sharply at 1 January 2019 (+10 percent to +30 percent) as the ILS market struggled with poor results, trapped capital and redemptions.

Following gradual gains post-HIM, US excess and surplus lines pricing gains started to accelerate through Q1 and have continued through the half-year, with much property insurance business obtaining 20 percent increases, directors' and officers' (D&O) up 10-30 percent and in some cases general liability also able to achieve 20 percent rises.

London market insurance rates have followed a similar trajectory through the year, although there has been a time lag, and

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Key points

- Excess capital is likely to contain blanket reinsurance rate rises unless there is another major cat loss
- Rating momentum still likely for challenged areas/clients
- Market is fearful of another cat-hit year and the fragility of the ILS market means we are one medium-sized loss away from property dislocation
- US casualty reinsurers' response to worsening loss picture as we head into Q4 will be closely watched
- Continental reinsurers have capital to expand and could be a drag on rates if they continue Q2 growth trajectory

INSIDE

SCOR launches its new strategic plan

QUANTUM LEAP
2019/2021

SCOR has now successfully concluded its "Vision in Action" plan, confirming its position as an independent global Tier 1 reinsurer with a "AA-" rating. SCOR has once again demonstrated its ability to combine growth, profitability and solvency in a period of low interest rates, marked by a series of natural catastrophes.

Things are speeding up. The environment is becoming increasingly uncertain and complex, in scientific and technological as well as economic, financial, geopolitical, societal and regulatory terms. In an expanding and changing risk universe, SCOR firmly believes that reinsurance has strong growth potential.

With its proximity to clients, its recognized expertise and its mastery of Life and P&C reinsurance, SCOR has all the vital qualities necessary to meet a growing demand for protection.

SCOR has set itself ambitious profitability and solvency targets in the current financial context. Under the QUANTUM LEAP plan, the Group will pursue its growth while staying true to the fundamental principles that have shaped its success – a controlled risk appetite, a robust capital shield policy, high diversification and a strong franchise - transforming profoundly to create the reinsurance company of the future. SCOR is using new technologies – such as artificial intelligence, robots, blockchain, big data, satellite imagery and multi-cloud… – to innovate, expand its offering and increase its efficiency for the benefit of its clients throughout the world. All of the company's activities are involved, from underwriting to asset management and from risk analysis to claims settlement. All SCOR employees are totally committed to implementing this ambitious plan, which will enable SCOR to fully adapt to the world of tomorrow.

In a changing risk coverage market, QUANTUM LEAP will ideally position SCOR to create even greater value for all its stakeholders.

TWO EQUALLY WEIGHTED TARGETS

HIGH RETURN ON EQUITY

> 800 basis points over the risk-free rates over the cycle[1]

[1] Based on a 5-year rolling average of 5-year risk-free rates.

OPTIMAL SOLVENCY RATIO[2]

Between 185% and 220%

[2] Ratio of Eligible Own Funds (EOF) to Solvency Capital Requirement (SCR) calculated by the internal model.

Is it time to move the *Rendez-Vous* somewhere else?

One of the privileges of being a journalist is being able to float ideas.

Things that aren't yet necessarily fully formed, or which you are not entirely convinced of.

But ideas which you are stress testing and trying to hone, including ones which will be tested to destruction either on the page or by the subsequent reader response.

The idea I would like to float here is that the global reinsurance industry should try holding its annual September gathering outside Monte Carlo.

I want to preface what I am about to say by emphasising that the Principality of Monaco has been a remarkable host for the *Rendez-Vous* for more than 60 years.

Monte Carlo has provided a spectacular backdrop to decades of productive and illuminating meetings, with the Monegasque people welcoming and warm.

Nevertheless, I think the idea of moving the *Rendez-Vous* needs at least to be considered carefully.

Traditions need to be respected, but there is nothing in business where it makes sense to do exactly what has always been done precisely and solely because it is what has been done before.

The status quo needs to be subjected to proper scrutiny and alternative approaches scrupulously assessed.

I think there are two primary concerns which I weigh against the emotional and practical draws of Monte Carlo.

The first is simply cost. The unique charms of Monte Carlo come with a suitably unique price tag.

And with 30-40 cents of each dollar of premium being absorbed by frictional costs, industry leaders must ask searching questions about whether the reinsurance sector can afford its annual pilgrimage to the Côte d'Azur, and whether it is comfortable with the signal that this sends.

My second concern is that returning to the same place every 12 months feeds a tendency towards conservatism, and even the danger of stagnant thinking.

Staying in the same hotels, eating at the same restaurants, looking up at the same olive tree, staring out over the same coastline – all of it tends towards the same outcome.

Your calendar rolls over from one year to the next and so does your approach.

It can feel like a closed system.

I have bumped into the same broker from Aon three years of the last four at or on my way to Nice Airport. We ran into each other again on Saturday.

Each year I have enjoyed seeing him. But it feels like we are stuck on repeat. I do not understand why it is never a broker from Guy Carpenter or Willis Re. It just never is.

I wonder whether by embracing a new city – or better yet a circuit of different cities – the industry would not benefit.

In part, the symbol of openness to change is a good one for a traditional industry to adopt.

But more than that, I think it would be a very different conference if we tried running it somewhere else.

Different cities have different feels and bring different ways of doing things. They help foster new thinking, new approaches and new connections.

Perhaps the industry's elders could even consider a pilot. Like Glastonbury, allow Monte Carlo a fallow year and see if there are any benefits to gathering at Madrid, or Amsterdam, or Paris.

If not, then the pilot could be written off as just that – a failed experiment.

As I said, I am floating an idea here. This is much more a call to thought and serious reflection than a call to arms.

Because I must admit that if the calendar ticked round to the second week of September and I wasn't packing my bags for Monte Carlo, I think I would feel a wave of nostalgic sadness. And I suspect I would not be the only one.

Adam McNeatrie, Editor-in-Chief, *The Insurance Insider*

adam.mcnestrie@insuranceinsider.com

Lloyd's 'follow' status a challenge to strategic vision: QBE Re

Getting Lloyd's syndicates on board as following syndicates will be critical for the Corporation's plans to overhaul its lead-and-follow model, said QBE Re CUO Jonathan Parry.

While he said creating more "follow" capacity was a good idea to help cut costs, the executive suggested that getting buy-in from syndicates to accept this status would be a challenge to achieving this goal.

"How many people will stand up and say, 'I'm a follower'?" asked Parry.

Lloyd's CEO John Neal has highlighted the importance of eliminating duplication among following syndicate capacity as part of the market's broader strategic overhaul.

The initial plans proposed creating new capacity that could be entirely on a follow-form basis – which could also be backed by third-party capital – but implicit is also the need to have existing syndicates providing follow capacity to cut costs and pay lead syndicates fees for their services. Neal has previously pointed to the banking sector as a model.

Meanwhile, at QBE Re the firm has been reshaping its portfolio in response to a tightening market in 2019.

Parry said that QBE Re saw opportunities to expand its retrocession book further in 2020 after doing "a bit more" cover in 2019.

On its retrocession purchasing, the firm has maintained its core protection despite instability in the underlying market. Parry said he was optimistic that as QBE Re had had a largely stable retro panel and paid back prior losses, that the firm would be treated better in 2020 than more opportunistic retro buyers.

He suggested the carrier's Bermuda division could be a possible growth engine in property catastrophe and added that in general, Lloyd's was also being flexible enough to allow carriers to pick up on opportunities from London.

Parry also highlighted opportunity in marine and accident and health lines of business, where improving primary pricing should begin to benefit reinsurers.

Renewals-wise, "Europe is going to be the biggest challenge" for 2020, he forecast, given that non-peak cat reinsurance markets are still inundated with excess supply.

But loss creep from Typhoon Jebi would help to continue momentum for re-rating in the April renewals.

Premia-Standard Syndicate deal challenges Enstar RITC market stronghold

The entrance of Premia into the Lloyd's reinsurance-to-close (RITC) market will provide additional competition in a space which is ripe with opportunity yet has few active players.

On Sunday this publication revealed Premia was set to acquire the Standard Syndicate, edging out a joint bid from legacy carrier Compre and Mike Millette's ILS fund Hudson Structured Capital Management.

If the deal is consummated, Premia would take on Charles Taylor's managing agency and the run-off liabilities associated with Standard Syndicate 1884, gaining access to the RITC market at Lloyd's.

To date the capital supply and pricing for Lloyd's legacy deals has been constrained by the relatively small number of participants.

The RITC market is dominated by Enstar, which executes transactions via Shelbourne Syndicate 2008, however RiverStone and Randall & Quilter are also active in the space. Berkshire Hathaway and Vibe remain in the market but have been largely dormant for years.

Shelbourne is believed to have more than £3bn ($3.7bn) of reserves, after signing four RITC deals with AmTrust for the 2016 and prior years of account for Syndicates 1206, 1861, 2526 and 5820, covering £650mn of reserves.

Enstar has also signed major RITC deals with legacy Novae and Neon, which accounted for a collective £1.26bn of reserves.

The Lloyd's market is seen by legacy acquirers as an area of opportunity, as syndicates seek to rid themselves of significant run-off liabilities generated by the Corporation's performance gap process.

Defunct syndicates could be another source of business, with nine syndicates and special purpose arrangements discontinued for 2019 for a range of reasons.

Lloyd's has more than £50bn of reserves. These for around a decade generated favourable development of broadly 6-9 points annually, but this crashed to 2.9 points in 2017 before recovering modestly in 2018 to 3.9 points.

Given the likelihood that the reserving position has continued to deteriorate as lower rates earn through and casualty loss inflation picks up, legacy transactions could become increasingly attractive to Lloyd's businesses.

Such deals would give carriers finality around their underwriting results, and would also free up additional capital at a time when rates on inwards business are improving and trade capital availability shrinks.

Previously, Lloyd's required RITC deals to encompass all business for a single year of account, but with the Corporation seemingly now willing to consider partial or early RITC deals, a diverse pool of legacy liabilities could come to market.

The opportunity is seen as even more enticing by legacy carriers given that the glut of UK employers' liability reserves has largely been sold off and continental Europeans still seem reluctant to sell their run-off in earnest.

As such, a number of legacy acquirers have shown interest in entering the RITC market.

Armour attempted a complex entry at the end of 2017 in tandem with a bid for the Neon legacy book, but was ultimately bested by Enstar. It subsequently was one of the underbidders for Munich Re's smaller Lloyd's business Beaufort.

Other legacy players, including Catalina and Darag, are also believed to have long-term ambitions to enter the Lloyd's market.

Before entering the bidding for Standard Syndicate, Premia also made moves to enter the RITC space and had secured "shelf" approval from Lloyd's to launch a syndicate of its own.

However, there are costs to doing run-off, and financial as well as regulatory barriers.

Run-off operators tend to have relatively high return hurdles due to the potential downside risks, and for many would-be sellers the increase in certainty or capital efficiency may come at a price.

Wildfire-hit CSAA pays 50% increase on 2020 cat treaty

CSAA Insurance Exchange will pay an average rate increase of around 50 percent across its 2020 catastrophe programme in a new indication of the radical repricing of accounts with wildfire exposure in California, according to reinsurance market sources.

In a statement to this publication, CSAA said it believed the increase paid on a risk-adjusted basis was 16 percent. The discrepancy is believed to reflect CSAA's significantly increased expected loss as a result of a changed view of wildfire risk.

The carrier, which is the Northern California insurance arm of the American Automobile Association, was hit heavily by the 2017 Northern California wildfires and the Camp Fire in 2018. Sources said that CSAA's loss for the Camp Fire was just below $1bn net of subrogation, while the 2017 wildfire loss was around $800mn.

It is understood that CSAA's 2020 cat reinsurance programme, which incepts at 1 January, has already been placed – as in 2018, the carrier has bought cover before the current year wildfire season.

Sources said that across the programme it paid an average rate increase of around 50 percent.

SNL data reveals that in 2018, CSAA's top five reinsurers by gross recoverables were RenaissanceRe Europe, Munich Re, Catlin Syndicate 2003, MS Amlin Syndicate 2001 and Tokio Marine Kiln Syndicate 510.

The renewal is an indication of the impact Californian wildfire losses in the last two years may have on 2020 pricing. The 2017 and 2018 fires, which according to S&P caused around $33bn in insured losses, have driven reinsurers to take a drastically more conservative view of wildfire risk.

A number of insurers in the state booked large wildfire losses last year, with implications for their reinsurance programmes.

Mercury General, which handed $216mn in wildfire losses to its reinsurers in 2018, doubled its cat limit to $589mn when it renewed its programme in July, as well as raising its retention from $10mn to $40mn.

AM Best placed the financial strength rating of California Capital Insurance Company under review in December, after the company went through the top of its $250mn reinsurance programme. It has since agreed to be acquired by Auto-Owners Insurance.

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Primary market dynamics	Reinsurance market dynamics	Retro market dynamics
London market rates up around 5%; US E&S rates up even more	Reinsurance rates modestly firming with harder pockets like Florida, Japanese wind and California	Rates up 20-40% year on year on limited mid-year volumes
Remediation drives from AIG, Lloyd's, FM Global, Swiss Re CorSo, and possibly now Allianz Global Corporate & Specialty	No capital impairments and remediation work has been relatively limited	Markel Catco collapse, trapped capital and redemptions have significantly reduced effective capital levels
Modest increase in cost of capital from reinsurance rate rises, but scope to retain more risk if portfolios are better priced	New capital formation in the form of Convex and a return to capital growth helped by falling bond yields. Biggest players show growth appetite	Damage to credibility and concerns around the impact of climate change are preventing new capital formation for higher-risk strategies
	Increased cost of capital resulting from rising retro prices	

Source: *The Insurance Insider*

an increase of 5 percent or 6 percent looks likely as the renewal rate index for Lloyd's at 1 January, with open market direct and facultative, cargo, aviation and D&O the drivers.

Reinsurance pricing has been much more stable through 2019, with 1 January considered a further disappointment to property reinsurers.

Since then reinsurers have exceeded expectations in Japan, where they were able to secure rate rises of 25 percent on loss-struck wind protections. They followed this up with 10-30 percent rises on Floridian accounts, and then 20-40 percent increases on treaties with California wildfire exposures.

However, crucially these victories were confined to areas with heavy losses where previous assumptions about loss experience had also been called into question by surprising loss development.

And even within these areas there has been a tendency towards differentiation by client, with worse-performing cedants paying bigger increases.

Florida rates also had an additional tailwind as a result of its status as the world's biggest peak risk zone, and the key driver of reinsurance capital.

Contagion into low loss markets like the UK or to loss-free US nationwides was limited, or even non-existent, and as a cedant offering diversifying risk Suncorp was able to escape with a broadly flat renewal at 1 July despite hitting its programme.

To date the casualty reinsurance pricing recovery that began in Q4 2017 has been driven more by original rates than by the reversal of years of increases in ceding commissions.

And, again, the market has clearly differentiated between the better and worse lines and clients.

Primary vs reinsurance vs retro

However, the dynamics within the reinsurance sector differ substantially from the primary markets in the US and London, and from the global retro market.

Both the primary markets referenced and the retro market have seen significant capital withdrawal via either capital depletion or dramatic remediation work.

AIG laid bare the degree of its remediation work on its second-quarter earnings call when it said it had cut back limits deployed through Lexington by half, as well as reducing its overall North American property limits by more than 60 percent.

Lloyd's, meanwhile, has seen dozens of exits from individual lines as part of the performance gap process, provoking a sharp and widespread contraction of available capacity.

And retro has seen both huge amounts of locked capital and the withdrawal of Markel Catco, a circa $5bn player in a $20bn market.

Reinsurance has not only lacked the same capital depletion, but it has seen the reverse, with falling bond yields and retained earnings pushing reinsurance capital 8 percent higher to $559bn by the end of H1, according to Willis Re figures.

The market is also poised for the arrival of Convex, Stephen Catlin and Paul Brand's $1.8bn start-up, which will be fully up and running for 1 January after writing around $25mn of cat business at mid-year.

Continuing excess capital and the relatively low level of contagion to diversifying markets that do not drive capital requirements and to "good" clients probably represent a reasonable predictor that – absent a loss – there will not be meaningful blanket rate rises.

Instead, there are likely to be strong pockets where rate rises are needed, and cedants which are adversely selected against by reinsurers that are focusing their capacity on preferred clients.

Most of the US casualty market, excluding workers' compensation, could fall into this category, as elevated jury awards hit the general liability and healthcare markets, and losses emerge from the opioid crisis and sexual molestation cases.

ILS fragility

Nevertheless, the current market dynamics seem more sensitive to further cat losses than the excess capital position of the market might suggest.

Discussions with reinsurers and brokers as Dorian threatened the Florida coast as a Cat 4 storm suggest the market is fearful of another loss year.

In particular, the ILS market looks to be in a fragile state as it continues to work through the fallout from the 2017 and 2018 losses.

After two years hit by trapped capital, ILS funds and reinsurers with third-party platforms or sidecars badly need to be able to roll over capital into 2020.

Given the way that the trapping mechanism works, even a $10bn-$20bn event could result in significant trapped capital, particularly if it is via a Florida storm where ILS is exposed across a range of different strategies.

Despite a very tight retro market, it has been all but impossible to raise new money to put to work in the sector amid investor scepticism resulting from Markel Catco's collapse, climate change and model misses.

Even with a clean calendar year for cats, with Swiss Re pegging H1 losses at $15bn versus a 10-year average of $31bn, the Eurekahedge ILS Advisers Index shows the market delivering a year-to-date return of -0.71 percent.

Analyst sources said that cat bonds currently have a meaningful positive spread versus similarly graded corporate debt, but are still struggling to attract new interest.

The ILS market has been the biggest driver of the reduction in cat reinsurance rates since 2012, and if capacity in the $90bn market is scaled back substantially then rates would rise.

The Dorian impact on reinsurers will clearly be muted. AIR Worldwide's $1.5bn-$3bn insured loss estimate tallies with the $1bn-$3bn estimates in the market, with the loss likely to skew towards quota share reinsurers of local players.

In the US and Canada, relatively little of the primary losses is likely to reach reinsurers, which tend to pick up losses only in excess of $5bn for a non-Florida storm.

Hurricane Matthew in 2016 showed near-miss events have next to no impact on rates.

Nevertheless, the emergence of Fernand and Gabrielle over the last week demonstrate that conditions are still conducive to storm formation.

Along with the remainder of the period of elevated wildfire risk in California and the typhoon season, reinsurers are a long way from home for 2019.

Dorian: State Farm has most exposure in Carolinas

State Farm, Nationwide and USAA are the nationwide US insurers with the biggest property catastrophe market share in North Carolina, according to SNL data.

Hurricane Dorian caused severe flooding in North Carolina's Outer Banks barrier islands after making landfall as a Category 1 hurricane over Cape Hatteras on Friday morning local time. The storm had maximum sustained winds approaching 90 mph at landfall, the National Hurricane Center (NHC) said.

There was up to seven feet of storm surge from Salter Path to Duck, and areas of southeastern Virginia experienced up to four feet of storm surge, the NHC added. The storm later turned sharply northeast to the Canadian province of Nova Scotia.

In North Carolina, there was $8.4bn of direct premiums written (DPW) across catastrophe-exposed lines last year, of which State Farm had an 11.5 percent market share with $959.8mn of DPW. It was trailed by Nationwide's 9.4 percent share and USAA, which had a 6.3 percent slice.

Though these carriers would typically have high retentions on their occurrence reinsurance covers, Dorian claims would be expected to erode deductibles under aggregate covers that both Nationwide and USAA buy, including cat bond components.

The major carrier that is more likely to have lower-lying reinsurance is North Carolina Farm Bureau Insurance, which has an 8.8 percent share with $735.3mn of DPW.

But while these insurers take a leading role state-wide, market share close to the North Carolina coast will differ significantly and is more likely to feature higher participation from the state insurers of last resort or other cat-heavy writers, which may share more losses with reinsurers.

For example, some Florida-based regional carriers such as Universal P&C, Heritage and UPC Insurance have small market shares in the state.

Universal had a 0.52 percent market share in the state last year, while UPC had a 0.42 percent share, putting them in 35th and 36th place respectively, with Heritage further behind with a 0.18 percent market share.

High-net-worth MGA business Pure had a 0.23 percent share.

Florida-based companies have expanded their businesses outside the state in recent years, in some cases prompted by assignment of benefits issues which have produced a spike in litigated claims.

In 2018 in South Carolina there was $4.9bn of DPW across catastrophe-exposed lines.

State Farm again had the leading market share at 15.6 percent on $4.9bn of DPW, followed by Allstate with an 8.2 percent market share and USAA with a 7.4 percent share.

The South Carolina Farm Bureau Federation, which again is likely to have lower-lying reinsurance, was in 13th place with a 1.6 percent market share.

Several of the Floridians also have a presence in South Carolina, and while Universal's share is smaller in the state at 0.29 percent, UPC has a larger market share at 1.15 percent.

Heritage's market share is similar to that in North Carolina at 0.20 percent.

MGA Pure has a higher market share in South Carolina at 0.69 percent.

South Carolina cat-exposed lines market share 2018

Rank	Company	Market share (%)	DPW ($000)
1	State Farm	15.64	766,746
2	Allstate Corp	8.24	403,973
3	USAA	7.38	361,945
4	Berkshire Hathaway Inc.	5.78	283,246
5	Liberty Mutual	5.53	271,291
6	Nationwide	4.93	241,873
7	Travelers	4.71	230,863
8	Progressive	4.32	211,985
9	Auto-Owners Insurance	2.80	137,527
10	Chubb	2.26	111,055
11	AIG	2.17	106,425
12	Assurant	1.83	89,658
13	SC Farm Bureau Federation	1.57	76,781
14	The Hartford	1.47	71,859
15	Farmers Insurance	1.37	67,055
16	UPC Insurance	1.15	56,158
17	CNA	1.08	52,956
18	Zurich	1.08	52,893
19	Selective	1.05	51,501
20	Tiptree Inc.	0.97	47,384
21	Southern Farm Bureau Casualty	0.92	45,063
22	American Family Insurance	0.86	42,322
23	State Auto	0.82	40,305
24	FM Global	0.82	39,988
25	Munich Re	0.80	39,218

Source: SNL

North Carolina cat-exposed lines market share 2018

Rank	Company	Market share (%)	DPW ($000)
1	State Farm	11.49	959,802
2	Nationwide	9.43	787,759
3	North Carolina Farm Bureau Insurance	8.80	735,295
4	USAA	6.25	521,631
5	Allstate Corp	5.26	439,090
6	Berkshire Hathaway Inc.	4.97	414,920
7	Liberty Mutual	4.52	377,854
8	Erie Insurance	4.10	342,032
9	National General Holdings	4.01	335,282
10	Progressive	3.33	277,966
11	Travelers	3.18	265,303
12	Auto-Owners Insurance	2.43	202,775
13	The Cincinnati Insurance Cos.	1.62	135,541
14	Zurich	1.46	122,340
15	Chubb	1.44	120,359
16	Assurant	1.17	97,697
17	AIG	1.15	96,365
18	CNA	1.14	94,970
19	The Hartford	1.10	91,657
20	MetLife	1.09	90,778
21	Farmers Insurance	1.04	87,247
22	Penn National Insurance	0.89	74,547
23	QBE	0.88	73,700
24	First Protective Insurance Co.	0.80	66,809
25	FM Global	0.79	65,964

Source: SNL

Axa IM doubles down on impact investing

The asset management unit of the French group believes (re)insurers are ideally placed to pursue the investment strategy

Axa Investment Managers (Axa IM) is preparing to launch its first third-party impact investing fund to capitalise on growing interest in the strategy.

The asset management unit of the French group believes that (re)insurers have the balance sheets and risk management nous to increase impact investing as a way of making a difference and addressing shareholder and client concerns about corporate responsibility.

Jonathan Dean, who heads Axa IM's impact investing unit, has travelled to the Monte Carlo Rendez-Vous to spread the word.

"For both reinsurers and insurers, impact investing is a very aligned investment strategy to their core businesses," including the preservation of natural capital, he said.

Environmental, social and governance (ESG) considerations are now mainstream, with the EU mandating the disclosure of sustainable investments and sustainability risks as part of its capital markets union programme.

But where ESG has traditionally focused on excluding certain assets, impact investing goes further, by investing in initiatives that can trigger positive change and measuring their societal or environmental – as well as financial – returns. The impact investing market has grown from $50bn in 2012, when Axa entered the space, to $500bn as of last year, said Dean.

To put that in context, global assets under management came to an estimated $74.3tn in total in 2018, according to Boston Consulting Group. (Re)insurers account for roughly a third of this, according to separate data from Goldman Sachs Asset Management.

Axa IM is not anticipating (re)insurers will overhaul their entire portfolios.

Dean said: "The impact investing market does not expect a material shift in asset allocation from insurers and reinsurers overnight, but even dedicating a small portion of their alternatives portfolio will begin the effort to align capital to address social or environmental issues at scale – whilst not detracting from their target financial returns."

Axa IM has previously established three impact investing funds. Axa was the sole investor at the July, $175mn first close of its third fund, which is focused on addressing climate change and biodiversity, and the cornerstone investor in 2013 and 2016 funds.

The new third-party vehicle aims to raise $300mn to $400mn from solely outside investors. Following its launch in the fourth quarter, its focus will include investments in the field of financial inclusion and healthcare infrastructure and diagnostics R&D in emerging economies.

Dean added: "It's about identifying a problem within society or the environment that is investable and measuring its success in solving the problem. It creates intentionality and accountability."

He stressed that his impact investing operation targets – and achieves – a market rate financial return.

"This is not philanthropy," he said.

Dean added that impact investing is a prudent response to macroeconomic and monetary headwinds.

"We are seeing an increasing market depth in terms of opportunity, which ironically is linked to some of these problems," he said.

"Clearly you have to be nimble across geographies and sectors and across asset classes – and the fact that macro problems are increasing is building the case for impact investing.

"The assets are being invested in multiple sectors – that brings some kind of resilience. This is a multi-sector, multi-asset class, multi-geographical approach."

Axa IM's impact investing operation focuses on private equity, private debt and real assets such as infrastructure.

These "are more consistent with delivering international impact outcomes", said Dean.

"We can invest in a smaller start-up whereas with larger companies the impact of a single investment can be lost.

"It is really about disruption – disruptive technology or disruptive business investments that create a leapfrog effect," he continued.

Dean was referring to the fact that these investments, when successful, can skip a stage in the hunt for solutions, much like mobile telecoms proliferated across Africa before the rollout of landline infrastructure.

Asset managers in the impact investing arena are working hard to identify the best way to assess and measure the investments, with many using the United Nations 2015 sustainable development goals as a framework.

As the sector grows, Dean said there was "increasing urgency about using common definitions and common taxonomies".

He added: "The clearest and most important piece we have to do post-investment is communicate with our investors.

"We're not only reporting key performance indicators – equally important is telling the qualitative story. The reason many look at impact investing is because it is different from traditional investment so we have to bring the investments alive."

Dean dismissed the suggestion that impact investment might be a fad.

"Investors' general behaviour towards impact investing is all moving in the same direction.

"There is so much momentum behind this it won't be in our generation that people suddenly stop caring.

"There might be peaks and troughs in the speed of growth but I can't believe we will wake up and decide that these factors are no longer important."

The executive added that Monte Carlo presents "an opportunity to meet a huge and very important investor base active across asset classes".

"It is about working with important people working on problems affecting our life on a day-to-day basis.

"Impact investing brings us all together on a common goal. It is a very collaborative approach, a new discipline that really builds relationships and breaks down barriers," he said.

Guidance through shifting sands

The CEO of Aon's Reinsurance Solutions business, Andy Marcell, explains how the broker is helping clients navigate the changing dynamics of the market

What will be the key talking points at this year's Monte Carlo *Rendez-Vous*?

There will be discussions around the original rate changes in the market and how long they will hold. Is the shift permanent and, if not, how long will it last?

There will also be talk about what had been a tightening retro market and how that caused reinsurers to change their view of risk, the returns they were looking for and how it's now driving changes in behaviour.

There are two other considerations there – one is revamped funds and the second is ILS capacity and how much will re-emerge in 2020.

But the most common topic will be the changes in original rates, and even though that's very much a US story and Monte Carlo isn't typically a US-centric conference, it will certainly be on everyone's mind.

There will also be talk about innovation and technology and its impact on the industry.

How is Aon's Reinsurance Solutions business positioning itself for continued growth?

We've been growing consistently for several years. Core to what we do is delivering value to our clients and making sure everything we do differentiates us from our competition.

When we look to 2020, we still believe there's a considerable amount of uninsured risk out there so our New Ventures Group, which focuses on areas including government de-risking and intellectual property coverage, is dedicated to generating new capacity and solutions to meet the needs of the risk world.

We've always been innovative as a firm and we will continue to push the New Ventures Group and how we integrate it with Reinsurance Solutions.

The core differentiator for our business remains its scale, its innovation and its commitment to data and analytics excellence as a way of providing value to clients.

For a broking house that doesn't have that quantity of scale and data, it's hard to deliver broad value other than on specific, individual transactions.

What do you make of the talk about reinsurers becoming increasingly tiered and the number of carriers on panels reducing?

I don't think there is a deliberate move to cut the number of reinsurers by clients. If you're a global insurer you have benchmarks in terms of the quality, rating and capital adequacy that qualifies a reinsurer to be an adequate counterparty. Beyond that, global companies are looking for relationships across the breadth of the reinsurance they purchase and they tend to favour companies that feature broadly across those programmes.

> "To be relevant as a reinsurance broker you have to help your clients become more effective in executing their business plan"

Naturally, the ability to offer broad geography and products tends towards the larger reinsurance companies. That's not to say that large companies don't have niche, specific reinsurance needs for certain lines, and they'll also go to companies they see as leaders in those segments.

Regional companies have a different view of their counterparties. They have solvency and capital requirements too, but they tend to utilise brokers to a greater extent to monitor those financial strength metrics. They often want to build longstanding relationships with their counterparties.

Other than providing insight and analytics, structure and advisory services, our job as a broker is wrapped around providing choice to our clients on the execution of any particular transaction.

Is InsurTech an enabler or a disruptor?

Throughout my time in the industry there have been challenges to the traditional model – cat bonds or ILS, for example – and now people talk about auctions and blockchain.

Everyone has a view on technology. Global insurance companies have their own technology initiatives – they have large resources and a number of relationships with technology providers. Lots of those companies are also investors in technology companies.

Companies that don't have those resources can turn to their reinsurance brokers to help them analyse the plethora of providers out there and seek recommendations on which one might be best.

In this regard, we track all the InsurTechs we can and categorise them into distribution, risk selection and efficiency.

Regional companies look more to efficiency and distribution, and they also look for technology to help them select better risk. Global firms tend to follow all this themselves, and if it's an area that's truly innovative they will come and discuss it with us. In some cases we partner with them.

Pushing away from all the innovation would be the worst thing to do. We should embrace it and utilise the elements that are of value to our clients.

Can you tell me more about the client segmentation initiative?

To be relevant as a reinsurance broker you have to help your clients become more effective in executing their business plan.

The best way to do that is to identify a common set of issues around a common set of clients, and to improve the outcomes for those clients by generating a deeper understanding of their needs. That is not just around reinsurance transactions, but everything that impacts them.

For our regional clients, we're thinking about how can we help them solve problems in areas such as healthcare, asset management, pension advice and growth strategies. We have all those tools within the Aon family and our goal is to unite them in a single set of solutions. We call this Aon United. It's not a gimmick, it's real and we're working it hard. We're just doing more things in a better way for our clients.

Andy Marcell
CEO, Aon's Reinsurance Solutions business

Akinova: building the Nasdaq of reinsurance

Akinova CEO Henri Winand wants to open up cyber risk to the capital markets, creating a new growth area within the ILS sector.

His start-up was the first to receive an "innovative intermediary" licence from the Bermuda Monetary Authority (BMA), under new rules introduced last month.

The dream, he explained, is that a broker can do all their 1 January renewals "while on the beach in Florida", through the digital marketplace.

Winand believes that institutional investors have a strong incentive to get more involved in putting capital behind cyber risk.

After all, they already get the downside of the hack.

When Capital One revealed it had been the victim of a vast cyber breach, impacting more than 106 million customers, the bank's share price dropped 6 percent.

The Insurance Insider revealed that the Capital One hack could cost (re)insurers up to $400mn.

"As an institutional investor, you own that risk. But you have absolutely no instrument, no contract, which allows you to participate in the upside," he explained to *The Insurance Insider*. In other words, investors don't see any of the premiums insurers get when hacks don't happen.

The Akinova thesis is built on a world in which these large hacks happen more frequently, and entire industries must grapple with systemic cyber risk aggregation.

He wants cyber insurance to become an asset class like any other. Although the platform will be able to handle bespoke, facultative risks, he believes standardised contracts will be more liquid.

The Capital One hack, along with recent breaches at Equifax, LabCorp, Marriott and BA, illustrates the scale of the challenge facing the cyber insurance market.

"These problems are of significant size – we now need to match that risk to a pool of capital. Those who ultimately own that risk are all the pension funds and all the capital markets players," Winand told *The Insurance Insider*.

He cited the example of a fund manager owning shares in Boeing, Toyota and Glencore – all uncorrelated companies, in different fields, listed on different stock exchanges.

But he argued that large corporates share the same technology and logistics contractors, not to mention financial services.

"The real catalyst for this is if you have some risks that are unprecedented", he explained.

"You need to have some mechanism to go from insurance to capital markets."

His solution is a cyber ILS contract, agreed with market participants, that can be bought and traded in the same way as a traditional cat bond.

He said (re)insurers can cede risk on the platform, creating the prospect of a liquid market in treaty and facultative cyber risk.

Akinova was founded in 2017 by Winand and Jean-Michel Paul, who had tried to do something similar in the 1990s. Paul founded hedge fund Acheron Capital and knows the ILS market well.

"My co-founder has been doing this for 30 years, but was too early," explained Winand.

Other members of the team include CFO and COO Nick Yeates, a former Xchanging executive who worked at insurance software house Xuber, chief technology officer Marcus Marr, who spent two decades in investment banking, and Alex Pike, commercial director, a former army captain who more recently brokered derivatives at Morgan Stanley.

The company has attracted industry figures including XL Catlin veteran Paul Jardine and Securis co-founder Rob Procter to its advisory board.

Akinova focuses on cyber market because it believes it is the future of the insurance industry.

Winand said the rationale for focusing on cyber was inspired by the "Nasdaq approach".

The-then insurgent stock exchange focused on technology stocks in the 1970s and 1980s, despite the market in those securities being far smaller than heavy industry.

Akinova does three things participants need from a trading platform, Winand explained: price discovery, information presentation and accounts, and compliance and settlement.

The InsurTech's "innovative intermediary" designation from the BMA is a new one, introduced this August through the Insurance Amendment Act, 2019. According to Appleby partner Tim Faries, the law introduces the idea of an "insurance marketplace", defined as a platform that enables the "buying, selling or trading contracts of insurance".

"In Bermuda, we are not regulated as a broker, or insurance company," said Winand. "We've done something a bit different".

The London-headquartered startup is currently part of the BMA's sandbox, a kind of regulatory playpen that gives tech businesses a licence to transact.

The company is also in talks with regulators in the UK and the US.

The market is ready to operate, but is not yet transacting business.

Winand's motto is "crawl, walk and run".

"When we come out of the regulatory sandbox in March 2020, then we start walking."

Akinova

Launched: 2017
CEO: Henri Winand
Co-founders: Henri Winand and Jean-Michel Paul
Funding raised: Over $4mn in seed and Series A funding, led by MS&AD Ventures
Investors: MS&AD Ventures, Plug and Play, Hiscox, FinTLV and others
Pitch: Creating a market in new types of ILS, linking investors, brokers and carriers
Rivals: Extraordinary Re, Singapore Cyber Risk Pool

Source: Akinova, Crunchbase


WILDLY CAPABLE
INNOVATIVE VISIONARIES
STRATEGIC THINKERS
CLIENT FOCUSED
CAPITAL AGNOSTIC

Maintaining momentum

Odyssey Group president and CEO Brian Young explains why discipline will be a key feature of the 1 January renewals for primary carriers, reinsurers and ILS players alike

What are your takeaways thus far in 2019?

I did not expect insurance markets to firm as much they have, especially in North America, and the pace of improvement is accelerating, which is great to see. I was in Germany in July and even industrial fire business there, which has long suffered from intense competition, is showing meaningful signs of improvement. A common refrain we hear, "pushing the market", is the contraction in capacity from many carriers.

On the flipside, the reinsurance market response continues to be disappointing. In most parts of the world, reinsurance rates are flat to down, and commission levels remain stubbornly high. Reinsurance rates have not moved nearly enough to address the loss activity of 2017 and 2018, or the significant rate erosion during the last decade or a casualty claim pipeline that is bursting at the seams. Getting a 25 percent increase on one third of a loss-affected cat placement up for renewal provides little solace, especially when the rate has more than halved over the last decade and reinsurers' retro costs have spiked. And with commission levels generally running in the mid-30s for all but the most distressed business, reinsurers will continue to struggle to generate adequate margins on proportional business.

One positive on the reinsurance side is the increased demand from buyers to purchase more cover. We started to see it in the second half of 2018 and it has continued in 2019. The increased opportunity is a pleasing development at a time when original prices are moving in a positive direction.

What are your expectations for the 1 January renewal, in the absence of any material loss events between now and year-end?

Insurance markets should continue to firm in 2020. I do not anticipate that the renewed pricing and capacity discipline that we are seeing from insurers will change anytime soon.

Reinsurers will benefit from rising insurance pricing on proportional contracts, and commission levels should continue to trend down, especially where experience warrants a reduction.

Excess of loss pricing will be subject to increasing discipline, but whether this translates to higher prices will depend on individual account circumstances. Clean business should expect a flat risk-adjusted renewal, and any account with losses during the last few years should anticipate paying more again in 2020.

> "The reinsurance market response continues to be disappointing. In most parts of the world, reinsurance rates are flat to down, and commission levels remain stubbornly high"

We have seen an increase in the demand for aggregate covers the last few years. These structures have increasingly become more complex in scope. In my view, these will get harder to place as reinsurers and the ILS market push terms, exercise more discipline and show greater appetite for simpler risk- or event-based structures.

How much of a factor will ILS play in the 2020 renewal cycle?

Retro capacity has become more precious and certainly more expensive the last two years. While a low interest rate environment will continue to draw capacity to the sector, the days of cheap retro are over, at least for the next few renewal cycles. This should introduce more pricing discipline into cat business and will force some reinsurers to adjust their risk appetites.

Odyssey Group has had an exceptional run in recent years and even managed to generate underwriting profits in 2017 and 2018 when few peers did. What are the key factors driving your success?

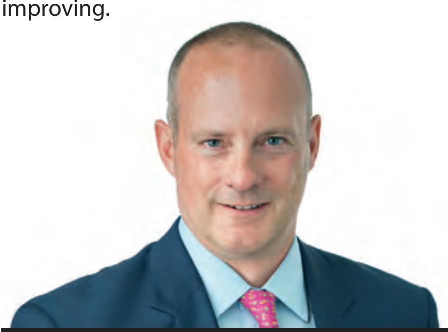
It helps to be a little lucky, and we have had our fair share of good fortune in recent years. As a group, we pride ourselves on the stability of our workforce and the consistency of our underwriting and claims handling. Discipline is embedded in our culture across our three platforms – OdysseyRe, Hudson and Newline – and embraced by a leadership team that has remained largely intact for two decades. Not having to answer to new masters every few years has allowed us to maintain our discipline and manage the business for the long term.

The focus on diversifying risk has been a key factor in our growth in recent years, but it has also played an instrumental role in helping us to generate underwriting profits the last two years in spite of the abnormally high level of cat activity. Our underwriting success in 2017 was driven by a 91.9 percent combined ratio in our Hudson and Newline insurance operations. In 2018, it was our reinsurance operation that delivered exceptional results, producing a market-beating combined ratio of 89.9 percent. Our results the last two years are a convincing display of the value of Odyssey Group's portfolio diversification.

Odyssey Group has grown significantly in the last few years. What have been the main drivers?

As I said earlier, diversification has played a huge role in our growth the last few years. Across our three platforms and 36 profit centres, our top line has expanded 40 percent from \$2.4bn in 2016 to \$3.3bn in 2018. Through the first six months of 2019, our top line is up an additional 10 percent and our new business pipeline remains solid.

The primary areas of growth have been in specialty lines, most notably in crop, motor, health, credit, affinity and cyber. We have also been growing selectively in property and casualty where results have been solid and/or where pricing and terms have been improving.



Brian D Young
President and CEO, Odyssey Group

We are one loss away from real dislocation: Brindle

The Fidelis CEO talks about climate change, the problem with Lloyd's and why ILS is on the ropes

Richard Brindle doesn't give many interviews, which is a minor tragedy.

With so much generic corporate verbiage permeating the press and so many commonplaces retailed as insight, Brindle presents a dramatic contrast.

He is a PR person's nightmare and refuses to be flanked by one at our meeting.

The Fidelis CEO speaks his mind with complete conviction, challenging anything that is half-baked or half-hearted in the most direct way possible.

Talk about business becomes talk about politics. He threatens to leave the country if a no-deal Brexit is forced through. He swears constantly. He teases his business partner and explodes with laughter.

But more than any of that he dissects the market with a clear-sighted mind and keeps nothing to himself.

Speaking at a previous interview in 2014, he was one of the first senior executives in the space to acknowledge that the London specialty insurance market was heading for a period of sharp softening.

Calling market dynamics and knowing when to write and when to walk away has been a hallmark, and his judgement bears watching.

And right now he thinks the cat reinsurance market is one loss away from major market change.

"One decent-sized loss by the end of the year and we're off to the races," he says.

The agent for change is the ILS market, which has been the key driver of pricing since 2012.

"Because it's just a load more trapped capital, a load more discredited ILS managers who told their investors some cock and bull story about 2019 – 'Oh we've re-underwritten the book and you're not going to respond to a medium-sized event'."

He continues: "They'll then get trapped capital from whatever it is and then it's just another nail in the coffin of these unaligned ILS managers that have no skin in the game."

Brindle says the received wisdom on post-event capital formation through the ILS market does not reflect the "jaundiced" views of the hedge funds and pension funds, and misses the point that money is bleeding away from activist managers.

"The traditional truism for a decade was that if you get a big event, some people get burnt and disappear, but there will be a wave of new capital looking to come in. Well, I don't think that's supported by the facts."

He goes on: "The available universe of investors is shrinking. Catco has had a massive impact on the credibility of our industry in this space – and it's really tough for anyone who wants to raise capital at all, regardless of track record."

'Get out of my office'

Brindle, an early exponent of third-party capital, is still in touch with the space due to Fidelis' sidecar Socium.

> "The available universe of investors is shrinking. Catco has had a massive impact on the credibility of our industry in this space – and it's really tough for anyone who wants to raise capital at all, regardless of track record"

And he notes that, right now, what he meets is extreme investor scepticism around the reinsurance sector.

"The ILS guys are horribly on the ropes," he says.

Investors are unsettled by climate change and the industry has no answer at this point to the increased risk in the system, as wildfires in Brazil and Siberia follow the 2017/18 conflagrations.

"We've spoken to investors that said they had guys through saying California in 2017 was a one-in-100-year event and then it happens again the next year and they say, it's a one-in-100 year event.

"Their response to that is: don't insult my intelligence and get out of my office."

Brindle adds that, until the models have been revised convincingly, firms that rely on model output to project returns for their fundraises will struggle to command any credibility. The Lancashire founder believes that even a $10bn loss event before year end would change the landscape given the amount of capital cedants would trap, and the near-impossibility of a third reload.

However, he stresses that there would be a delayed impact on reinsurance pricing from the locking up of the retro markets, which are 75 percent written by ILS money.

"It's like the roadrunner running off the end of the cliff and continuing to run on thin air for a while. They'll go through 1 January as if nothing has really changed but history suggests that it's always at the end of Q1 that the roadrunner finally crashes to earth, and then

CONTINUED ON PAGE 16

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CONTINUED FROM PAGE 14

you have the big corrections.

"Happened in 2002, happened in 2006, happened in 2012 and I think it will happen next year [if we get a loss]."

Brindle is adamant, though, that there needs to be some additional cat loss activity before year end.

If the rest of the year runs clean, even the weaker ILS funds will "get away with it" and the market may lose its backbone.

Some in the market have said they think rates in the excess-of-loss reinsurance market will be bid up by the transitioning US excess and surplus and London specialty markets.

Brindle says the argument is overdone, and believes the read-across from the primary to the reinsurance markets is exaggerated.

"I think each market has its own dynamics. People are siloed in most companies. I'm pretty sceptical [that primary will drive reinsurance pricing]."

Brindle argues that change comes from some authority imposing discipline on front-line underwriters. This can be senior management reducing available aggregate limits that can be deployed, or a move from Lloyd's or AM Best.

"The ability of cat underwriters to self-regulate is minimal, in my experience."

'Damning statements'

The Fidelis CEO made his reputation writing London market specialty lines like marine war, aviation, terrorism and energy as main underwriter at Lloyd's business Tarquin in the 1990s before taking big positions in those classes at his class of 2005 start-up Lancashire.

But Fidelis has been notably underweight in most of these classes since it was founded, reflecting Brindle's scepticism around rate adequacy.

And even now he remains something of a bear about the rating bounce, which looks set to see the Lloyd's market report around a 5 percent average rate increase on its renewal book for 2019.

According to Brindle, executives at carriers are straining to make the most of an improving rating picture, which is highly uneven.

"It's not a broad-based rating revival – it's patchy," he argues.

Areas that Brindle cites as evidence of uneven rating momentum include aviation, which is "uninteresting", downstream energy which is a "disaster" even if rates are

> "Look at the way these aviation brokers are staffing up. You stick a whole load of very experienced brokers into the pot and then 10 percent new capacity via a major new entrant, and any broker worth their salt will use that to undermine pricing"

up 20 percent, and "run-of-the-mill" blue-water hull and cruise liners.

And even areas of renewed interest such as satellite business, where rates have spiked after $800mn of losses, are priced at a third to a half of historic levels.

Brindle also flags the war market as indicative of the worst of the specialty markets. He says that, regardless of your view of the breach premiums being charged – which he thinks are deficient, it makes no sense to charge this at the same level for British flag ships and, for example, Liberian flag ships.

"It's quite a damning statement on the specialty markets."

Brindle thinks it is "the critical cat areas" where "real movement" is likely.

The exception is areas where Lloyd's has borne down, including the cargo and space markets.

For Brindle, the inability to drive rates higher reflects structural features of the specialty market.

"I think the ultimate reason for what I'm saying is that the lines of business I'm talking about are not critical cat, so if they're not critical cat they are diversifying within people's business models – it's not moving the needle in terms of how much capital companies have to carry.

"So they can easily compete irresponsibly on price within those classes of business and the only inhibitor on them is self-discipline rather than capital controls."

The Fidelis founder says his scepticism on pricing also reflects some of the new capital formation, and the changes taking place

> "I've been saying for 20 years, forget these B, C-list syndicates – they add no value, they lead nothing. What is the point of these people"

within distribution.

"Look at the way these aviation brokers are staffing up. You stick a whole load of very experienced brokers into the pot and then 10 percent new capacity via a major new entrant, and any broker worth their salt will use that to undermine pricing."

Winners and losers

Questioned on the Future at Lloyd's vision, Brindle notes that Lloyd's first had to resolve some fundamental questions.

"Is it a unitary entity collaborating? Or is it a whole bunch of competitors scrabbling around and biting each other in a barrel? Until you decide that you can't articulate this bold vision."

Brindle says the idea of creating a virtual following market which would pay fees to leaders would make Lloyd's more attractive to Fidelis.

"Do you actually anoint leaders, experts in given classes of business and the market lines up behind them and pay varying degrees of commissions? And they speak with one voice for all of that capacity?

"That would be awesome, but I can't see it happening with all of the different capital bases, different shareholder bases."

He continues: "At the moment, it's the worst of all worlds because they have all this duplication of cost, but they don't speak with one voice and they scratch each other's eyes out for every piece of business."

Brindle goes on to state that Lloyd's urgently needs to find a way to address the follow market problem.

"I've been saying for 20 years, forget these B, C-list syndicates – they add no value, they lead nothing. What is the point of these people?"

According to Brindle, Lloyd's CEO John Neal and the Corporation faced a major problem implementing any vision which required significant market players to accept unpopular decisions.

"They can't [impose the vision]," he says. "The fundamental problem is if they overreach – they can do it with perhaps smaller syndicates – but if they try it with Beazley or Hiscox, they'll say 'I'll take it to my company market platform'."

He also lighted on the winners and losers problem, with Neal thus far keen to avoid bringing into sharp focus who will lose as a result of the changes.

"Somebody has to decide who the winners and losers are. And who is above or below the line. Pick any company: which are above or below the line?"

Adapt or die?: The future for brokers

With data, technology and the risk landscape evolving at break-neck speed, brokers must broaden their value propositions to satisfy customer needs, according to Tim Page of Bielka Consulting

Adapting to change is in the insurance market's DNA, but with the world evolving at an increasingly rapid rate, is it keeping pace?

In July, Sequel Business Solutions sponsored a survey of London market practitioners, including a mix of both large and medium-sized brokers, MGAs, tech start-ups and carriers, on the future of the insurance intermediary. The message was clear: insurance needs, distribution methods and capital flows are changing, and intermediaries must adapt or die.

In today's world, multiple social, political and economic factors hint at impending crisis. Democracy is under threat, trust in the old political order is in short supply and nationalism and protectionism have re-emerged. Climate change and population growth are compounding the impact of extreme weather events and natural catastrophes. Wealth is concentrating in the hands of a shrinking few while many economic indicators point again to recession. The "protection gap" is growing, yet trust in insurers is diminishing and the emergence of new and difficult-to-insure risks raises questions around the value of traditional insurance products.

For the biggest corporations, insurance is becoming less important – other than as a strategic funding tool – as these firms have the balance sheets and expertise to self-insure. Even for smaller companies, intangible risks such as reputation are growing in importance, meaning intermediaries must broaden their propositions if they are to remain relevant.

Then there is the all-pervading influence of technology. Data, analytics, social media, AI and robotics are transforming both the industry and society. Data volumes will expand with the growth of smart technologies. This data can facilitate new understanding of risk and the development of flexible, individually tailored policies.

But as datasets and models become broader and more powerful, the "tyranny of the model" threatens to create uniform pricing, with certain risks excluded from coverage and governments becoming insurers last resort. This could not only erode the principles of insurance, but mean the poorest elements of society get "priced out".

Future broking demand

- Small commercial and retail lines will be serviced through transparent, self-service tech and hubs for bespoke products, sponsored and perhaps controlled by the broker
- Mid-sized businesses will get smarter, but will continue to value the risk management knowledge and leverage provided by the broker
- Large corporations will increasingly self-insure, applying risk management and capital using captives, alternative capital and reinsurance

Nevertheless, technology holds the key to the development of new models, products and efficiencies in the insurance chain.

We live in a world of "and", not "or": insurance is one solution among many. But total displacement is rare and insurance business models are becoming more diverse, often in collaboration with the tech and data providers driving innovation.

Insurance buyers want the best elements of commoditised products and tailored solutions. Speed of delivery, flexibility of coverage and the ability to self-manage policies through portals is fast being seen as the norm, particularly amongst the young.

Retail and small commercial insurance is at the vanguard, though self-service, automation and commoditisation are gradually becoming more widespread. The speed at which this will impact reinsurance and large commercial insurance is, as yet, unclear, though there is potential for datasets captured by primary insurers to be linked dynamically to reinsurers' modelling and pricing algorithms.

Exchanges and hubs for pricing and distribution, often managed by tech companies, pose both an opportunity and a threat for brokers. On one hand, they reduce costs, drive efficiency and facilitate tailored coverage, while on the other they consolidate the market and threaten disintermediation. Alliances with tech firms will therefore continue apace as carriers and brokers battle to assert control over the customer and distribution process.

Brokers, however, feel this is a battle they can win as the agent of the client, and as manipulators and controllers of vast quantities of data. This data advantage means they could soon technically price risk better than smaller underwriters. The future broker must harness this power to provide analytic insights to help clients manage risk and operate more efficiently, and to offer organisation-wide insurance solutions.

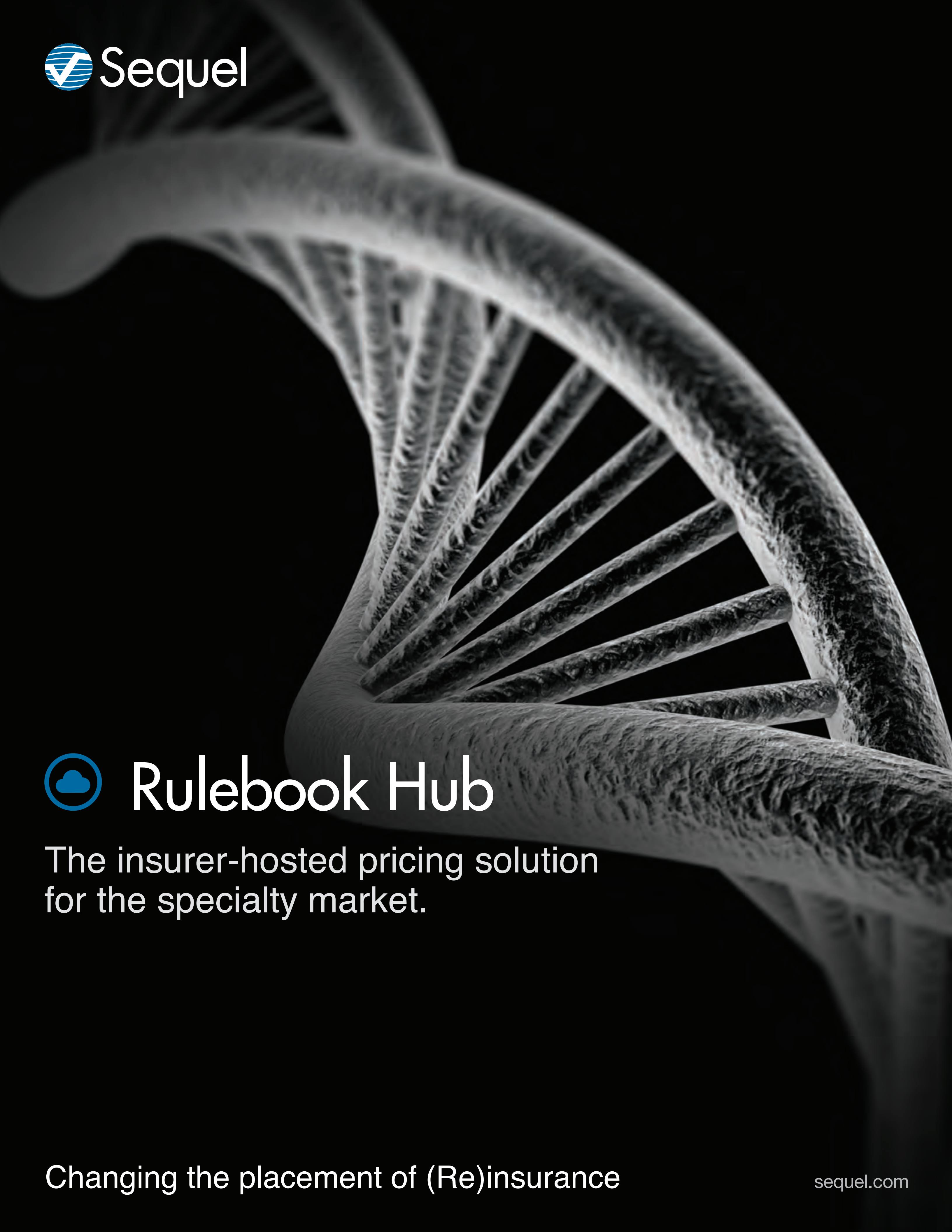
In addition to data analytics, the client of the future will increasingly expect brokers to advise on risk management, risk mitigation and loss prevention as well as the mix of insurance and capital markets products best suited to their needs. Brokers will increasingly control the distribution of risk, leveraging a variety of distribution channels and partnering with carriers and capital markets to offer hybrid products that hedge against interest rates, currency and commodity prices, for example.

According to those surveyed, the traditional transactional role of the broker will survive– the intermediary will remain the agent of the client – though there is likely to be a shortening of the chain. Future intermediaries must therefore be agile innovators to add substantive value to the process, transcending the traditional placement function, and becoming a deeply embedded strategic partner.

For big brokers, which can offer broad-based range of services or highly specialised expertise and services, the future indeed looks bright. If they play their cards wisely, including managing potential conflicts of interest, they look set to thrive.

Wholesalers and small firms, however, face greater uncertainty, unless they offer genuine differentiation and expertise. Consolidation of the distribution chain looks inevitable, with space for specialists. However, for those which don't excel in a particular field, the future may simply be "get bought or go bust", practitioners said. The time to adapt is now.

Tim Page
Bielka Consulting



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Looking to the future

SCR's Youssef Fassi Fihri explains how his firm is working to help close the African protection gap and why the continent's insurance and general economic outlook is brightening

How do you expect the themes and talking points at Monte Carlo to differ from those of 2018?

As every year, discussions will continue with all the key reinsurance stakeholders in a positive vein. It is worth mentioning that this year will be particular for us, as a regional reinsurer, with the launching of our insurance catastrophe model effective from 1 January 2020 in Morocco.

For that reason, our emphasis will be on finding the best reinsurance coverage for the regime. At the same time, we are also maintaining our international development strategy and looking at attractive opportunities in Africa and the Mena regions.

What do you expect to be the strategic high points for SCR de Maroc in the coming year?

These will stem from the implementation of a new strategic transformation plan driven by three pillars. These are: client service and access facility – we are targeting faster, more efficient underwriting decisions based on shorter application times. Risk knowledge and appetite management is the second pillar, centred on the implementation of ERM and risk-management standards.

Finally we are focusing on capital strength and improving our rating: we are offering a capital comfort to our clients and partners and working on improving our underwriting profitability.

What impact have the heavy cat losses of North America and Japan had on the African reinsurance market?

The worldwide market is still soft and prices are still not affected by the heavy cat losses of North Africa and Japan.

The players in our regions are very aggressive regardless of large claims that have happened, including about $60mn from a refinery fire, a $15mn loss at an aluminium plant and a $35mn engineering all-risks loss at a thermal power plant.

For us, with our strict underwriting policy, we continue to rely on our historical partners to find adequate reinsurance coverage.

In such a diverse (re)insurance market as Africa, if it's possible to speak in generalities, name some of the factors determining rates.

The level of capitalisation of local and regional reinsurers is one – we need to reinforce these. Modest local/regional retention is another. It's important to note also that technical reinsurance expertise is still being developed.

What needs to change for African insurance penetration to increase significantly?

Obviously, we have in Africa a very low level of penetration rate (about 3 percent) compared to developed countries. The main reasons behind this low level include socio-cultural factors such as traditional solidarity and the principle of family proximity, considered the principal engine of the social structures that determine economic exchanges.

Another factor is a lack of insurance culture in Africa in addition to the negative image towards insurers considered to be slow to settle claims.

The supply of insurance products is also considered to be inadequate regarding the realities of local populations and income levels.

So we need to develop a new model with micro insurance coupled with digitalisation and if necessary state subsidy for a period in order to offer medical, agricultural or natural catastrophe insurance.

SCR is organising the 26th Afro-Asian Federation of Insurance and Reinsurance conference in Marrakech on 23 to 25 September and we will develop these points as regards emerging economies based in Africa and Asia.

You've previously cited industry and energy sectors as presenting the best opportunities for primary and secondary carriers in Africa – which countries/geographies look most promising and which other sectors are opening up to insurance?

The industrial and energy sectors indeed still present the best opportunities for primary and secondary carriers in Africa. In Morocco we have 700 megawatts of installed solar capacity and we want to reach to 2000 megawatts in 2020 and wind power is expanding in a similar manner. Senegal and Mauritania have both made significant recent oil discoveries. Things will change positively for the next five years for the whole economy and the insurance industry will benefit from this.

> "The industrial and energy sectors still present the best opportunities for primary and secondary carriers in Africa"

Climate change has hit the headlines in earnest this year – what do you see as the impact of climate change and accompanying regulation on African reinsurers' business, including long-tail liability risks. How can the (re)insurance industry help?

It is certain that the consequences of climate change are quite real to our industry and it will have a significant impact on the economy going forward. SCR, as a key stakeholder in developing the insurance/reinsurance industry in Morocco and Africa, is promoting better land-use planning, including the respect of better building codes and greater use of green infrastructure to protect properties.

We are also a member of the UN programme aiming to implement environmental principles of the Sustainable Insurance Initiative.

In addition to that, we recently launched a new project of implementing measures and best practices of corporate social responsibility. We are striving along with the concerned authorities to promote measures protecting our environment and as well the local insurance/reinsurance business model.

Youssef Fassi Fihri
CEO, Société Centrale de Réassurance

ILS innovation in casualty

Praedicat CEO Bob Reville argues that liability cat bonds are well-placed to meet investors' demand for assets uncorrelated with broader financial markets

Ever-increasing jury awards for product liability litigation have grabbed the headlines and sparked conversation within the casualty market on ways to address risk aggregation.

The market is keeping a close eye on awards from product liability in particular, such as the ruling last month that Johnson & Johnson must pay $572mn for its role in manufacturing drugs that have spawned an addiction crisis across the US.

The extent to which the casualty market will absorb significant losses of this nature is unclear. However, the seemingly growing scale of these liability awards has led some to ponder whether the ILS market could play a role in managing these "casualty catastrophes", Bob Reville, CEO of casualty modeller Praedicat, said.

ILS investors primarily participate in the property catastrophe space, but recently cat bond issuances have been failing to keep pace with maturing deals.

In addition to the investor capital eroded by losses, capacity has been reduced by investors redeeming their funds following a disappointing 2018 that came hard on the heels of a post-Hurricane Irma fundraising boom.

Development of ILS in the liability market could mitigate the risk of large losses in general liability and other casualty lines such as cyber if certain key factors are addressed.

The nature of the beast

According to Reville, investors are looking for large-scale, insurable risk that can be broken down into "named perils" in the way property risk can be broken down into specific exposures such as wildfire and windstorm.

Given that investors are attracted to ILS in part due to its lack of correlation with broader financial markets, ideally ILS transactions would not be correlated with the market or with the other sorts of risks that exist in an ILS fund.

"With those characteristics without a doubt there should be a tremendous bout of interest in liability catastrophe," Reville told *The Insurance Insider*.

He suggested the risk has the potential to eclipse recent property cat losses.

Given that the active ingredients in some products being successfully litigated exist in many similar products, aggregation risk is real in this sector.

For example, litigation over products such as Roundup, which is owned by Bayer's Monsanto, will also affect the producers of hundreds of products that use the active ingredient in the weed killer, Reville explained.

But before casualty ILS can reach its full potential, the nature of the tail of perils must be addressed.

Chasing the tail

Modelling and developing products around the long tail of casualty perils remains a major hurdle, according to Reville.

Investors in wildfire liability are taking on a risk that has a set date of inception and a tail that amounts to the length of time it takes for the claims to resolve.

> "Without a doubt there should be a tremendous bout of [ILS] interest in liability catastrophe"
> *Bob Reville*

On the other hand, talc and opioid risks comprise the inception risk of the litigation as well as a tail based on the time it takes for the litigation to resolve.

"That tail is too long for capital investors today," he said.

Reville said that his modelling firm Praedicat has put a lot a lot of time and effort into modelling the "time tail" of that litigation, as different risks can have very different tails.

A bundle of risks over litigation that a commercial product may cause autism would result in several claims closing after four to five years as the product in question would be removed from the market, Praedicat estimates.

Litigation surrounding a hypothetical pesticide causing Parkinson's disease would have more of a 50-year tail.

"There, you can well understand the tail because you know what the harm is and the potential product that is driving that harm."

With that understanding, the industry will be able to create tranches that will allow you to "time box" the litigation, Reville said.

Different members of the market could participate at different stages.

"With those tranches, you could have a system where capital markets get involved in the first tranche and reinsurance involved in the out-year tranches," he said.

Model familiarity

One of the reasons the ILS market has yet to make inroads into casualty is that investors are more familiar with traditional catastrophe modelling frameworks.

Modelling in the casualty space is derived from analysing scientific literature around these risks, looking at exposure settings involved and simulating mass litigation from the literature to estimate the size of the litigation and when it will emerge.

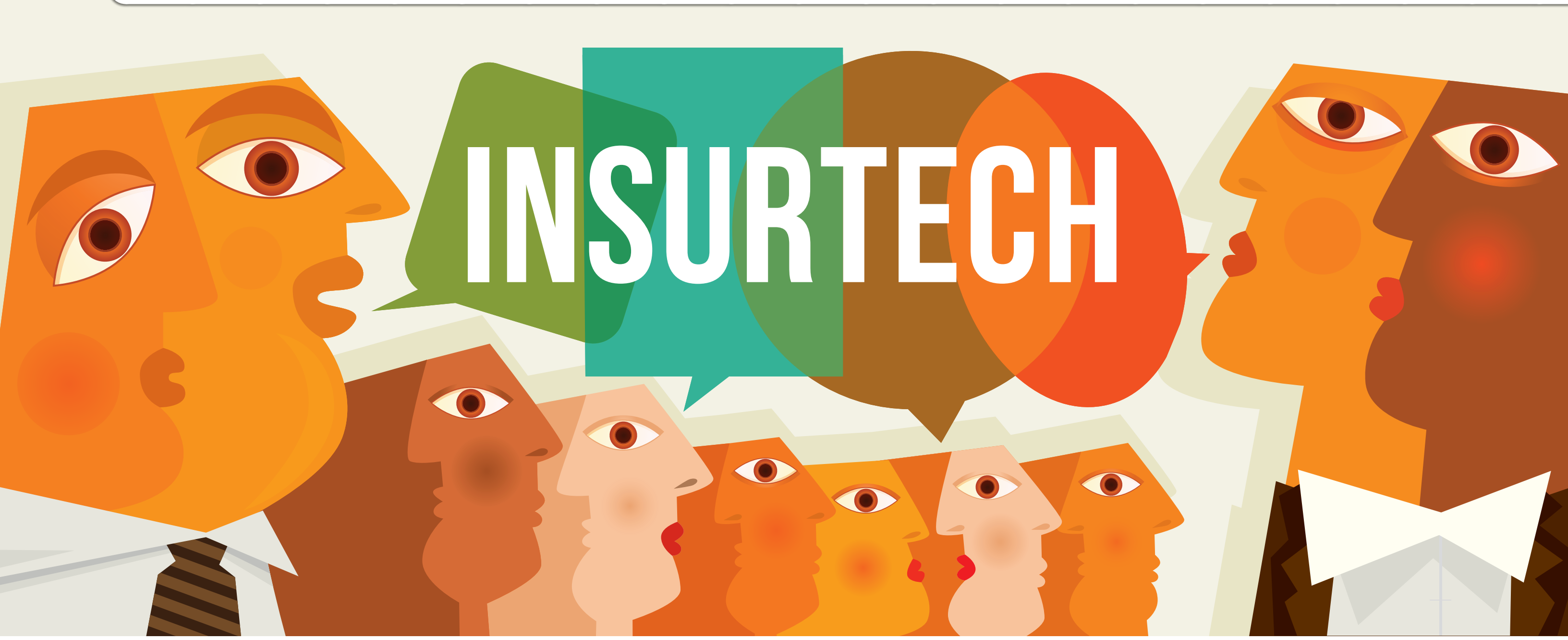
For example, Praedicat estimates DEHP, a chemical used in medical tubing and building products among other applications, is capable of producing litigation of over $117bn, with 1 percent probability.

Given the framework established in these models, the industry has to reckon with an additional challenge of attaching a value to litigation before its resolution.

It is unclear how the market would put a valuation on litigation that has been unfolding over many years but has not been resolved by the end of the time window.

For now, the market is adapting to the emergence of new reinsurance products around liability catastrophe that are trying to deal with casualty catastrophe on a named peril basis.

"It may be that once reinsurance starts to try to address it like that, that will provide for credibility for the underlying modelling approaches such that the capital markets investors will get involved," Reville concluded.



How far has InsurTech lived up to the early hype?

Adrian Jones, leader of ventures & strategic partnerships, Scor Global P&C: Where the initial hype was grounded in a solid understanding of our industry InsurTech has performed well. What has performed: digital distribution, certain forms of customer engagement, back-office digitisation, claims management and the development of new specialties.

The problems, somewhat predictably, came when someone tried to impose on our industry a successful model from elsewhere. "On-demand" works for taxis and restaurant meals. But on-demand insurance has mostly failed to scale up.

Dirk Lohmann, head of Schroder Secquaero: It depends upon how much of the Kool-Aid you drank at the beginning. In developed highly regulated markets the talk of disintermediation is overblown.

It is clearly having an impact on the retail side when it comes to price shopping via aggregators, which is increasing the commoditisation of obligatory insurance lines like auto or health insurance. But if you look at total sales, it is still a fraction of the pie. A lot of insurance still requires expert advice whether this comes through a broker, an in-house distribution force or a bot.

Jobay Cooney, senior managing director, Aon: Technology is changing risk in every corporate vertical; cyber security, the growing value of intangible assets and the gig economy are just three examples of the underlying impacts of risk emerging from technological advances.

This has been happening for some time now, but the difference now is the speed of change. The hype issue comes from the sheer number of potential technological options available to solve our clients' problems, advance strategic initiatives or grow operations. Aon tracks more than 1,200 start-ups to match partnership opportunities with insurers' strategic goals.

Peter Roeder, board member, Munich Re: There are start-ups looking to support or disrupt at each stage of the insurance value chain, and many processes have changed and are now more data-driven and digital. Whether InsurTechs do eventually disrupt the industry or not is not the decisive point for me.

These companies have triggered a movement whereby all insurers have upped their game to improve the products and services offered, how customers are serviced and the prices they pay for their policies. Ultimately, the end-customer is the winner.

> "Currently, the major disruption comes from implementing technologies in spaces where there had been none, and by improving a traditional competitor's ability to wield innovative technology"
> *Andrew Johnston*

Sven Althoff, executive board member, Hannover Re: Compared to the past few years, we see less new ideas right now, but a vertical expansion of existing ones. Concepts that worked in one market are copied for other markets.

One commonality is the focus on customer-centricity and automation, often through AI. These disruptive ideas are mostly at an early stage. At the same time, we see a change from disruption to co-operation. More and more InsurTechs collaborate with incumbents to leverage synergies between technology and insurance expertise. Investor interest in InsurTechs in general is unwaveringly high.

Luca Albertini, CEO and founding partner, Leadenhall Capital Partners: The reinsurance industry's attitude to tech has always been way more realistic than the equity market, valuing loss-making technology companies at billions of dollars in market capitalisation. It is important to measure the value added of each initiative and use it at its best.

There is much to innovate and improve in reinsurance and ILS management, and technology will support addressing some of the questions around the cost base.

I see these opportunities as way outweighing the perceived disruption threats.

Andrew Johnston, global head of InsurTech, Willis Re: The general consensus is that it probably hasn't. The answer depends, of course, on what your expectations were and are, and how relative success is measured. If improved investment returns, falling loss ratios, and reduced operating costs were the goals of InsurTech, no across-the-board success has been achieved. If, however, the goals were to expand the industry's view and understanding of the longer term role of technology in the insurance and reinsurance sector, and to set a course to implement change, the initial steps are critical.

Plenty of companies are making first steps, and InsurTech has been a good avenue for companies around the world to dip their toe into the technology pool.

Talk of collaboration with InsurTechs has supplanted discussion of wholesale disruption. Does that analysis reflect the reality of what's happening?

Cooney: The money that has funded the InsurTech ecosystem has supported InsurTech companies that are out to disrupt the traditional ways of distributing and servicing insurance.

However, it's early days for these disruptors so time will tell whether they will be able to acquire and retain customers in a profitable manner. It also remains to be seen whether these business models will have enough cash to wait it out, become profitable and be a viable long-term option for consumers.

InsurTechs that are applying technology to enable carriers to sell more product, be more efficient and improve risk selection have started to reap real benefits and are partnering with the industry at steady pace to the benefit of both parties. It's been a catalyst for positive change to modernise our industry at a faster rate. The big tech companies are also poised to disrupt as they continue to accumulate data and become more entwined in consumers' lives. That could be more disruptive than the InsurTech movement.

Johnston: It is far easier for a new entrant to support the incumbency than to acquire customers and navigate complicated regulatory landscapes. As a result, we have seen the "improve, enhance, enable" narrative come through a lot more than full-on disruption.

Currently, the major disruption comes from implementing technologies in spaces where there had been none, and by improving a traditional competitor's ability to wield innovative technology.

InsurTechs, however, will continue to grow. One day they may wish to compete so the threat of disruption – in its traditional sense – will never disappear entirely.

Albertini: For me, the collaboration attitude has far more chance of success. One of the issues with most technology is that good ideas can be replicated and if an initiative does represent a threat because of technology, large incumbents can always look at the best of it and plug it in their processes facing their customers. Probably the biggest threat would come from a truly innovative InsurTech initiative from someone with its own large customer base that is currently buying insurance somewhere else and can be offered a better, cheaper or cooler product.

Roeder: InsurTechs and insurers have skill sets and qualities that complement each other in culture, mindset, capital, risk understanding, IT know-how and so on. Working together is often better than trying to beat each other at the same job.

To tackle the challenges the industry faces collaboration continues to be key, especially given that the entry barriers in the insurance sector are high and not easy to overcome for a start-up.

Lohmann: There are clearly areas where insurers (more than reinsurers) are benefitting from collaboration with InsurTechs or taking these capabilities in-house to improve their understanding of their client base, as well as to improve and automate their processes and enhance the customer experience.

Here, the reality is that if one is not user-friendly there is a high risk of losing that customer to a competitor that is. Long term, these efforts are also going to be key to reducing the cost base of the primary insurers.

Althoff: InsurTechs are adapting quickly. In the past, most of them wanted to become full primary insurers. Right now, many focus on offering solutions instead of building insurance companies. Incumbents also embrace InsurTechs as partners.

Collaboration between InsurTechs and incumbents brings advantages for both the insurance industry and the policyholders. Through such partnerships, our industry has already become more innovative and responsive to the changing needs of our clients.

What characterises the most effective InsurTech-reinsurance alliances?

> "The big tech companies are poised to disrupt as they continue to accumulate data and become more entwined in consumers' lives. That could be more disruptive than the InsurTech movement"
> *Jobay Cooney*

Roeder: In general, there should be a tangible problem for which an insurer and a start-up company can combine forces – for example, bringing together an on-demand digital front end with underwriting skill set and insurance licenses.

In my experience, alliances work best when both partners bring something to the table because then new things can develop. We have achieved this with co-operations with or investments in InsurTechs. Think of Metabiota as an example for Munich Re's long-term co-operation, where epidemics expertise, insurance know-how and data have allowed us to create new products.

Lohmann: I'm afraid I am not aware of that many in the reinsurance sector. Where I see increasing success is in the primary sector, where technology and AI is being used for underwriting and pricing purposes. But is this "InsurTech" or are these simply MGA's in a different guise using modern technology?

Johnston: MGA-type businesses that allow reinsurance capacity to be deployed in new markets by supporting innovative, well-priced products. Alliances are typically best when everyone's objectives are aligned, and all members truly understand their roles.

Althoff: Reinsurers can establish digital innovation platforms. These allow InsurTechs to offer their solutions to a reinsurer's clients.

Reinsurers can support the digitisation of primary insurers and insurance products without being in direct competition. That is why we launched our innovation platform "hr | equarium" earlier this year. It is a perfect fit with our strategy to focus on reinsurance. We are not building insurance companies from scratch or acquiring significant stakes in promising start-ups to compete with our clients. We are happy to support InsurTechs with traditional

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reinsurance services, expertise, contacts and capital.

Jones: We believe in an alignment of interests to create long-term partnerships that benefit both parties. Often, that means both investment and a commercial arrangement. We look for entrepreneurs who are culturally aligned and need what we provide. For example, we back entrepreneurs who want to build and operate their own tech stack, but who see value in a partner like Scor bringing expertise and risk capacity.

We also believe successful InsurTech companies need a good understanding of insurance. We have pursued a number of such relationships, where our role as both an investor and a risk taker should foster profitable and successful outcomes for both parties.

Cooney: Those InsurTech companies that have data and analytics at the core of their offerings, or allow for a smarter and more efficient way to access capital, are the ones the reinsurance industry is going to be interested in.

Also, many InsurTechs are enabling some active reinsurers in the space to get closer to the original customer and could be a means to diversify into the primary business.

InsurTechs that find new ways to enable the understanding and coverage of emerging risks that may be currently underinsured will be desirable to the reinsurance community.

How long will it be before we see sizeable takeovers of InsurTechs by reinsurers and reinsurance brokers?

> “Once firms have established a demonstrable record of generating value we will start to see those businesses being acquired. Many start-ups already have insurer shareholders and/or capacity providers that are likely to become their ultimate owners when they reach maturity”
> *Will Curran*

Johnston: It's already happening. For example, Willis Re parent Willis Towers Watson closed a transaction recently to acquire Tranzact, a direct-to-consumer healthcare InsurTech that links individuals to carriers. It has become part of the WTW Benefits Delivery and Administration business. Another example is Munich Re's purchase about a year ago of Berlin-based relayr, which developed a platform to supports data collection and analysis for industrial companies through internet-enabled sensors.

Althoff: It's happening here and there but it's still early days for most InsurTechs. It is our strategy to support InsurTechs with our global expertise and through reinsurance products.

We can connect InsurTechs with our ceding companies or other InsurTechs and service providers. We see ourselves as a business partner for InsurTechs, not as an investor in them.

Will Curran, departmental head of reinsurance, Tokio Marine Kiln: While the pace of technological change is rapid, InsurTech firms are still in their infancy.

However, once firms have established a demonstrable record of generating value we will start to see those businesses being acquired.

How soon that will be depends on the speed with which they can develop either unique propositions or something that could provide a prospective parent company with a competitive advantage. Many start-ups already have insurer shareholders and/or capacity providers that are likely to become their ultimate owners when they reach maturity.

Roeder: Many insurers, reinsurers and brokers have set up funds to invest in start-ups they see potential in. So, should the right opportunity arise, the insurance sector is well positioned to seek an acquisition.

I would expect the focus for this to be twofold: first, InsurTechs that are disrupting key segments; and second, areas where an InsurTech does markedly better than an insurer or enables the insurer to complete or do something much better.

Albertini: The non-sizeable takeovers or venture capital contributions are already happening so once the business model has been proven to work on a smaller scale, surely the largest players will be ready to scale up for the right opportunities

> “Non-sizeable takeovers or venture capital contributions are already happening so once the business model has been proven to work , surely the largest players will be ready to scale up”
> *Luca Albertini*

Cooney: As expected, we are already seeing consolidation within the InsurTech ecosystem. As InsurTech matures, traditional players in all areas of insurance will look to gain a competitive advantage by acquiring or partnering with start-ups.

Those reinsurers that are looking to take on more diversified risk will also look for technology-enabled ways to distribute and service risk.

CONTRIBUTORS

Luca Albertini, CEO and founding partner, Leadenhall Capital Partners

Sven Althoff, executive board member, Hannover Re

Jobay Cooney, senior managing director, Aon

Will Curran, departmental head of reinsurance, Tokio Marine Kiln

Andrew Johnston, global head of InsurTech, Willis Re

Adrian Jones, leader of ventures & strategic partnerships, Scor Global P&C

Dirk Lohmann, head of Schroder Secquaero

Peter Roeder, board member, Munich Re

The capital equation… and the *Lloyd's* capital equation

Capital is the foundation of the insurance industry, the essential base on which (re)insurers are constructed.

It used to be so much simpler. But today the complexities of (multiple) regulators and the demands of rating agencies and other stakeholders, together with the need to compete for capital with other industries, make creating the optimum capital structure a degree-level problem for management.

These issues are magnified still further when operating at Lloyd's.

It's not as if there is a shortage of capital. Arguably there is more capital around than ever before. Low interest rates have led to more pension fund and sovereign wealth fund money flowing into the hands of alternative asset managers as they search for yield. Niche and specialist industries have also attracted capital.

But the complexities of capital structure are demanding management teams at Lloyd's to develop new ways to optimise capital structure in a Lloyd's environment. And as no two firms have the same issues, this is a truly bespoke conundrum.

Let's break the problem down into its component parts.

First, the capital requirement to operate at Lloyd's has been moving upwards for some time, and there is no sign that this trajectory is going to change any time soon. So, in a softening market environment, optimising return on equity has become ever more challenging.

Second, we have seen two years of high cat activity, resulting in trading losses for some, and causing regulators (here I mean Lloyd's) to ensure that there is sufficient capital in the system to cover those losses. So the issue is magnified.

> "The complexities of capital structure are demanding management teams at Lloyd's to develop new ways to optimise capital structure in a Lloyd's environment. And as no two firms have the same issues, this is a truly bespoke conundrum"

Bill Cooper
TigerRisk

Last, Solvency II and its equivalent regulatory regimes in other jurisdictions demand a holistic view of funding across its components. For insurers this is the capital structure (equity and debt) and reinsurance, which is therefore not just a form of risk management but also a component of the capital equation.

The softening market over the last few years, and the flurry of M&As which have taken place during this period, have led to a number of firms discontinuing lines of business and thus tying up capital to back their books. Rationalising the balance sheet is also a key tool for some, either through reinsurance transactions or by selling non-core companies.

We have also seen some of the traditional sources of capital at Lloyd's become restricted. This happened most obviously with letters of credit.

Following the introduction of rules around the usage of letters of credit in 2017, total volume has fallen from over £9bn to just over £7bn today. This has been replaced largely by cash and investments from the parent companies of some of the firms at Lloyd's owned by international trade players.

A number of reinsurers which once supported capital at Lloyd's have also exited or reduced their exposure, driven by poor returns over the last two years, and in some cases, by issues specific to their own businesses.

Yet in spite of all these challenges, the advantages of operating at Lloyd's are well-known and significant: the licence network, the rating, the brand, the operating leverage, let alone the critical mass of insurance expertise in EC3. Moreover, new management is developing ways to enhance and broaden the appeal of Lloyd's.

Meanwhile, rates are rising in many classes of business and management teams are looking to develop growth plans. The key to future growth will be identifying and deploying the right capital.

At TigerRisk we believe an adviser which can bring together the diverse elements required for a holistic view of capital (equity, debt and reinsurance capacity across reserves as well as front book) can create meaningful value for insurers.

Bill Cooper recently joined TigerRisk to help clients develop optimal capital structures. Before joining TigerRisk, he was managing director of insurance and specialist finance at Lloyds Bank. He can be contacted at bcooper@tigerrisk.com or +44 (0)7764 625154.

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‘Great idea’ no longer enough: Munich Re’s Dennis

Financial strength is becoming an increasingly important factor when choosing potential InsurTech partners, according to Munich Re Digital Partners’ Mark Dennis.

Dennis, who is co-founder, COO and European CEO of the reinsurance giant’s InsurTech arm, said: “What has become clear is that a great idea with a strong team behind it is no longer enough. Equally important now is a credible route to market with clear distribution potential.

“And we also look more carefully at the financial strength of prospective partners to ensure they have sufficient runway for launch and beyond.”

Munich Re Digital Partners was founded in 2016 with a remit to become “the fastest and most flexible insurance partner for digital disruptors”.

It has alliances with companies including Trov, Hippo and Bought By Many.

Dennis told this publication: “The main pillars of our model are key product and pricing expertise, global capacity, flexibility and patience in developing the business, data analytics to enable fast response, and an execution focus to facilitate speed to market. For us the partnership is paramount but investment may follow.”

The Munich Re operation has about 20 live partnerships and has invested in around a third of them. It has a further 20-30 partnerships with start-ups in the pipeline.

Willis Towers Watson’s second-quarter InsurTech briefing showed that InsurTech funding breached the $1bn mark for the fourth quarter in a row, with a doubling in the number of Series D and E+ rounds.

Dennis noted that incumbent carriers were increasingly willing to forge partnerships with InsurTechs.

“In the earlier days of InsurTech there was suspicion and even fear of what disruption InsurTechs might bring. Now there is a clearer realisation that collaboration is the key,” he said.

However, reinsurers have been ahead of the pack in terms of partnering with start-ups.

“It’s fair to say that some reinsurers have stolen a march on the primary insurers. At Munich Re we recognised some time ago the opportunity that disruptors will bring to the market, and we have embraced that disruption.

“Over the last three years there has been positive movement from the insurance sector to engage with InsurTechs rather than to be suspicious of them, so that is great for the industry as a whole.

“I do believe that some reinsurers have an advantage still in that they do not have any legacy to speak of, whereas some insurers will have existing business which can be impacted, as well as systems and processes which are hard to change.”

Last year, Munich Re Digital Partners’ portfolio of InsurTech partners wrote in the region of EUR100mn ($111mn) of premium. Dennis expects that to double in 2019.

He added: “We are not complacent and we continuously look at how we can improve our engagement model, our network of service providers, and our active partnerships.”

Big-name VC interest is ‘thumbs-up’ for InsurTech: Scor’s Thorne

Increased interest from big-name Silicon Valley investors in InsurTech is a vote of confidence in the sector and will have a ripple effect on funding, according to Will Thorne, head of Emea, specialty and Lloyd’s ventures at Scor Global P&C.

Thorne told *The Insurance Insider*: “It’s a big deal in the VC [venture capital] community when you do have firms like Bond (Hippo investor) or Sequoia (Lemonade investor) making large InsurTech investments in later-stage funding rounds because they’re considered market leaders; it suggests they believe in the exit case.

“We’ve seen increased VC confidence in the sector as a whole as a result. Belief spreads to earlier-stage funding rounds and is helping to attract capital to the series A to B transition, which can sometimes be the hardest fundraise.”

Having large VC firms investing in later-stage rounds is a “thumbs-up” for the sector as it showed that investors increasingly believed in that InsurTech was scalable, he added.

According to the latest Willis Towers Watson InsurTech briefing, later-stage funding is on the up, with Hippo and Lemonade recently closing Series D fundraising rounds of $100mn and $300mn respectively.

In the second quarter of this year, later-stage funding from Series D onwards accounted for 23 percent of all transactions, as opposed to 14 percent in the previous quarter and 19 percent in the same quarter last year.

The briefing also found that seed and Series A funding fell to $147mn, the lowest level since the third quarter in 2017.

Scor P&C Ventures, which Thorne co-created in 2017, predominately invests Series A and B rounds in carriers, technology companies and MGAs. It makes four to five deals a year.

Since its creation, Thorne has noticed a shift in focus among InsurTechs.

“We’re starting to see more start-ups try to innovate in specialty insurance.

As someone who originally joined the industry as a specialty underwriter, I find it extremely interesting watching InsurTechs try to work out how to deliver innovation in non-consumer lines in a way which can scale and can therefore be backed by venture capital. There are still a lot of untouched specialty segments which InsurTechs have not yet unlocked.”

He also pointed out that the makeup of InsurTechs has changed, with more and more companies focusing on service provision and product innovation, rather than distribution. Full-balance-sheet InsurTechs remained rare, he said.

Thorne noted that increasing entrepreneurial interest in insurance and improved regulatory landscapes in Asia and Latin America, including Vietnam and Brazil, made them attractive environments.

The Scor unit has a partnership in Brazil with Scor-owned Essor.

Thorne added: “We’re very keen to establish partnerships with InsurTechs in certain countries in Latin America, such as Brazil, because of the opportunities arising from the chance to deliver wholly new propositions which use technology to bridge the penetration gap and provide products to the previously uninsured instead of iterating on existing insurance propositions.”

Tackling technology

IGI's Hatem Jabsheh and Nasser Zagha explain how the carrier is boosting its tech know-how and why the sector as a whole still lags behind banking

Incumbent insurers have typically been wary of InsurTech. Why and how has that changed?

Hatem Jabsheh: InsurTech was seen as highly experimental and over-hyped by some in the market, but there has been a shift of attitude in the sector to embrace technology. The reinsurance industry is currently at a crossroads – it faces the huge challenge of bringing its products and systems into a new, digitally focused era if it wants to stay relevant. In the last five, 10 years, a perfect storm has been circling the reinsurance market in global economies: a slowdown in growth of traditional businesses; a rise of software-based companies; change in consumer behaviour; availability of considerable computing power through the cloud; and a wave of millennials joining the workforce with a significantly different skillset based around digital expertise. Many in the market have also started to believe that technology can help lower operational costs and to improve analytics. That said, there has not yet been an InsurTech initiative that is truly disruptive. Currently the reinsurance industry is more focused on how incumbents can work with InsurTech providers, either through partnerships or by investing in software to improve pricing and underwriting tools, which simply digitises existing processes.

Which works better for IGI – organic InsurTech development, partnerships with start-ups or something in between – and why?

Hatem Jabsheh: First and foremost, we work out what the problem is that we are trying to tackle. Then we look at whether we already have the systems and operations in place, or whether we need to bring in someone else to help. It really should be as simple as that – figure out what the problem is that you are trying to solve and then look for the optimal solution, both for the short term and the long term. However, building strong strategic partnerships is more powerful than simply acquiring a technology firm. A partnership combines our industry's analytical expertise and customer relationships with the vision and innovation that only a tech firm has.

Hatem Jabsheh
Chief operating officer,
IGI

What are the most important benefits of InsurTech alliances – wider distribution or operational improvements?

Hatem Jabsheh: Before joining IGI, I was part of the technology revolution in stock market trading and saw the shift to automated trading. If done correctly, InsurTech will innovate every part of the process and distribution chain, but my worry is that the reinsurance industry does not appreciate the speed of advancement with technology. For the reinsurance sector, the benefits will be on processes, underwriting, decision-making and operational improvements. Reinsurance is a complicated sector, with high operating costs and a big reliance on underwriter and actuarial influences. As a relatively small underwriter, I will not be able to influence the distribution channel, but I can make a change to my company's own internal costs.

Nasser, you took up this newly created role from the banking sector – how do the tech challenges for (re)insurers and for banks compare and contrast?

Nasser Zagha: For banks, their business is based on a high volume of transactions, which requires the ability to take decisive decisions and be agile, so they care about maintaining their large volume of transactions and being able to make decisions efficiently. The banks' customers interface with them on an almost daily basis and there is a high demand for better customer experience. Banks tend to provide services over different mediums such as online and mobile. Now we are seeing emerging technologies, such as smart ATMs and a high level of automation for devices. We also see chatbots, some of which are augmented with artificial intelligence (AI) and some of which have predictive modelling, which is game changer for the banking industry. This has attracted many start-ups to address such issues. On the other hand, with the insurance industry, we don't interface with our clients every day. But there is still a high demand for providing better services for clients, such as better claims processing. There is a need for better capabilities for insurance companies, but there is still a huge contrast between insurance and banking, especially with reinsurers.

Could you elaborate on that reinsurance tech deficit?

Nasser Zagha: Reinsurers need to enhance AI capabilities along with predictive modelling. There is potential for reinsurers to look into such capabilities to augment their overall operational capabilities and be able to reduce risks, improve their revenues or gross written premiums, and ultimately cut down claims over time.

Is the (re)insurance industry tech savvy enough and if not, how can IGI and others nurture the right talent?

Nasser Zagha: There is a huge lack of expertise when you bridge between reinsurance, insurance and technology. In the banking industry they are using emerging technologies like blockchain, AI and augmented reality and predictive analytics. However, with the insurance industry we do not see much being done to leverage emerging technology and that would be a great enhancement for the industry. In our three-year strategy we are sending most of our employees for extensive training on technology and insurance and teaching them how to leverage the most from new technologies. We are trying to align ourselves with some of the subject matter experts and small corporations, as well as InsurTech and FinTech start-ups, so we can understand how the paradigm of the insurance industry will be changed over time.

Nasser Zagha
Chief technology officer,
IGI

How taxi drivers and drone pilots are changing the loss adjusting industry

DropIn founder Louis Ziskin explains how his InsurTech can slash claims costs and curb fraud

Louis Ziskin thinks insurance is doing claims all wrong. The DropIn founder believes misaligned incentives and dubious practices have sent claims costs spiralling.

Ziskin set up DropIn in 2015, when he realised that the advent of smartphones and the gig economy could revolutionise the way insurance claims are adjusted.

His company now employs thousands of drone pilots and taxi drivers as ad hoc insurance inspectors and loss adjusters.

The technique is now being used to do everything from cheap on-site inspections during a commercial insurance underwriting process to adjusting auto or property catastrophe claims.

DropIn has three years' experience of operating in natural catastrophe zones.

In November 2018, the Woolsey Fire in Los Angeles provided the ideal testing ground for DropIn's video streaming technology.

An insurer contacted the company to say that two clients had homes in the Malibu area threatened by the fire.

In a bid to get eyes on scene, DropIn COO Ian Wilson strapped a drone in a waterproof box to a jet-ski and rode to his parents' beach house in Malibu, an area cut off by the flames. A drone pilot went with him on the back of the jet-ski.

Wilson beached the vessel and the drone was launched, filming the fire. It was able to take imagery of the insured homes, feeding the pictures back live to the family whose home was threatened. One house suffered minor damage and the other was fine – the insured family were able to see pictures of their undamaged home in real time, while they sat in a rescue shelter.

"The insurer had one very happy client – they are probably going to renew with that company forever," Ziskin explained.

Once the checks on the insured property had been completed the pilot stayed on the beach, taking live footage for the fire department. The use of live imagery on a drone, rather than bringing a drone back to ground, plugging it in and downloading the footage, gives insurers immediate information about what is happening.

The technology also allows an insured to use their own phone to stream footage straight to an insurer.

DropIn has a partnership with ride-hailing app Lyft, with drivers able to pull in a new income stream serving insurers with instant claims images. Ziskin also works with numerous freelance drone operators.

DropIn has attracted interest from Lloyd's, which picked the company as one of the inaugural members of the Lloyd's Lab.

Ziskin has an unusual background for a CEO. He spent 12 years in a California prison for trafficking 700lbs (318kg) of ecstasy into the US. When he was caught in 2000, it was the largest haul of the drugs ever detected by the US authorities.

Ziskin said his background makes it easier for him to see structural problems with the way the industry adjusts claims.

"I did what I did when I was younger, I was a drug trafficker, I was around criminals, I was around scammers," he told *The Insurance Insider*.

"I've heard every scam there is, you can smell 'em, and then spending 12 years in prison hearing even more scams – I mean, you can just tell right away."

He said that the auto loss-adjusting process has misaligned incentives that lead repair shops to inflate claims costs.

"Insurers are overpaying on bodyshop work and vendor work."

Ziskin argues that if insurers get accurate imagery of an accident from the day of the crash, rows between customers and carriers over the extent and cost of damage can be avoided.

Ziskin is a vociferous critic of his biggest rivals: the incumbent third-party administrators (TPAs) that dominate the claims business.

"TPAs are taking too much money out of the game," he argued.

"Why are insurers paying high-value dollars to adjust low-value claims? It takes the same amount of money to adjust a $3,000 claim as it does to adjust a $30,000 claim."

His main criticism is that traditional TPAs take far too long to send an adjuster out on site. Following a cat event, it can take weeks for a claim to be adjusted.

He said one of the "ten commandments" of insurance is "the sooner you have eyes on scene, the lower the claim".

Drone operators worldwide

Certified commercial drone operators: 3,400 (US), 4,200 (International)

"Droperator" partners: 2 million (US) 3.7 million (International)

He said that the "only people who benefit" from longer waits are TPAs and ambulance-chasing lawyers.

Under the conventional loss-adjusting model, adjusters in the US spend hours on the clock driving from claim to claim. Ziskin said that Lyft drivers know the local roads and are more emotionally invested in the area hit by a hurricane than employees of big adjusting companies.

DropIn adjusted 900 claims in days after Hurricane Florence last year.

The aftermath of Irma in 2017 is an example of what can go wrong if claims are not adjusted quickly. Many insureds were still waiting for loss adjusters when contractors arrived, saying they'd fix the roof for free if they'd sign some paperwork handing over their right to indemnity.

Instead of a customer who just wanted their roof fixed as quickly as possible, insurers were faced with litigious contractors and their lawyers, hell-bent on claim inflation.

Such assignment of benefits (AOB) fraud has proved hugely costly for the industry. Florida carrier United Insurance Holdings, for example, said in February that claims Irma claims had crept by 44.5 percent since 2018 to $900mn.

Florida has now passed an AOB law that is set to be bring claims costs under control, but only after litigation costs spiralled out of control for what should have been easily handled property claims from Irma.

As well as reducing the cost of loss adjusting, DropIn claims to be a good way of separating honest claimants from fraudsters.

"We send you a text saying we may be able to get you a vendor in today [to fix the problem].

"Our unique proposition is that the bad actor is self-identifying. A good actor will let someone stream using their phone," explained Ziskin.

"The really interesting thing is that the bad actor isn't going to want any of that."

The Insurance Insider 2019 EVENTS

***Insider* Progress: Nurturing a Changing Workforce**
18 September 2019 | 8:30 - 11:30
Clyde & Co, Beaufort House, 15 St Botolph Street, EC3A 7NJ
#InsiderProgress

(Webinar) *The Insurance Insider* | On Air: Keeping ahead of the hackers
19 September 2019 | 15:00 - 16:00
Watch live or on demand
#InsiderWebinar

***The Insurance Insider* Cyber Rankings Awards**
20 September 2019 | 12:30 - 17:00
Banking Hall, 14 Cornhill, London, EC3V 3ND
#InsiderCyberAwards

(Webinar) *The Insurance Insider* | On Air: Foundations for our future
26 September 2019 | 11:00 - 12:00
Watch live or on demand
#InsiderWebinar

***Trading Risk* New York**
3 October 2019 | 08:15 - 15:30
(followed by networking drinks)
Convene, 75 Rockefeller Plaza, New York, 10019
#TradingRiskNY

Guy Carpenter's Baden-Baden Reinsurance Symposium
20 October 2019 | 16:30 - 18:30
(followed by a cocktail reception)
Kongresshaus Baden-Baden, Augustaplatz 10, 76530 Baden-Baden, Germany
#BBRE19

The London Market Conference
7 November 2019 | 08:15 - 16:00
(followed by networking drinks)
etc venues 155 Bishopsgate, Liverpool Street, London, EC2M 3YD
#InsiderLMC

For further information on attending any of the above events, please contact:
events@insuranceinsider.com
+44 (0)20 7397 0607

For further information on speaking, exhibiting and sponsorship opportunities, please contact:

Sajeeda Merali, Commercial Director
sajeeda.merali@euromoneyplc.com
+44 (0) 20 7397 0613

Benjamin Bracken, Head of Marketing Services
ben.bracken@insuranceinsider.com
+44 (0) 20 7779 8754

Oliver Nevill, Head of Strategic Partnerships
oliver.nevill@insuranceinsider.com
+44 (0)20 7397 0619

THE TEAM

EDITORIAL DIRECTOR
Mark Geoghegan
mark@insuranceinsider.com

EDITOR-IN-CHIEF
Adam McNestrie
adam@insuranceinsider.com

ACTING MANAGING EDITOR
Catrin Shi
catrin.shi@insuranceinsider.com

EDITOR
Laura Board
laura.board@insuranceinsider.com

ASSOCIATE EDITORS
Christopher Munro
christopher.munro@insuranceinsider.com
Christie Smythe
christie.smythe@insuranceinsider.com

FEATURES EDITOR
Gavin Bradshaw
gavin.bradshaw@insuranceinsider.com

SENIOR REPORTERS
Fiona Robertson
fiona@insuranceinsider.com
Lucy Jones
lucy.jones@insuranceinsider.com
Rachel Dalton
rachel.dalton@insuranceinsider.com
Emmanuel Kenning
emmanuel.kenning@insuranceinsider.com
Bernard Goyder
bernard.goyder@insuranceinsider.com
John Hewitt Jones
john.hewittjones@insuranceinsider.com

REPORTERS
Sofia Geraghty
sofia.geraghty@insuranceinsider.com
Anna Sagar
anna.sagar@insuranceinsider.com
Samuel Casey
sam.casey@insuranceinsider.com

DIRECTOR OF RESEARCH & HEAD OF AMERICAS
Gavin Davis
gavin.davis@insuranceinsider.com

SENIOR ANALYST
James Thaler
james.thaler@insuranceinsider.com

ANALYSTS
Gianluca Casapietra
gianluca.casapietra@insuranceinsider.com
Dan Lukpanov
dan.lukpanov@insuranceinsider.com

COMMERCIAL DIRECTOR
Sajeeda Merali
sajeeda.merali@insuranceinsider.com

HEAD OF MARKETING SERVICES
Benjamin Bracken
ben.bracken@insuranceinsider.com

HEAD OF STRATEGIC PARTNERSHIPS
Oliver Nevill
oliver.nevill@insuranceinsider.com

SUBSCRIPTIONS DIRECTOR
Tom Fletcher
tom.fletcher@insuranceinsider.com

PARTNERSHIPS MANAGER
Joel Lagan
joel.lagan@insuranceinsider.com

SENIOR ACCOUNT MANAGER
Georgia Macnamara
georgia.macnamara@insuranceinsider.com

SUBSCRIPTIONS ACCOUNT MANAGER
Luis Ciriaco
luis.ciriaco@insuranceinsider.com

SUBSCRIPTION SALES SUPPORT
Paul Mansfield
paul.mansfield@insuranceinsider.com

HEAD OF MARKETING & ANALYTICS
Lynette Stewart
lynette.stewart@insuranceinsider.com

BRAND MARKETING & ANALYTICS MANAGER
Aimee Fuller
aimee@insuranceinsider.com

EVENTS MARKETING ASSISTANT
Luke Kavanagh
luke.kavanagh@insuranceinsider.com

EVENTS DIRECTOR
Sara Donaldson
sara.donaldson@insuranceinsider.com

CONFERENCE PRODUCTION MANAGER
Matthew Sime
matthew.sime@insuranceinsider.com

CONFERENCE PRODUCER
Miraal Mayet
miraal.mayet@insuranceinsider.com

EVENTS OPERATIONS MANAGER
Holly Dudden
holly.dudden@insuranceinsider.com

EVENTS EXECUTIVE
Amelia Blanks
amelia.blanks@insuranceinsider.com

PRODUCT MANAGER
Carlos Pallordet
carlos.pallordet@insuranceinsider.com

DATA ANALYST
Khilan Shah
khilan.shah@insuranceinsider.com

PRODUCTION EDITOR
Ewan Harwood
ewan@insuranceinsider.com

SUB-EDITOR
Steve Godson
steve.godson@insuranceinsider.com

JUNIOR SUB-EDITOR
Simeon Pickup
simeon.pickup@insuranceinsider.com

SENIOR DESIGNER
Mike Orodan
mike.orodan@insuranceinsider.com

1st Floor, 29 Ludgate Hill, London, EC4M 7JE, UK, Tel Main: +44 (0)20 7397 0615, Editorial: +44 (0)20 7397 0618, Subscriptions: +44 (0)20 7397 0619

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