FINANCIAL SERVICES INDUSTRY

2023 MID-YEAR INSURANCE INDUSTRY UPDATE

In this review, A&M's Insurance team revisits the predictions made early this year, providing an update on how the outlook for UK and Europe insurance industry has progressed so far. Additionally, we share two further themes that we believe are emerging in the second half of 2023.

If you missed our previous outlook of the insurance market, you can access it here.

REPORT CARD – REVIEW OF OUR OUTLOOK.

01 Cost-of-living crisis **continues to impact all the insurance sub-sectors**

High inflation is expected to persist in the UK until early 2024, and the cost-of-living crisis is unlikely to abate in the second half of the year.

In January 2023, the Financial Conduct Authority (FCA) estimated that around 6.2 million people had cancelled or reduced cover on their protection policies since May 2022[1]. According to a report[2] from Royal London Group in April 2023, 5% of individuals have already decreased or stopped their pension contributions, while another 5% have reduced or stopped their protection premiums to cope with the rising cost of living. Additionally, the report also found that that 8% and 9% of respondents intend to lower or stop their pension contributions and reduce their protection cover, respectively.

Rising inflation has also driven the sales of annuities, which grew by 22% in the first three months of 2023[3] .

Insurers and providers have experienced increased claims and costs, including fraudulent claims. This has led to more rigor in claims assessment and increased settlement times. Subsequently, insurers have increased premiums, an average of 15% for motor insurance[4] and 6% for buildings and content insurance[5] in Q1 2023 compared to Q1 2022, to account for inflation leading to improved H1 2023 results.

This is developing against a backdrop of growing scrutiny over how customers are treated. With the implementation of Consumer Duty at the end of July, insurers now need to demonstrate that they are treating customers fairly during challenging times.

As we predicted, the cost-of-living crisis has proven to be at the forefront of influences on the insurance industry in 2023 and will undoubtedly be a continuing theme for the rest of the year.

[1] https://www.fca.org.uk/publications/financial-lives/financial-lives-january-2023-consumer-experience
[2] https://www.royallondon.com/articles-guides/cost-of-living/cost-of-living-report/
[3] Pensions Expert, https://www.pensions-expert.com/Law-Regulation/Annuities-are-back-in-fashion-but-take-up-needs-to-be-a-long-term-trend
[4] https://www.abi.org.uk/news/news-articles/2023/5/above-inflation-costs-for-insurers-continue-to-put-pressure-on-motor-insurance-premiums/
[5] https://www.abi.org.uk/news/news-articles/2023/5/below-inflation-rise-in-the-cost-of-home-insurance/

02

Broking and risk transfer markets **continue to see consolidation**

The broking and the risk transfer/bulk purchase annuity (BPA) market led M&A and consolidation in the first half of the year. Howden has been one of the most active, acquiring brokers across the UK and Europe to build its cross-geography expertise and capabilities. Recently, Clear Group acquired two UK regional brokers focused on commercial insurance.

The BPA market saw deals involving Aviva (two transactions), Legal and General, PIC and Just Group. According to data from Autonomous Research, H1 2023 saw £20.3 billion of bulk annuity volumes, 15% higher than the previous record of £17.6 billion in H1 2019. Given the buoyant BPA market and multiple transactions, the Prudential Regulation Authority (PRA) has cautioned the industry to show restraint and discipline.

Within the Master Trusts space, NatWest acquired an 85% majority shareholding in Cushon for £144 million. Across the protection insurance market, Chesnara acquired Canada Life's UK individual protection book while Royal London Group acquired Aegon's individual protection book.

Aligned to our outlook, M&A and consolidation will continue in the second half of the year. In addition to the broking and the BPA markets, we expect to see some deals in the master trusts space given significant interest from corporate buyers and investors.

03

Technology has **become more critical to product innovation**

Over the past six months, technology has taken centre stage, driven by the enormous interest in ChatGPT and the rapid growth of generative AI. Insurers are actively exploring potential applications to incorporate generative AI capabilities into their products and operations. AXA, for instance, has taken a significant step by introducing AXA Secure GPT, an internal service built on Microsoft's Azure OpenAI Service, which is initially available to 1,000 employees at AXA Group Operations. They can use the tool to generate, summarise, translate and correct texts, images and codes[6].

In addition to generative AI, we have also seen growing adoption of technology-led product innovations such as embedded insurance and parametric insurance. ING Group and Qover have recently partnered to introduce a new embedded insurance offering underwritten by AIG, targeting ING's premium bank account holders. AXA and Kayrros are collaborating to introduce a new wildfire risk prevention service across France and Swiss Re and ICEYE have launched parametric flood cover in New York.

We see more insurers and financial services companies investing in technology, including adoption of AI and data analytics, to bolster their capabilities, aiming to create comprehensive ecosystems and expand their range of products and solutions.

[6] https://www.axa.com/en/press/press-releases/axa-offers-securegenerative-ai-to-employees

LOOKING AHEAD

The first half of the year has been eventful, and looking ahead, we anticipate two additional trends to emerge.

01 Insurers **will focus on cost and efficiency**

UK insurers reported worse profits and in some cases losses in 2022 driven by underwriting performance, weak pricing, increase in claims (motor) and weather events (home insurance). Due to the challenging environment of late, insurers will increase their focus on cost reduction and efficiency initiatives. We expect companies to implement initiatives such as operating model optimisation, product rationalisation, IT simplification, digitalisation and automation. This also means that insurers may retrench to their core lines of business and drive sector consolidation.

02 Investments **into fintech and insurtech**

M&A and investments into fintechs from incumbent insurers have been muted so far this year in contrast to the previous years. However, we observed Admiral Group's acquisition of online insurer Luko and Direct Line Group's acquisition of ByMiles, a provider of pay-by-mile insurance policies.

With depressed valuations and insurtechs due for another funding round, we believe it is a favourable time for insurers to consider acquiring and investing into these businesses. As a result, we expect increased transactions in this space.

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