Commercial resilience in the insurance sector

April 2020

Impacts and outlook

Analysis of the current macro-economic climate points towards a large fall in output in the second quarter of 2020. In some countries this could exceed 10%, as large sections of the economy essentially shut down.

Consumer demand will also suffer as social distancing and low confidence lead to a big drop in discretionary spending, especially for big ticket items like recreation, leisure and travel.

On top of this, investment is likely to decline as the pandemic hits business confidence and cashflow, leaving projects postponed or cancelled, and export demand limited by lockdowns elsewhere overseas.

While the short-term contraction in output is set to be large and result in some long-term scarring to the economy.

In the UK, for instance, Experian's central economic scenario projects that output will rebound swiftly in the second half of the year. The analysis assumes that the outbreak is brought under control within a predicted five-month timeframe.

Imperial College London charts a V-shaped recovery in investor, business and consumer confidence, where financial markets stabilise and tightening credit conditions prove to be relatively short lived.

What solutions could help the insurance sector in the current crisis?

The outbreak of Covid-19 and the economic repercussions of the pandemic look set to last. An economic downturn is anticipated with significant impact to the world economy. The effect on the insurance industry will be unprecedented. Although a global pandemic was recognized as the biggest risk to the sector several years ago, the insurance industry has made very little progress in the meantime in preparing for it.

Despite the solvency positions of the European insurers being generally sound, the crisis is expected to deeply impact their exposure levels, provisioning, capital requirements and profitability. Insurers' operations will also be influenced by rising risk across the whole economy, increasing number of claims, as well as potential new regulations aimed at mitigating the impact of the economic downturn. Due to the nature of the sector, insurers will face difficulties.

Life insurance, travel, health and specialists handling high-value risks are particularly exposed. Re-insurers are also expected to be particularly affected and are projected to show a decline in their credit quality. Elsewhere. mid-size insurers could see some of their lines fully used, even though they generally use policy limits and exclusions. For property and casualty, greater impact may be driven a global fall in activity. Beyond public health, three of the most significant expected impacts to the insurance industry stem from cancellations in travel, shelved events alongside a loss of revenue.

Policy coverage will depend on individual circumstances and the specific insurance, but there are some general themes now emerging.

Impact on life insurers[1]

- Industry analysts believe claims are broadly expected to be manageable, given the relatively low mortality rate for infected individuals.
- The adverse reaction of financial markets to the coronavirus outbreak may affect insurers' profitability, including earnings generated from their investment portfolios.
- Insurers operating in higher-risk countries are now seeing some disruption in their day-to-day operations, which will likely have an impact on revenues.

The outbreak is also likely to affect life insurers in the following ways:

- Increased incurred claim costs, including death and disability claims and drug costs.
- Adverse movements in the financial markets, including declines in bond yields, equity markets, and real estate, all reducing profitability.
- Business interruption and potential impact on revenues.

[1] http://www.actuarialpost.co.uk/article/the-impact-of-coronavirus-on-life-insurers-17931.htm

Impact on property and casualty insurers[2]

Key highlights include:

- Insurance clients in the hospitality and tourism sectors are particularly exposed to incurring losses as a result of large-scale cancellations.
- Event cancellation insurance is most likely to be negatively affected compared to other policies. However, as mentioned above travel, business interruption, workers' compensation, and general liability policies may also be affected.
- The most apparent impact for insurance companies in the short-term will be in the reporting of realized, or unrealised gains, from equity market fluctuations and movement in interest rates. This will be partly mitigated by higher underwriting revenues because of hardening of global insurance markets.

The outbreak will likely affect property and casualty (P&C) insurers in the following ways:

- Underwriting results may not be affected materially for the time being. However, claims will start to manifest in some niche industries like hospitality, tourism, transportation and entertainment, as trips and events get cancelled, or infections rise.
- Equity market fluctuations and cuts in interest rates by central banks to limit the economic fall-out from coronavirus may also affect investment income following fluctuations in realised and unrealised market losses. Therefore, the most immediate impact for P&C insurance companies will be in the valuation of equity investments and fixed-income assets – both of which are affected by equity and bond market volatility.

Improve market position and support growth of digital acquisition channels

Shifts in consumer behavior and working habits are expected to drive the adoption of technology and digital processes for on-line customer acquisition, distribution channels and digital insurance payments. Accepting the wrong customers, or offering the wrong premium, may incur significant costs that directly impact the insurer's overall profit. Fraud and risk assessment in the insurance sector needs to consider external sources of information to ensure acceptance of the right customers. External data could also be used for targeted products and offers based on more granular segmentation and channel preferences, as well as matching insurance premiums to predicted claims potential.

Solutions based on a correlation between external data such as geo-marketing, payment behavior, fraud or web data and insurance claims, could greatly enhance the diversification of distribution channels, digital acquisition of customers, efficient and appropriate risk-based pricing schemes.

[2] http://www.actuarialpost.co.uk/article/impact-of-coronavirus-on-property-and-casualty-insurers-17970.htm

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Focus on customer management

Downturns drive greater focus on customer value, relationship and retention management. It's also important to note that external data and scores could support not only underwriting practices, but also play a very significant role in growing relationships with existing customers. Bureaux, alternative data and scores, as well as ML&AI applications could help a more-informed understanding of existing customers profiles. Tailored price offers to existing low-risk customers will also help improve conversion rates, loyalty and retention. External data, as well as advanced analytics, are also very powerful tools for detecting insurance claims fraud by ensuring that false positive rates are kept at an efficient level.

Bureaux, alternative data and scores, as well as machine learning and AI are key elements in insurers' strategies for their transition to digital acquisition and customer management channels. They also offer improved fraud detection, better service to customers and decision-making for insurers.

Update of acquisition and customer management models and strategies

Population shifts happen a lot more during downturns. They affect models and strategies built on historic data, prompting a pressing need to recalibrate acquisition, customer management models and strategies around emerging shifts in risk profiles. It also offers a timely opportunity to adopt alternative data as well as machine learning and AI applications in evaluating new applications or managing the existing portfolio. Both are valuable routes to up-to-date insights and better-informed insight into key segments such as SMEs.

Modification of application, customer management models and strategies, are among the first critical steps insurers must take to manage the impact of the crisis on their portfolios.

Operational efficiency within the organization

Insurers are expected to face rising operational risk due to the closure of office operations, while suffering capacity issues from staff sickness, higher risk-management demands and on-site work restrictions. Areas like analytics are core competencies for insurers, but they're focused primarily on the assessment of risk. However, deep fraud, customer profile and customer behavior insights could all help insurers better-manage the impact of a downturn. Therefore, insurance companies will benefit from outsourcing strategies which provide the right mix of internal and external capabilities.

Near-shoring and cloud-based collaboration platforms drive operational efficiencies in insurers' key competence areas such as analytics

How we can help

The circumstances we find ourselves in are unparalleled and changing daily. The way we prepare to weather the impact in the short-term will be key to making sure its long-term effects are contained as much as possible – both for the customers in our care and for our own businesses.

If you'd like to discuss any aspect of this report or find out more about how we can support you through this crisis, please get in touch with your Experian account manager today.

While the road ahead may be rocky, and there will be new developments to navigate, we believe that by working together, and bringing you powerful data and tools, we can help you and your customers.

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