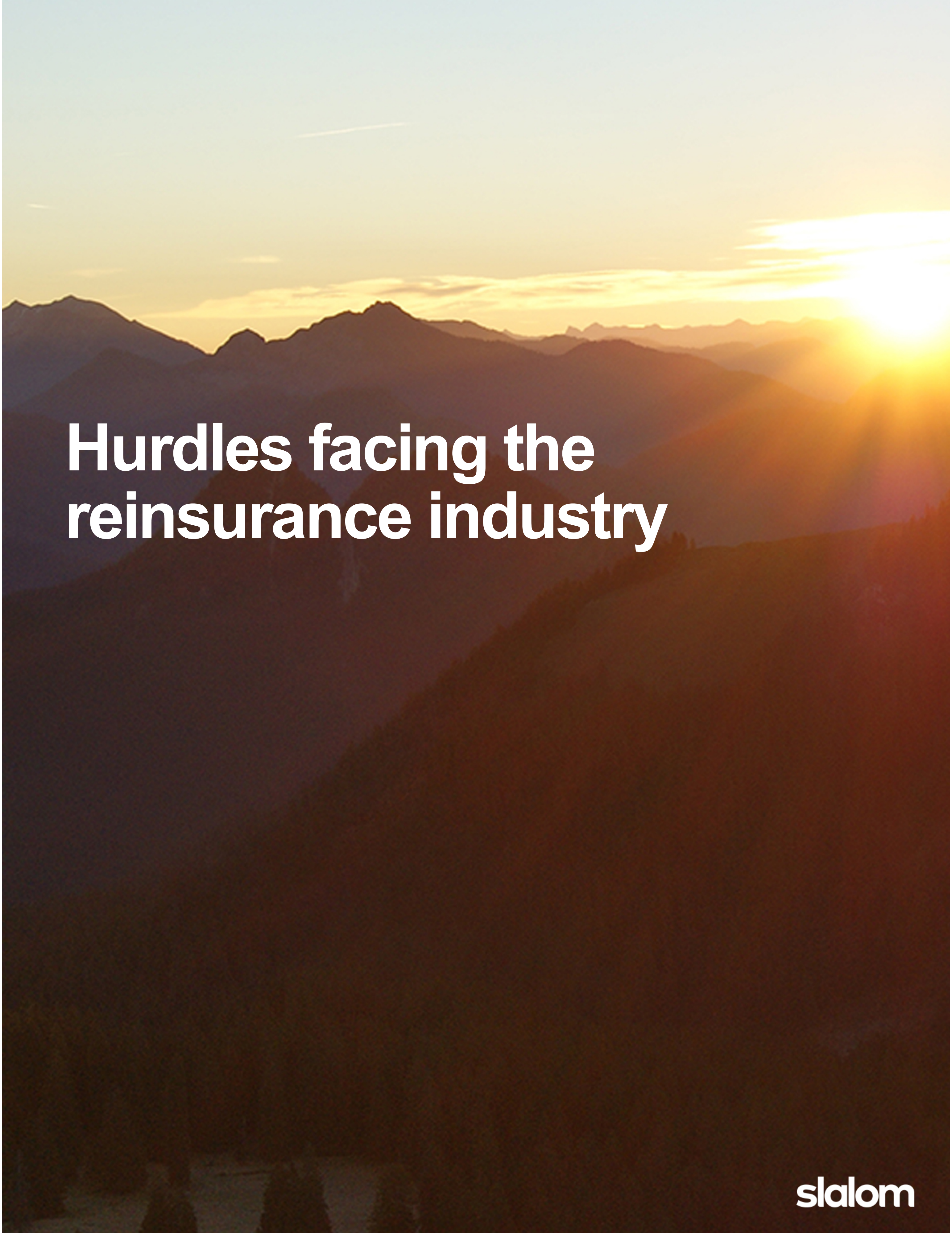

Hurdles facing the reinsurance industry

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Reinsurance has been around for hundreds of years, but the industry currently faces challenges that will require fortitude, organization, and innovation to surmount. From an influx of capital and competition from alternative lenders to regulatory requirements and technological hurdles, the time has never been more ripe for reinsurers to take a close look at their underwriting processes. In the past, “collaboration” may have been a simple buzz word, but now this concept may be central in determining which reinsurers struggle and which weather the storm.

For expert insights, we spoke to Matt Edwards, National Insurance Practice Lead at Slalom; Tom Terry, Managing Director at Slalom; and Stephen Lord, Global CTO and Reinsurance CIO at AXIS Capital, which provides specialty insurance and treaty reinsurance on a global basis.

Excess capital in the market

“Right now we’re seeing an influx of cheap capital into the business,” Lord says. This is the result of the ultra-low interest rate environment dating back to the financial crisis, augmented by a period of quiescence in major catastrophes, which has improved reinsurers’ loss results in recent years. “There’s a massive amount of assets searching for returns … which puts the market under pressure.”

As a result of this competition, reinsurers are searching for new ways to expand, such as exploring new geographies, undergoing mergers and acquisitions, or seeking out different risks. “Reinsurers need to find ways to stand out in the marketplace,” Terry says, lest customers leave them for other types of capital or gravitate toward bigger reinsurers. This also puts pressure on reinsurance companies to get smart about managing client and customer relationships. Lord adds, “What is our relationship with specific clients across all the geographies and products we cover? Reinsurers are becoming choosey about risk selection. Before, anything that generated revenue was good, but now we’re looking not just at revenues but the expected profit of a deal, and beyond that, how that risk correlates with all the other risks we have.”

“Over the years, the reinsurance market has always fluctuated,” Terry says. “But now we’re seeing a fundamental shift in terms of how capital flows into the market. I think the outlook is just less certain for the foreseeable future.”

Disintermediation of traditional reinsurers

The industry is shifting in terms of the classical ways reinsurance risk is transferred, Lord says, particularly through a disintermediation of the relationships between reinsurers, brokers, and ceding insurers. Forms of alternative capital, such as hedge funds and asset managers, are now getting in the game by underwriting risks directly, with less focus on generating underwriting profit. As a result of this competition, “reinsurance brokers are less inclined to involve as many markets, so there’s this winnowing out of the smaller players who have less capacity or global presence. Reinsurers themselves are now going directly to cedents, or forming direct ventures with asset managers to try to co-opt the disintermediation that’s going on and to offer capital a way to be paired up with risk transfer through the auspices of a reinsurance company,” he says.

Increased regulatory requirements

Having a comprehensive picture of one’s full reinsurance portfolio can sometimes be challenging, Edwards says, “but it needs to be addressed, if only because of changing regulations in Europe, the U.S., and in Bermuda, where a lot of these carriers reside.

Reinsurers will have to share a lot more information with regulators going forward, so the more organized you are and the better you capture detailed information regarding risks, the better you'll be able to meet regulatory requirements now and in the future. Not to mention that streamlining your processes while improving the quality and volume of data will help you grow your business in a profitable manner."

Fragmentation in underwriting

"In a typical underwriting process," Edwards says, "when the reinsurer gets a request for an underwriting decision and price quote, they could come in on a piece of paper, email, mail, scribbled down on the back of a file—anything. There's no single point of entry for some of these smaller carriers, which causes inconsistency." As you move through that process in a smaller company, the underwriter traditionally has his or her own approach, such as calculations and decision documentation that are stored on the underwriter's computer but are not necessarily available to the rest of the stakeholders involved in the decision-making process. "That would include the actuarial team, which should be consulted," he says, "or the catastrophe modeling team, which can point out individual risk or broader portfolio issues that the underwriter may not have insight into."

One reinsurance submission might look good on its own, but when you take into account your entire portfolio, that submission may skew your overall portfolio in an undesirable way. During past major catastrophes, many reinsurance companies were unaware of just how exposed they were to particular risks. Terry says, "Maybe you had too much exposure in Florida and then there was a hurricane, or you were reinsuring more banks than you realized and had too much exposure to the financial crisis." Yet, unless you're collecting the right data and operating as a whole business unit, it's hard to understand for sure what you've been exposed to.

Barriers to technological implementation

The reinsurance industry suffers from legacy issues in technology, the accumulation of bad data, and the lack of solid aggregate client data—but many reinsurers have made good strides in fixing their front-end modeling, pricing, and underwriting processes, Terry says, providing an opening to take their technology tools to the next level.

The reinsurance space tends to be less technology-driven than other industries, Edwards says, because the complexity of the business requires more specialized software. Unless a company has enough capital on hand to invest in a large piece of custom software to be implemented by an expensive team of specialists, it is often left to cobble together its own enterprise solutions. "There isn't a large selection of reinsurance-ready applications you can pull off the shelf and get running," Terry says. Despite new technology like data visualization, storage in the cloud, and collaboration tools, small- and mid-size reinsurers haven't typically made use of these options to determine the best solution toolset to manage their books of business.

How can we surmount these hurdles?

Changing corporate attitudes and openness

"Technology is not the silver bullet," Terry says. Before you get into the weeds of a technological solution, it's very important to foster an operating model, culture, and process mentality that helps to facilitate the sharing of information. "This entails more of an enterprise perspective than a business-unit-centric point of view. How do you bring your enterprise data together in a fashion that's broadly understood, so you don't have to accumulate it on your own?" He suggests starting by painting a picture of the end game to gain consensus throughout the organization. From there, you can start to think about a technology platform that would align with the operating model and the company's objectives.

"Achieving this consensus isn't necessarily a technology challenge so much as a major cultural shift that requires support from the top down … Although technology can help, the broader question is how to simplify front-end processes so there's more seamless integration on the back end," Terry says.

Reorienting to a unified client approach

In this increasingly competitive environment, one solution is to start taking a more strategic view of one's client list. Terry says, "The important thing is to be conscious of who your top customers are so you can think about more targeted marketing." Becoming more customer-centric can actually increase profitability, Lord says. "Our reinsurance unit is orienting its strategy around customer segmentation with special emphasis on our top 25 clients, and we can use this information to develop individualized marketing and servicing strategies. Our larger clients will now have a more holistic relationship with Axis, where it's not just about the basic risk transfer but about helping them innovatively manage their capital." Previously, different underwriting product groups might have contacted clients separately to discuss various pieces of business.

It sounds very basic, Terry says, but it's difficult for many mid-size reinsurers to even ascertain who their top 15 customers are, because much of the process is manual. "I've seen some places where the customer actually had a better view of what the reinsurer was doing for them than the reinsurer did. It sounds a little shocking, but it's necessary to have the basic ability to see who you're doing business with, who you want to be doing business with, and who your key contacts are."

Once a company identifies its top customers, it can start to think about their risk appetite, pricing constraints, and product offerings they might be interested in. In other words, "show customers your whole menu rather than having them speak piecemeal to various smaller groups in your company," Terry says. This enables companies to generate proposals on ways their top clients can manage their risk, versus simply receiving their requests passively.

Consolidating one's approach also means removing the overlap between various departments' effort on visits, phone calls, and contacts, giving underwriters extra bandwidth to process more deals. "I would expect to see the number of submissions reviewed by underwriters increase over time," Lord says, "and I'd expect profitability and share within these top 25 clients to increase. I'd expect the whole portfolio to shift to what I'd call higher quality premium. If we can earn the same amount of money while taking on less risk to earn it, that is hugely important, especially since those top 25 clients are a sizable fraction of our business."

Combatting fragmentation through technology

Once an organization is unified around its holistic, client approach, the next step is to start exploring technology solutions that can help execute those changes. "We have pre-built the components necessary for reinsurance solutions using typical Customer Relationship Management platforms," Edwards says. "The first step is to create a single repository as a starting point for all of your relationships. This makes it much easier to answer questions like, 'Who are our primary contacts? What business do we do with them? What business should we be doing with them? Do we have submissions in the queue? How's their performance?'"

On top of standard enterprise software platforms, Slalom built a solution to facilitate the uniqueness of relationship management in reinsurance along with the underwriting process by creating a single entry point for submission information. "It makes sense to build these customizations into an off-the-shelf solution so you can really focus on an individual carrier's process," says Edwards. When you move toward a standardized, single entry point, you can learn key details around your book of business at point of submission: What's the risk you're trying to underwrite? What's the treaty structure? What types of coverages are involved? What are the facts to help you figure out how to price that business and whether you even want to take it on?

A cohesive workflow management system can streamline the process of requesting review by actuarial staff, disaster modeling, legal, and any other stakeholders. The beauty of customizing a solution to your particular business's workflow is that you can create the tools and connections you need. For example, you can build connections between your workflow system and your financial system so all the details around the transaction are collected and sent to the financial ledger. "On top of that," Edwards says, "there's obviously the reporting piece, including visualizations around performance, depicted in geographic views or graphs."

As a client who has been through this process, Lord says, "Slalom helped us create a nexus to see all the activity going on with key clients across the traditional silos of the company, so we can share reports, business plans, strategies, and analytics to show the portfolio metrics already in place. That lets us evaluate future programs both against each other as well as against the ones we've already completed. In the older days, the technology didn't exist, nor was there motivation to implement it, because there was no need to. Now we must be more customer-centric and aware of portfolio and risk metrics than we had to be in the past."

Shifting from a group-based to a portfolio-based outlook

One of the biggest shifts in AXIS's underwriting process is that submissions will now be more rigorously judged for their impact to the company as a whole, rather than just their projected profitability. "We're also looking at correlation and impact to our risk portfolio," Lord says. He hopes that will place more control in the hands of underwriters by helping them make better choices or negotiate better terms involving smaller clients. "In this market, where there's pressure to write business no matter the quality or the risks, at some point you cross a threshold where a deal could be damaging to a company's bottom line and risk position." In the past, he says, a few catastrophically bad decisions had the potential to destroy smaller-scale reinsurers. Shifting from a perspective focused on just one reinsurance group to a viewpoint that incorporates the entire portfolio helps prevent concentrating too much exposure in one place without backing it up with sufficient capital.

Exploring new segments

As a small- or mid-sized reinsurance company trims away business it sees as unprofitable or overly risky, there are many other opportunities available within the $2 trillion reinsurance universe, Lord says. "For example, we're seeing agriculture as a major growth area," he says. "Alternative forms of risk transfer like weather and commodity price hedging have to do with parameterized deals rather than actual physical losses. There's also classical agricultural reinsurance, in which you reinsure agricultural insurance companies." Another way to diversify is to deploy capital to international geographies where there's less penetration and relatively better market conditions, he says. "You can withdraw from what's revealed to be insufficient return on the risk taken, and redeploy to places you wouldn't have considered otherwise. For a company the size of AXIS, there will always be areas we're not yet participating in, where we can go in the future."

Why this is a unique time for innovation

We know that reinsurance companies particularly need collaboration solutions now because of the difficult market environment, but this is also a prime time to create tools that can truly transform a business.

There are more technological resources available now than ever before. For example, Edwards says, "There's a proliferation of coders who understand [how to create collaborative cloud solutions], and there's now a gigantic world of open-source technology to play with, so you're not necessarily locked into having to buy something from a technology company." Previously, he says, reinsurers had to hire people from those companies to implement solutions because they had all the real knowledge. "These days, there's a lot more computer science or information management folks in the marketplace who understand these languages, which provides the flexibility to build custom solutions. That's one of the big things that makes this a great time."

Edwards also looks to the proliferation of mobile devices and technology as a frontier in reinsurance. "A lot of times, an underwriter will be in a broker's office making a list of requests to bring back to the office. New technology means that you can now make a more informed, preliminary decision about coverage on a tablet or mobile device. You can key in the information while sitting side by side with a broker, before you do the heavy lifting and detailed analysis back in the office."

Key takeaways

1. Evaluate where you are; decide where you want to go; and make a plan.

Edwards suggests that any reinsurer looking to streamline data and underwriting processes start with an analysis of the current data environment. "Document what data you have, who has access, and how it's shared within the organization. Next, understand and document your process around underwriting decision making and pricing, such as who should be sharing what data and who should be involved at which stages." Once you've assessed your current environment and where you'd like to go in the future, Edwards recommends performing a high-level gap assessment to see how far away you are from where you want to be. He says, "That will help inform your next move."

2. Get the whole team on board.

Creating a program to increase efficiencies in reinsurance requires a partnership with business owners and stakeholders. Lord says: "Here at AXIS, this was an idea I had independently that happened to synchronize quite nicely with the goals of the segment chief executive who'd recently arrived. Since then, these principles have been embraced by several others. It's key to evangelize these concepts in their own right, outside of the technology. Technology is an enabler, but the critical components are the concepts of being customer centric and having a holistic approach to accessing data early in the process."

3. Apply retail concepts to your business.

Even though reinsurance is not a consumer-facing business, Lord believes that concepts from retail or high-volume sales environments can provide value. “When people talk about something like sales force automation, the examples provided are always around consumer-facing, retail-oriented stuff with large scale,” he says. “They’re low-dollar, high-volume situations, but the idea of being customer focused and capturing metrics around your deal pipeline has value for reinsurance all the same.” In the current soft market that has no signs of abating soon, he insists that these concepts aren’t just a luxury: “They may be a survival imperative.”