DAC BEACHCROFT

Reimagining general insurance

Published 11 September 2018

The very nature of insurance, its role and its relationship with society is undergoing a profound and irreversible transformation. This is not just about managing change and disruption. It is about reimagining what insurance is. The industry has to take a step back and challenge a wide range of assumptions that have underpinned it for generations. This is not easy when the bewildering pace of change sweeping through and around insurance seems relentless, rarely leaving time to reflect on the impact it is having on a sector vital to all modern economies.

Technology and the changing nature of risk

The biggest drivers of this change are technology and globalisation, but alongside them is the changing nature of risk. This ranges from the escalation in terrorist attacks on people (as opposed to property), the threat of major cyber-attacks and the impact of climate change on natural catastrophes at one extreme, to the fragmentation and individualisation of insurance at the other. Changing lifestyles mean the established model of annual insurance contracts is no longer relevant to many people and businesses.

Into this mix must be added the way people communicate with each other and, in particular, the way they wish to communicate with the corporate world that provides the products and services on which modern lifestyles depend. Communication is mobile, fast-moving and social and is fraught with awkward contradictions, especially around privacy. People appear willing to share personal details and yet are increasingly aware of their privacy rights around where their data goes and how it is used.

Reimagining insurance

The combination of these powerful forces is doing more than just reshaping the insurance industry. It is demanding that we reimagine what insurance is for, what society expects from it and how it can deliver the promises that lie at its heart. It also means reimagining the skills insurers and brokers need in order to flourish in the future and what they will expect of service providers, including law firms.

Many of those skills will be transformed – or eliminated – by artificial intelligence (AI). Roles involving the scrutiny and processing of data can now be carried out more efficiently using AI. This includes roles in underwriting and finance, where once high-level human skills, knowledge and experience were vital.

AI will staff the call centres of the future, interact with customers, answer their queries, sell them policies and process their claims. A small number of human customer service staff will be there for customers with complex needs, but they will be far, far fewer. To embrace this aspect of the digital revolution will require investment, but often overlooked is the fact that it will also require writing off some of the major investments of the last two decades in call centres, including the once highly controversial offshoring projects of the major insurers.

It also brings challenges around business continuity and succession planning. What happens when the technology fails, perhaps because of a major cyber-attack? At present, in most businesses, there are plenty of people available who have the knowledge, experience and traditional tools to keep the business running and restore it to its full operational capacity. These are not IT staff, but people who until recently did the jobs that the machines are now performing and so know what to do instinctively when asked to step in. In a decade's time that knowledge and expertise will not be so readily available and companies need to think about how they will replace them.

Similar considerations apply with succession planning – developing the smaller number of highly skilled and knowledgeable people who will control what the machines do, add the vital human element and become the next generation of senior managers shaping the strategy of the industry. In many professional, technical and customer-facing roles these people start at a junior level doing routine, even mundane, work and progress up a career ladder, gaining invaluable experience and insight along the way. What happens when that work is carried out using AI? Where does the next generation of human managers and experts come from and on what should they 'cut their teeth'? This is a challenge across the insurance industry and the professions.

Transforming risk

The revolution in transport technology is one of the most obvious areas transforming risk, with active development towards driverless cars, crewless ships and pilotless planes. As this revolution gathers pace, risk arising from human error will be overtaken by risk of product safety defects, software failures and cyber interventions. This transfer of liability will be felt most acutely on our roads, where over 90% of accidents are currently caused by human error. To quote Alex Glassbrook, barrister and expert in the law relating to autonomous vehicles, the impact on society of 'robots on wheels' will be akin to

the advent of 'horseless carriages' in the late 19th century.

As automation becomes the norm, eventually leading to fully autonomous vehicles, the consumer may not see much change in how insurance works. But behind the scenes, it will be transformed as the fronting insurer seeks to recover from product software and infrastructure manufacturers and their insurers when things go wrong. This, in turn, is prompting manufacturers to seek new ways of mitigating, sharing or transferring risk. We are already seeing a trend towards retention of risk (through captive entities) in a bid to compete for market share by offering consumers the simplicity of a single price package for car, maintenance and insurance. Another commercial imperative is the war for control over personal data, where one of the key outputs from vehicle automation is the generation of data about how, when and where vehicles are driven.

Attitudes to car ownership are changing too and automation will accelerate that trend, especially as we move towards an era in which 'driving' will become a sport relegated to racing tracks. Even now, Generation X and Millennials do not have the same desire as previous generations to own or be responsible for cars. This is linked to a potent mix of other factors such as greater urbanisation, scarcity of property and parking space, enhanced environmental awareness and more flexible lifestyles. The insurance industry needs to respond to that with affordable, short-term insurance that insures people’s mobility (for example, through carpools and daily leasing arrangements) and which is available through the full range of mobile technologies.

That is one of the many implications of what is often termed the sharing economy. The pay-per-click insurance model that is emerging in response threatens established distribution channels dependent on longer-term customer relationships and the commission they generate.

The connectivity now prevalent in developed economies is transforming risk beyond how people buy insurance. The Internet of Things – devices which interact with humans and with each other – is at the heart of this for insurers as it opens up new opportunities for risk mitigation. The monitoring of pipes for potential water leaks is already helping to reduce claims. In the US thousands of agricultural workers are now wearing biometric devices that monitor when they are becoming fatigued or in danger of injury so managers can intervene before injuries and accidents occur.

Connectivity also brings greater interdependency, especially in complex and extended supply chains. All businesses need a greater awareness of whom (or what) they depend on and who depends on them; this helps them to understand fully the risks to which they are exposed and where their liabilities might lie if that connectivity fails or is attacked.

The risk of cyber-attacks constantly grows with criminals developing new lines of attack faster than adequate responses to the existing threats can be devised. With cyber-terrorism now a serious threat and cyber warfare between states a reality, the need to rethink the scope of cyber risks and how the insurance industry responds to them has become urgent.

Terrorism and malicious acts have not just inevitably found an outlet in the digital world but are changing their nature in the physical world too. Previous manifestations of terrorism, especially in the UK, have largely been focused on property. By the 1990s, that caused sufficient strain on the insurance industry that Pool Re had to be set up with the Government standing behind it as reinsurer of last resort. Present day terrorism has changed its focus from causing property damage to causing human casualties and business disruption. This fundamentally changes the insurance risk. The Government has recognised this in its recent commitment to amend the 1993 Reinsurance (Acts of Terrorism) Act to enable Pool Re to extend its cover to include non-damage business interruption losses resulting from acts of terrorism.

As man-made risks grow rapidly, so do natural catastrophes, although at their heart may lie another man-made factor climate change. As reported by Munich Re, 2017 was the worst year on record for insured losses through natural catastrophes, but also one that highlighted the growing gap between insured and total economic losses. This has prompted a search for fresh solutions.

A brave new world

The answer to the changing face of risk does not lie exclusively in the hands of the insurance industry. New forms of capital from the InsurTech sector are being attracted into a market striving to find solutions to providing cover for mega-risks, and innovators are constantly reinventing the relationship insurers have with their customers. There are new partnerships, new solutions and innovations emerging, which will require more dynamic and flexible partnerships between insurers, businesses, regulators and governments to ensure they can flourish. Commerce is, after all, driven by consumer forces.

In the reimagined insurance industry the boundaries between private and public will become intertwined, much as they have already with pooling arrangements for some risks and with the emergence of parametric insurance for some previously uninsured catastrophe risks. It will also require regulators to move at a pace that supports and does not inhibit the industry in responding to the changes in how society wants to buy insurance and interact with the industry.

Forging this new relationship with society, governments and regulators will in itself require imagination as the relationships between states and the private sector are often defined by history and legacies that are hard to challenge. It is all about imagination. Those with the imagination and courage to apply it will thrive in the digital age and meet the challenge of protecting society against the consequences of risks that are transforming apace.

Authors

Helen Faulkner
London - Walbrook
+44 (0)117 918 2225
hfaulkner@dacbeachcroft.com

Wendy Hopkins
London - Walbrook
+44 (0)20 7894 6863
whopkins@dacbeachcroft.com

DAC BEACHCROFT