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Insurance Growth Report 2023

Mid-year update

Interactive PDF
optimised for desktop

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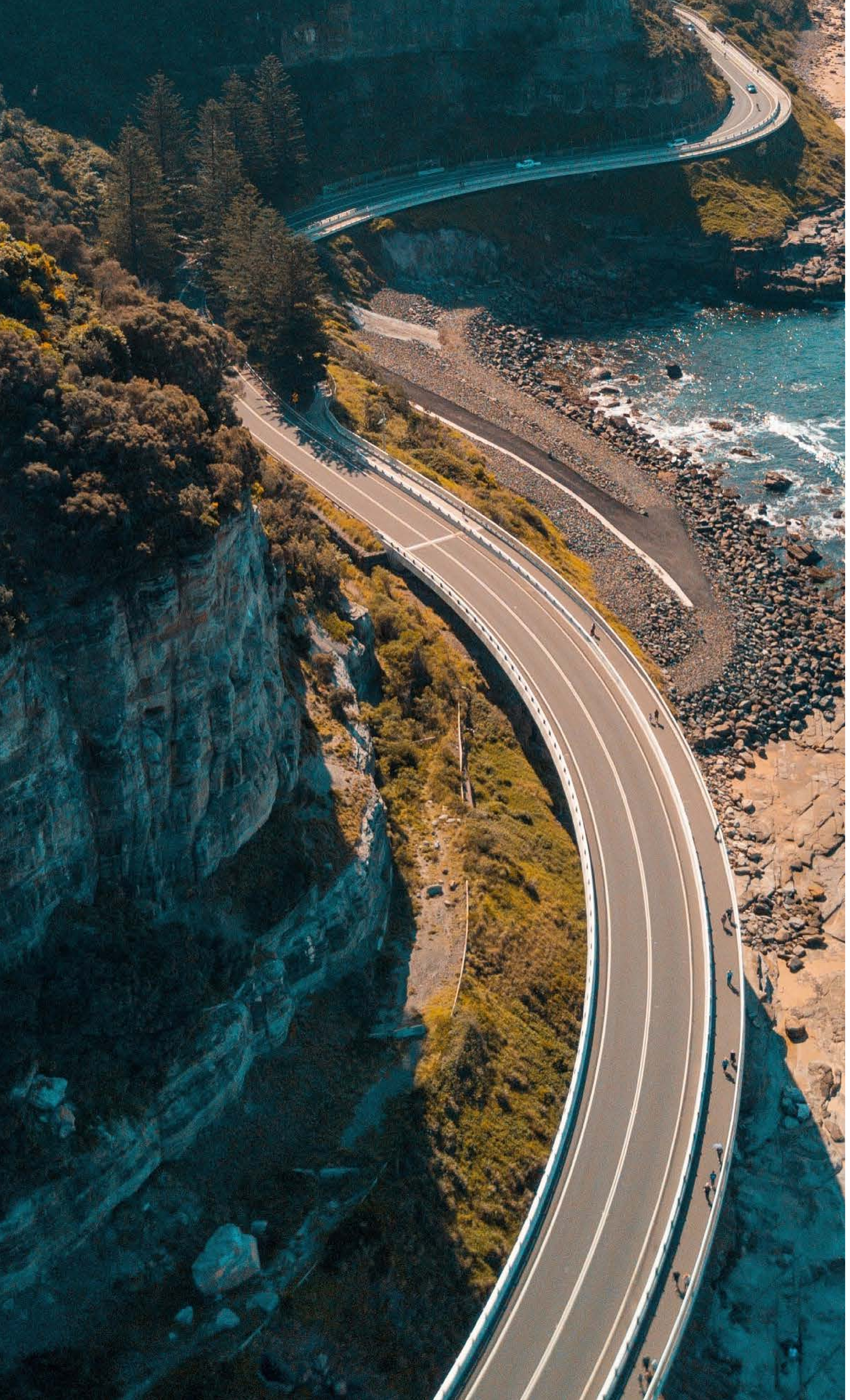

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Introduction

Welcome to the Insurance Growth Report 2023. This report provides market data alongside insight and analysis from Clyde & Co's global Corporate & Advisory team, exploring how insurers are growing and developing their businesses in the face of an opportunity rich, but increasingly volatile and risky business landscape. Our Corporate & Advisory team are adept at helping organisations successfully explore opportunities and navigate associated risks so that they can realise their ambitions.

Despite a continuing hardening market in many lines of business, the growth outlook for insurance businesses remains uncertain in the face of continuing geopolitical uncertainty and economic volatility.

As the property and casualty market struggles to maintain premium volumes in more challenging classes such as financial lines, and with some corporate buyers choosing to self-insure rather than pay higher risk-adjusted rates, carriers are looking at all available options for increasing revenue while mitigating potential risks across the insurance landscape.

While a merger or acquisition remains an attractive way to deliver synergies, scale and reach, insurer M&A activity has dropped significantly. After reaching a 10-year high last year, there were 171 completed deals worldwide in H1 2023, down from 207 in the second half of 2022. All regions, with the exception of Middle East & Africa, have been impacted. Deal size has also dropped with fewer mega-deals – those raising over USD 1 billion – getting over the line.

Given that growth in M&A activity typically lags behind improvements in underlying market conditions by anywhere from eight to 12 months, these developments are unsurprising. However, we anticipate that the volume of transactions will start to rise again towards the end of 2023 as insurance businesses acclimatise to the new operating environment, with the broker segment leading the way. There are certainly opportunities for savvy businesses able to respond rapidly to a positive shift in markets.

In the Projects and Construction (P&C), space, there is an appetite for purchasing monoline carriers in classes of business the buyer doesn't already underwrite, while regional distribution partnerships, and the use of MGAs, are seeing an uptick in activity.

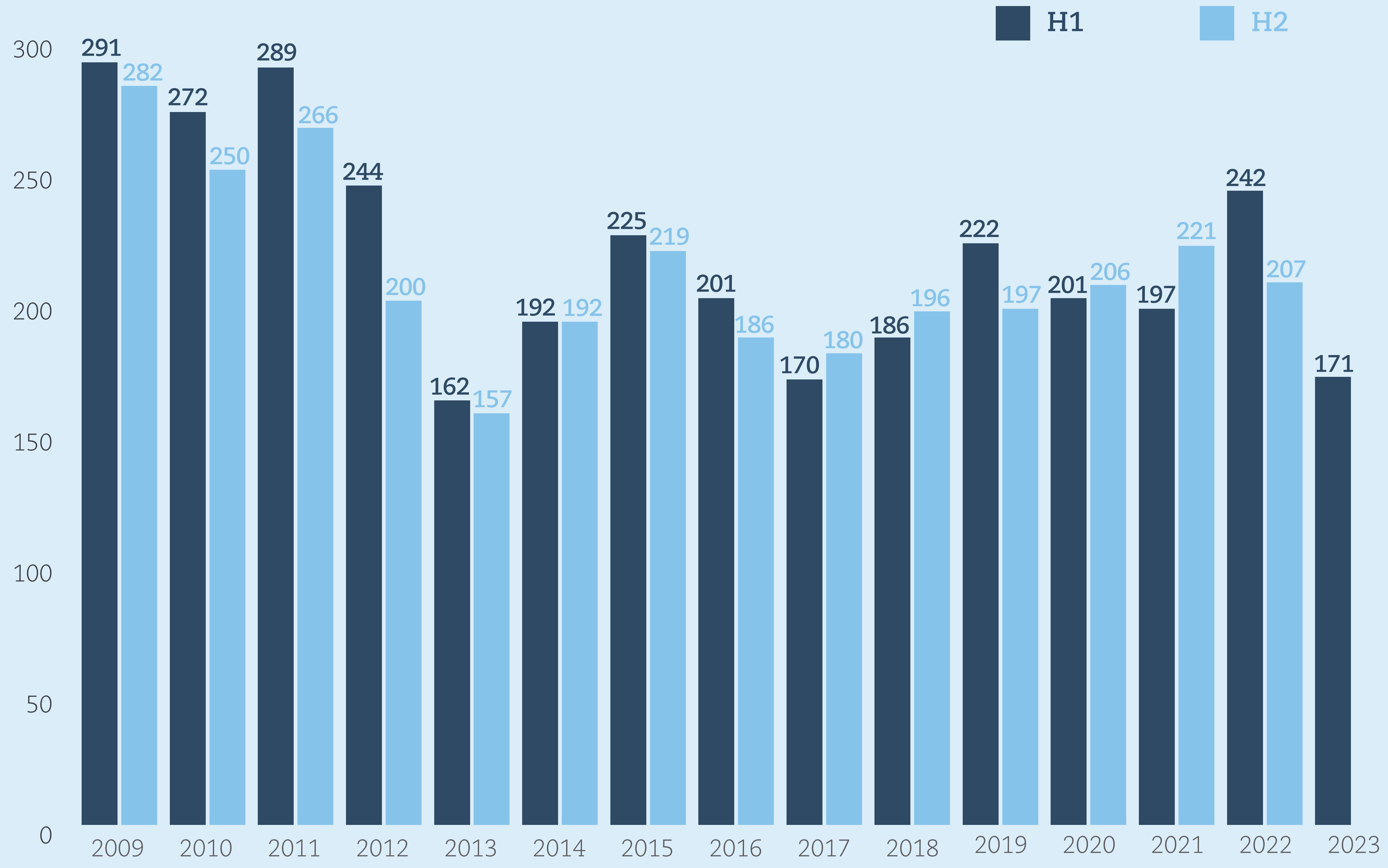
In the London market, there appears to be growing interest in Lloyd's, with capital seeking to enter via full syndicates, special purpose arrangements, and syndicates-in-a-box – vindication, perhaps, of the hardline stance taken with Lloyd's Decile 10 review.

Those with growth ambitions are also looking further afield. International capital has been re-entering the Middle East through investments in regional brokers and third-party administrators. Meanwhile, there has been an uptick in interest from those looking to penetrate the US market via strategic acquisitions to obtain direct access to the world's largest insurance market. After a challenging few years, insurers who can successfully navigate continued economic and political risk are starting to see returns on their investment, avenues for growth and the potential to futureproof their business.

The lull in insurer M&A will be short-lived. Despite ongoing geopolitical and economic uncertainty, insurance businesses are adopting a ‘Keep Calm and Carry On’ approach. Carriers are less dependent on bank financing for strategic transactions as they are restricted to leveraging a smaller proportion of the transaction anyway. With insurers typically balance sheet-heavy at present, the break in carrier M&A activity is likely to be over. Meanwhile, private equity capital is returning to the market for broker deals.

Eva-Maria Barbosa, Partner, Munich

M&A activity drops in H1 2023
Volume of deals completed globally, 2009–2023



Source: Refinitiv

Number of mega deals drops sharply

- There was only one transaction in **H1 2023** valued at over **USD 1.0 billion**
- There were **19** in the whole of **2022**

Large deals spread evenly across the globe

- US and Japan had six deals each of the **top 20**

Cross border activity holds fast

- There were 38 completed cross-border deals in **H1 2023 - 22%** of the global total, this year compared with **21.5%** last year.
- **18 of 38** cross-border deals were inter-region – **47%**

Activity down in all regions except Middle East and Africa

Region	H2'22	H1'23	% change
Global	207	171	-17.4%
Americas	104	79	-24.0%
Europe	60	47	-21.6%
APAC	33	29	-12.1%
MEA	8	9	**12.5%**

Five growth drivers to watch

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1 Cyber offers growth opportunities, but also challenges

Cyber continues to rise up the leaderboard, both as a growth opportunity for carriers and a risk management concern.

The potential impact of cyber exposures on deal-making is a growing focus for M&A deal-makers. Anecdotally, many acquirors have revealed that due diligence around cyber risks of target companies has risen from a top ten to a top five concern when considering potential acquisitions.

Correctly worded warranties in relation to IT systems and cyber issues are a key concern, as the broad wordings in existing agreements are less likely to pick up potential post-transaction issues.

Many corporations are still not adequately prepared for cyber incidents, and are seemingly unaware of the regulatory, liability, litigation, contractual and reputational risks around cyber.

Underwriting cyber coverage continues to offer significant business opportunities, therefore, but carriers need to be mindful of the potential for extensive contingent business interruption exposures in insureds' supply chains, which can cause losses to quickly escalate.

The development of GDPR-style data protection laws across a number of jurisdictions, particularly in the Middle East, is likely to drive uptake of coverage, as regulatory enforcement actions increase awareness of the risks around data collection and storage.

Both insurance buyers and carriers also need to be aware of potential litigation risks on the cyber landscape, such as those relating to the Illinois Biometric Information Privacy Act (BIPA) and various metapixel litigations in the US.

A real risk of cyber incidents is the nature of interlinked systems when there is a compromise, and the related legal issue of who is the data controller. When a purchaser acquires the target company's data, will the contract make it clear who retains responsibility? Is there an understanding of legacy data that it might be acquiring? If data is compromised, the relevant entity may be subject to scrutiny and liable for potential regulatory fines.

Rosehana Amin, Partner, London

The uptake of cyber insurance in the MEA region is still fairly limited. As a result, there's a huge governmental focus on promoting preventative measures available to businesses and an education drive by brokers to address the lack of understanding around what cyber insurance can do. We are at a turning point in terms of changes in the local laws and regulations which will have a significant impact on the risk landscape – including the introduction of stringent notification requirements in relation to personal data breaches – resulting in greater interest in and need for cyber insurance.

Olivia Darlington, Partner, Dubai

2 Regulation is both an aid and hindrance to growth

Regulatory activity across the globe is having a two-fold impact on growth, with enforcement activities expected to put the brakes on some insurance activity due to the increased cost of doing business, while new legislation in other territories is helping to drive new business opportunities through the acquisition of companies, business units, and legacy portfolios.

In Hong Kong, the Legislative Council is considering draft legislation for a risk-based capital regime for insurers, expected to come into force in 2024. Under the regime, well-managed insurers are likely to benefit from lower capital requirements, but those with higher risk profiles will likely need to hold more capital. This could potentially drive M&A activity including transfers and restructuring of legacy/long tail portfolios in future, if operating in Hong Kong or running a certain business line proves too capital-intensive for some.

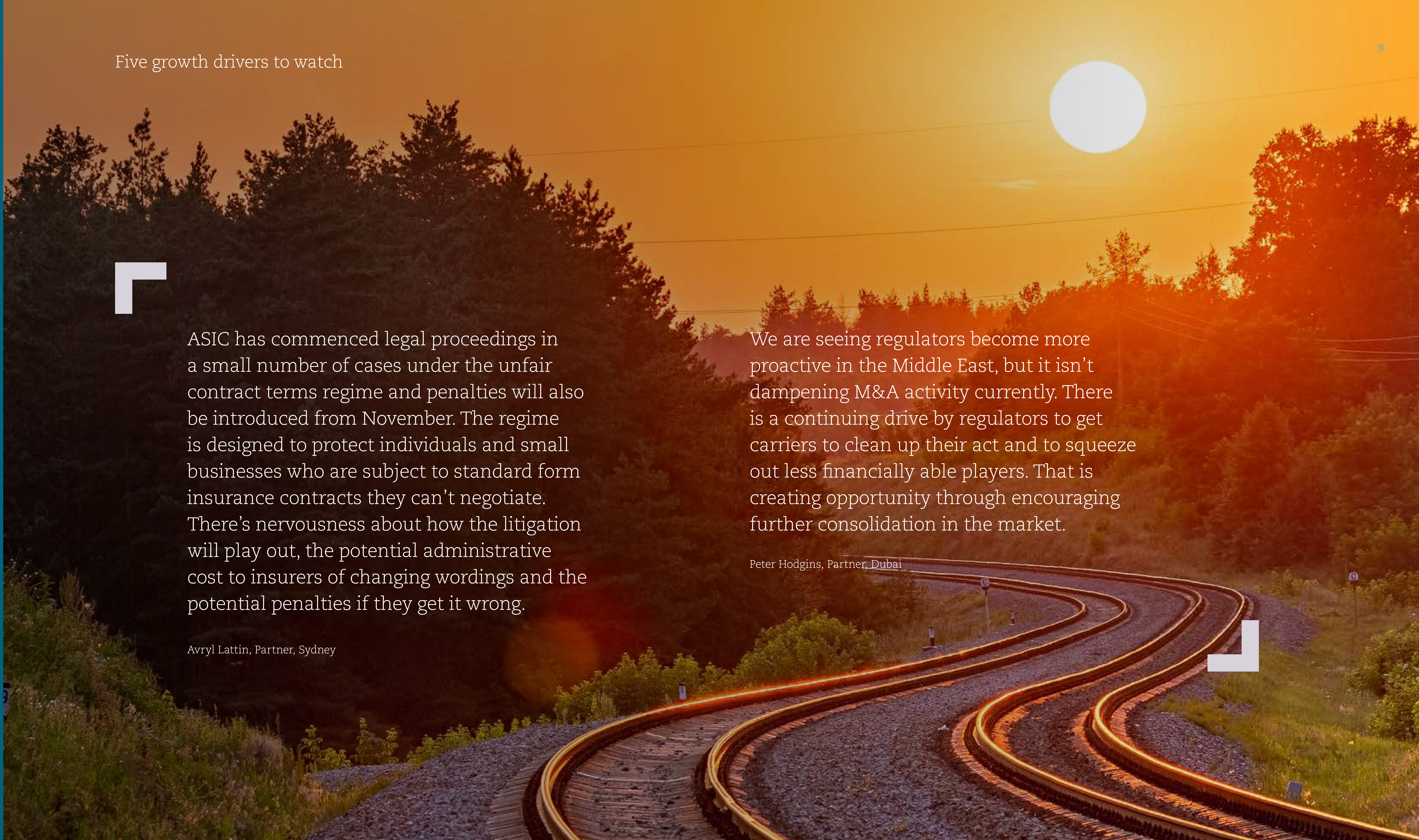
The insurance sector in Australia is anticipating a higher compliance burden for incoming regulations. There is growing anxiety about the cost of changing policy wordings and the potential exposure to significant penalties under the unfair contract terms regime, as the Australian Securities and Investments Commission (ASIC), commences initial proceedings against a handful of carriers.

The Australian Transaction Reports and Analysis Centre AUSTRAC regulations for anti-money laundering and counter-terrorism financing are now being actively enforced against banks and casinos, raising concerns that it could ultimately impact directors' and officers' coverage.

Australia's Financial Accountability Regime (FAR), will soon take effect, although there will be an 18-month transition period for companies to comply. The regime is expected to add significantly to carriers' administrative costs, as they address its requirements for nominating senior executives as 'accountable persons' in every area of their business operations and ensuring they have systems to monitor and report on compliance, and to ensure their accountable persons can satisfy their obligations.

In the Middle East, there is a growing regulatory burden for the insurance industry, particularly in Saudi Arabia and the UAE. In line with previous initiatives by the Saudi Central Bank, the Central Bank of the UAE has implemented corporate governance regulations for the sector, with regulatory investigations and fines expected for insurers that fail to meet expected standards.

While this activity will continue to squeeze out less financially strong and well-structured insurance businesses, it will also force incumbents to adopt international best practice and open up M&A opportunities as the market consolidates further.



ASIC has commenced legal proceedings in a small number of cases under the unfair contract terms regime and penalties will also be introduced from November. The regime is designed to protect individuals and small businesses who are subject to standard form insurance contracts they can't negotiate. There's nervousness about how the litigation will play out, the potential administrative cost to insurers of changing wordings and the potential penalties if they get it wrong.

Avryl Lattin, Partner, Sydney

We are seeing regulators become more proactive in the Middle East, but it isn't dampening M&A activity currently. There is a continuing drive by regulators to get carriers to clean up their act and to squeeze out less financially able players. That is creating opportunity through encouraging further consolidation in the market.

Peter Hodgins, Partner, Dubai

3 Insurtech is still a boom market – for some

The insurtech boom of recent years may have died down in some territories, but in other markets appetite is strong for investment in these businesses.

In Europe, finding capital for insurtech businesses at any size or stage of development is proving difficult. While the reason for investors' hesitancy is unclear, continuing inflation and rising interest rates have driven up the cost of capital, likely persuading private equity to sit on its money in the near term.

In the US, the drop-off of investment continues, perhaps due in part to the lack of true insurtechs coming to market – rather than traditional carriers seeking new distribution channels – and a lack of novel insurtech concepts. As the use of AI in insurance becomes better established, investment is likely to return to insurtech – as the sector best-placed to leverage the emerging technology.

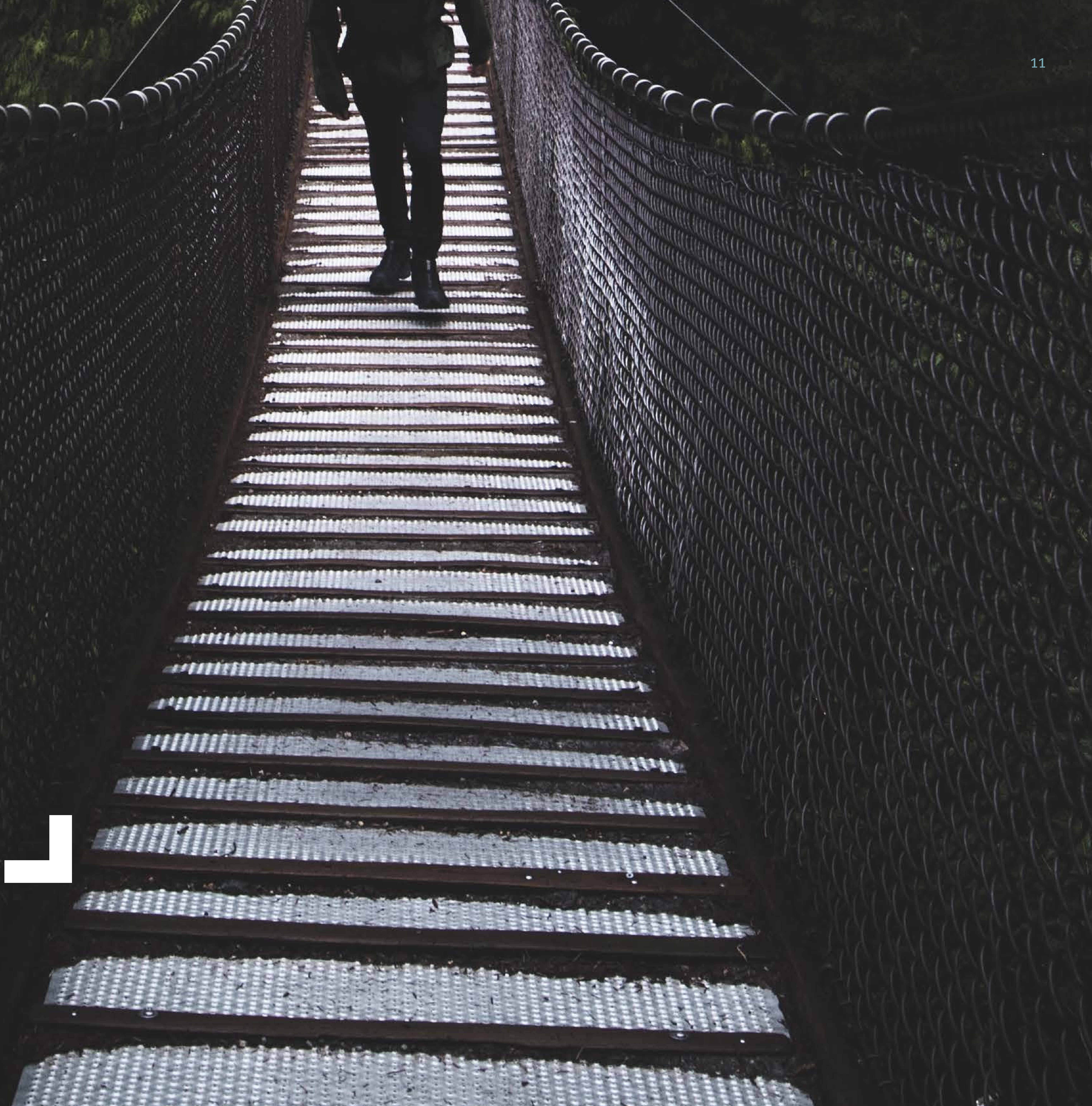
Across Asia there has been significant development in the insurtech space, particularly in countries with high levels of internet penetration – including Indonesia, Vietnam, the Philippines, and Thailand – for a range of personal lines business.

In Latin America, Chile recently passed the Fintech Law which not only covers regulation of insurtechs, but also explicitly addresses the use of parametric structures.

Immediately following the legislation the Chilean government established a $630 million parametric catastrophe bond for earthquake, developed in partnership with the World Bank. Longer-term, however, the new law is also expected to drive investment in insurtechs for retail and commercial products.

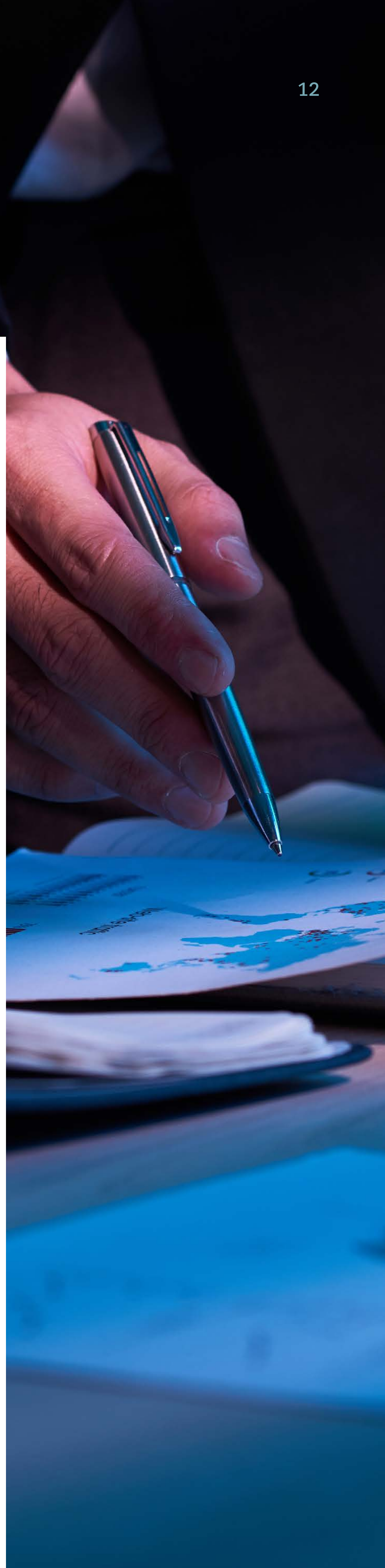
> Private equity firms are looking to invest in tech players across Asia, at all stages of development, with prospective capital providers fairly evenly split between international PE firms and regional asset managers.
>
> Joyce Chan, Partner, Hong Kong

> Many startups have chosen Chile as a regional hub and there are promising growth opportunities here for insurtechs. Once insurtechs attract sufficient attention to get initial financing from local banks and companies, the next funding round will see them looking to the US, where there is tremendous interest in investing in Latin America.
>
> Felipe Hoetz, Partner, Santiago



> It’s a challenging market for insurers, in terms of competition on rates and identifying good quality risks. Teaming up with a programme agent to get products out in the marketplace and to generate more premium is worth the additional commission. There are a lot of insurers who want to do business that way.

Marc Voses, Partner, New York



4 MGAs still buoyant, but embedded insurance is the hot ticket

The distribution space is experiencing a great deal of activity currently, as both brokers and insurers pursue alternative opportunities for growth. While some of the mega-mergers anticipated in the European broking market failed to materialise, held back by economic uncertainty, there is likely to be more movement on deals in the second half of this year. In the US there is strong appetite for broker acquisitions, predominantly of small, medium-sized and some national broking businesses.

MGA partnerships are proving to be popular in many regions, despite speculation that the insurance market might have reached 'peak MGA'. The market is growing substantially in both the UK and US, with some continuing growth also seen in Europe. In the London market there is also a healthy appetite for MGA acquisitions, as an easy route to acquiring a healthy book of business.

At the same time, the rules around the proportion of retail business that can be reinsured by UK insurance branches have become more onerous. Carriers who would have typically reinsured a significant proportion of their business may be forced to recapitalise in order to meet the requirement to retain at least 50% of the risk. This could see some carriers retrench from the market to cut costs, opening up opportunities to acquire books of business for insurers with capacity to spare.

In Asia, insurers are looking to form partnerships with companies across a range of sectors – retail, transport, service providers and others – to expand distribution of their products.

International carriers are looking at a range of options for conducting business in the US – either through domestic start-ups, distribution agreements as non-admitted carriers, or buying ownership stakes in US carriers.

Embedded insurance is the hot topic, however. Despite the modest premium volumes generated, opportunities for selling insurance this way are potentially highly significant, provided carriers have access to a suitable platform for distribution.

As carriers scan the market for gaps in coverage of products and services where insurance solutions can be introduced, new partnership opportunities are emerging for coverage attached to large retail purchases. A significant untapped opportunity for embedded insurance exists within the bancassurance model, which is still a major distribution channel in Asia and the Middle East – but via smartphone banking apps rather than face-to-face interactions in branches.

For more information on the MGA market, click here to read our opinion report.

Regulation of retail insurance business written by UK branch offices is becoming more onerous, particularly for new companies. With carriers expected to retain at least 50% of the business, insurers who previously reinsured 80-90% of their line are now facing dramatically increased capitalisation, making the cost of doing business too expensive for some.

Ivor Edwards, Partner, London

> There's acknowledgement from governments and the insurance industry of the potential for transformation within society that artificial intelligence can bring, and high level policies geared towards allowing and encouraging its use. There is less immediate activity around regulatory controls, but they will inevitably have to come.
>
> Dino Wilkinson, Partner, Abu Dhabi

5 AI is a double-edged sword that few are ready to wield

Artificial intelligence (AI) is the topic du jour, but the lack of substantive regulations governing its use means that while many insurance businesses are developing AI tools, most are at a beta-testing stage rather than being deployed as operational solutions.

As the recent experience of some in the legal profession has shown, insurance businesses need to be cautious in their approach to AI, both in deploying the technology and insuring professionals who are making use of AI platforms.

The use of AI to supplant professional decision-making is likely to feature, in the near-term at least, as a policy exclusion in professional indemnity/liability covers.

Currently, AI technology is finding widespread use as a customer service tool, with chatbots being used to improve the user experience for clients accessing online services.

Insurtechs, whose business models are typically predicated on automating many manual underwriting and claims processes to deliver faster decision-making, are also early adopters of AI solutions.

However, it is likely to require the launch of a commercially-available AI platform by one of the big names in AI, such as Microsoft or IBM, to really jumpstart more extensive use of AI by traditional insurers.

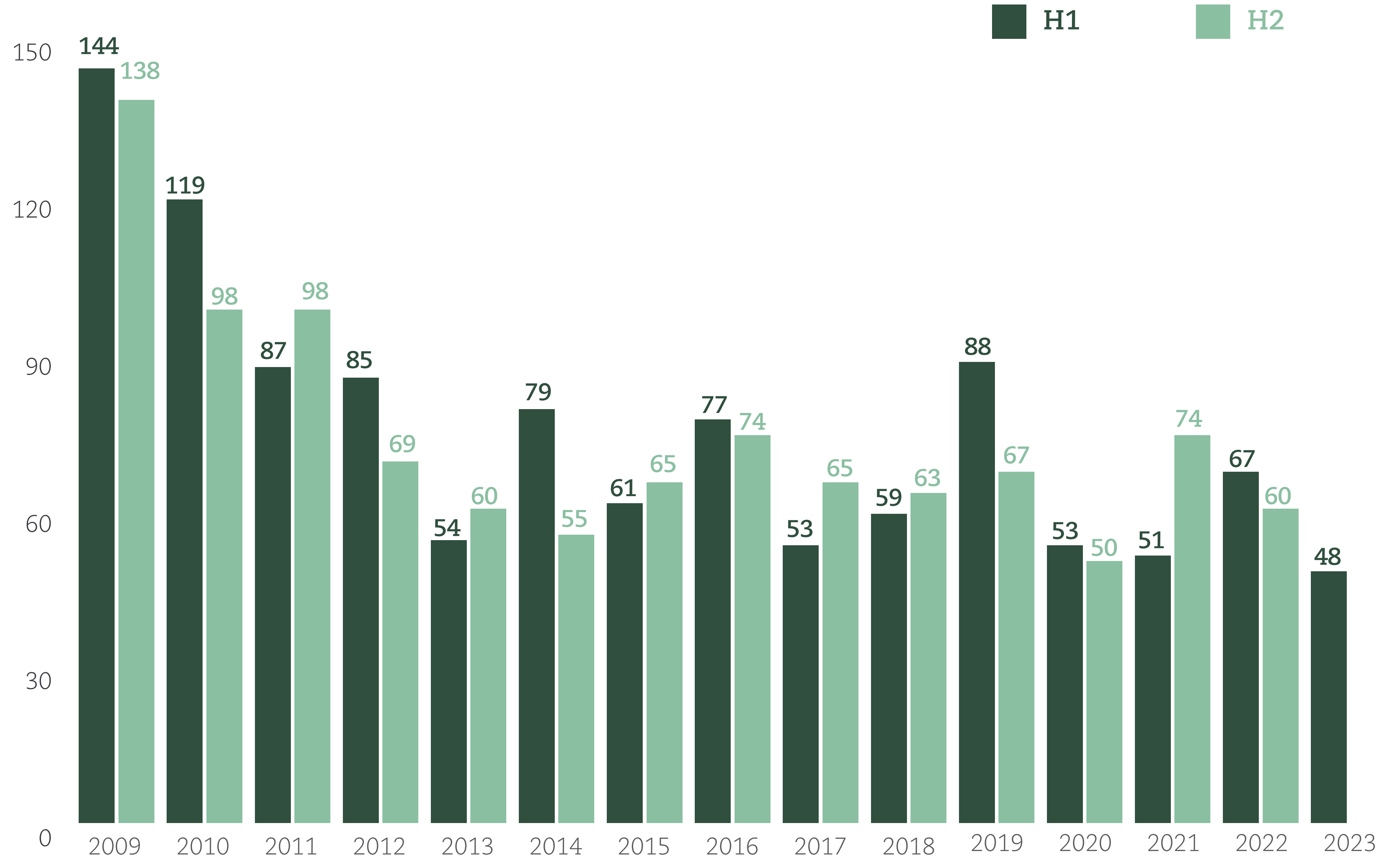
In the short-term, partnerships with insurtechs could offer a more reliable route for insurers looking to harness the power of machine learning and AI.

In the litigation space, AI is currently being used to assist with disclosure review, greatly improving the accuracy of the review process.

> The reality is that AI will provide efficiencies for organisations by automating processes, and will be used more and more as insurers find novel ways to employ it. However, there are many ethical and regulatory issues that will arise from the use of AI – privacy, questions of legal liability, and unconscious bias are just a few of the complex issues the industry is considering.

Matt Ellis, Partner, Melbourne

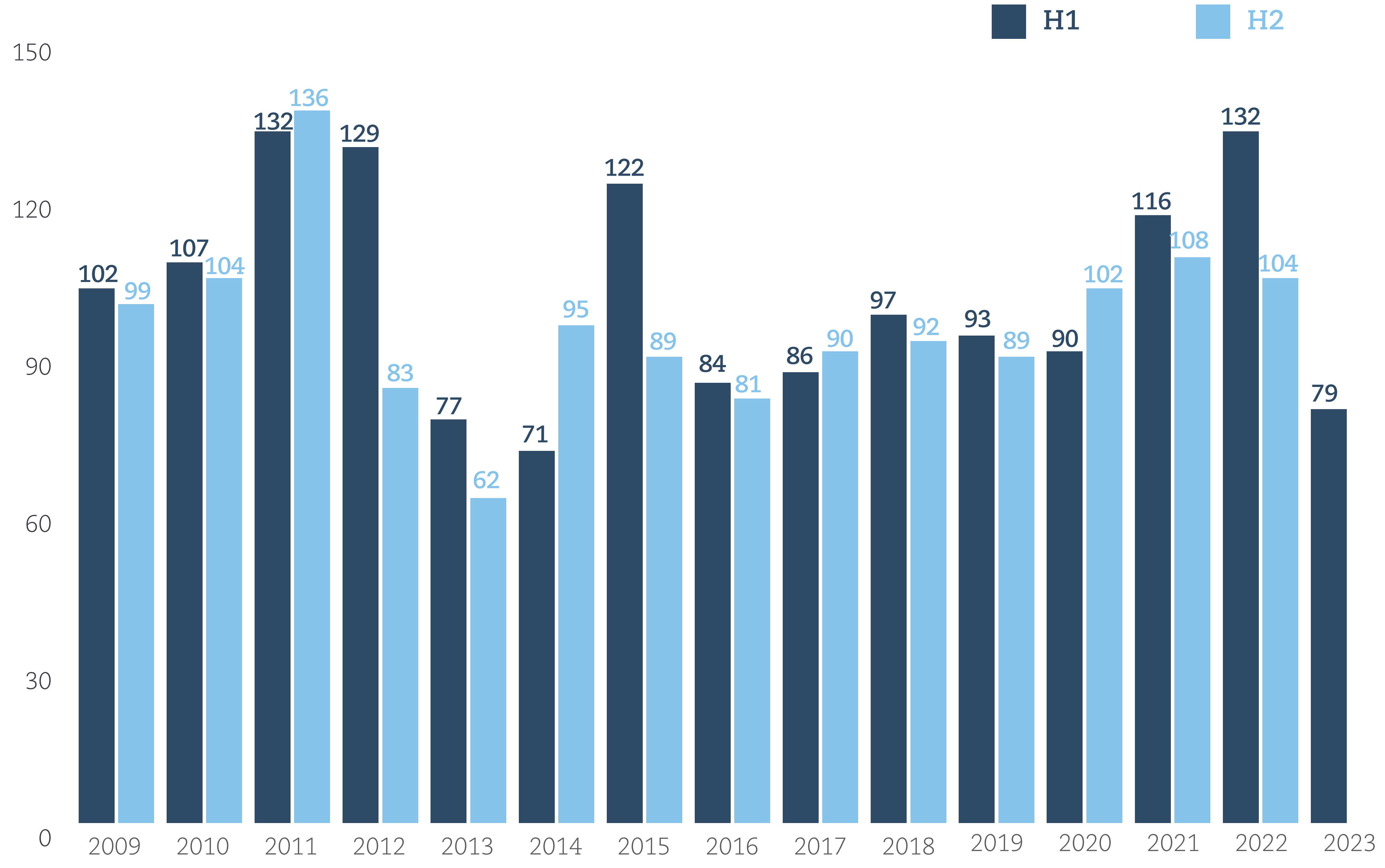
European M&A activity at lowest level for more than a decade
Volume of deals in Europe January 2009 to June 2023



Most active countries in Europe by number of deals: **UK 11, France 8, Spain 6**

Source: Refinitiv

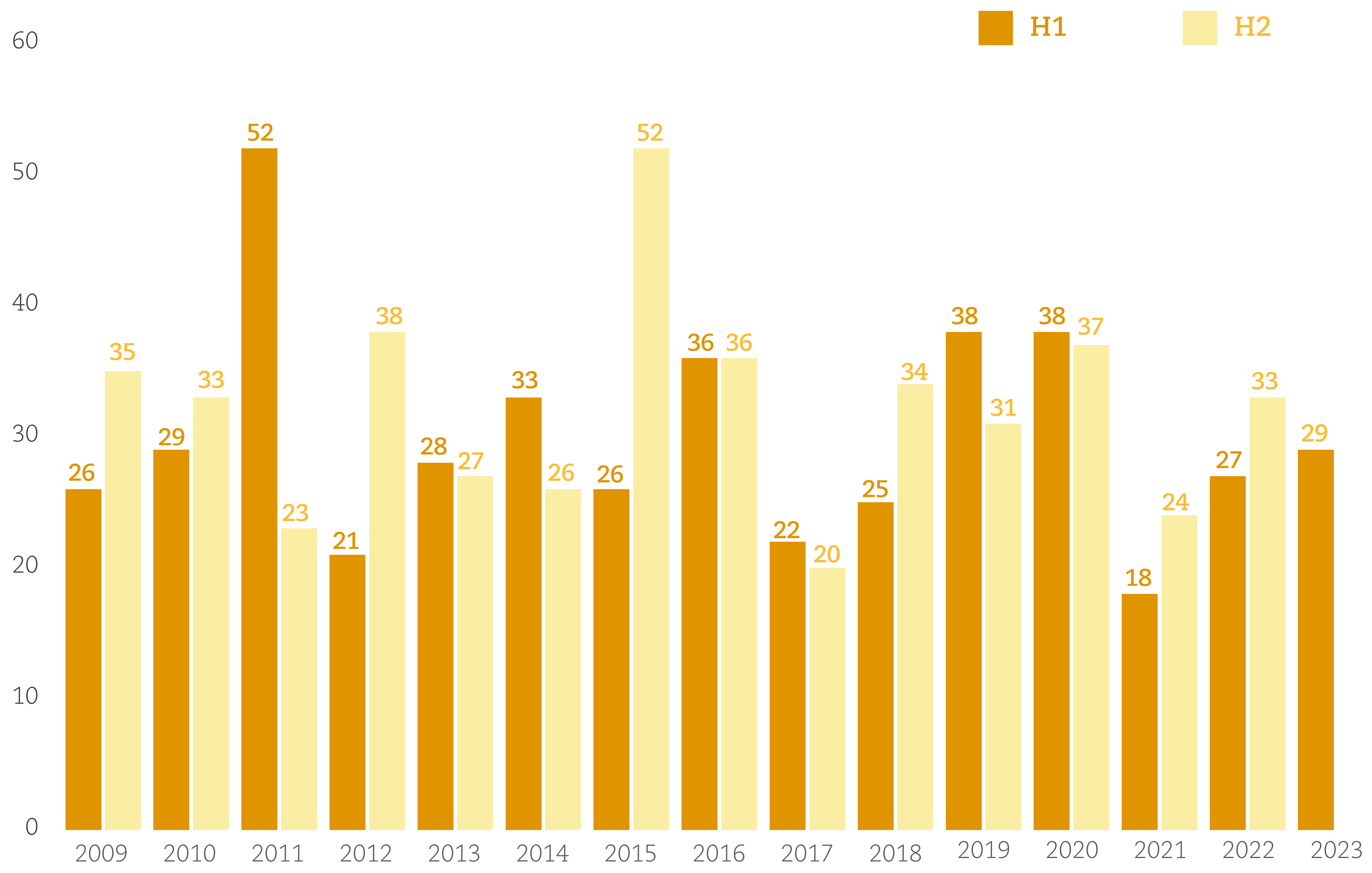
Drop in US deals drags down Americas' activity
Volume of deals in the Americas January 2009 to June 2023



Most active countries in the Americas by number of deals: **US 60, Canada 14, Mexico 2**

Source: Refinitiv

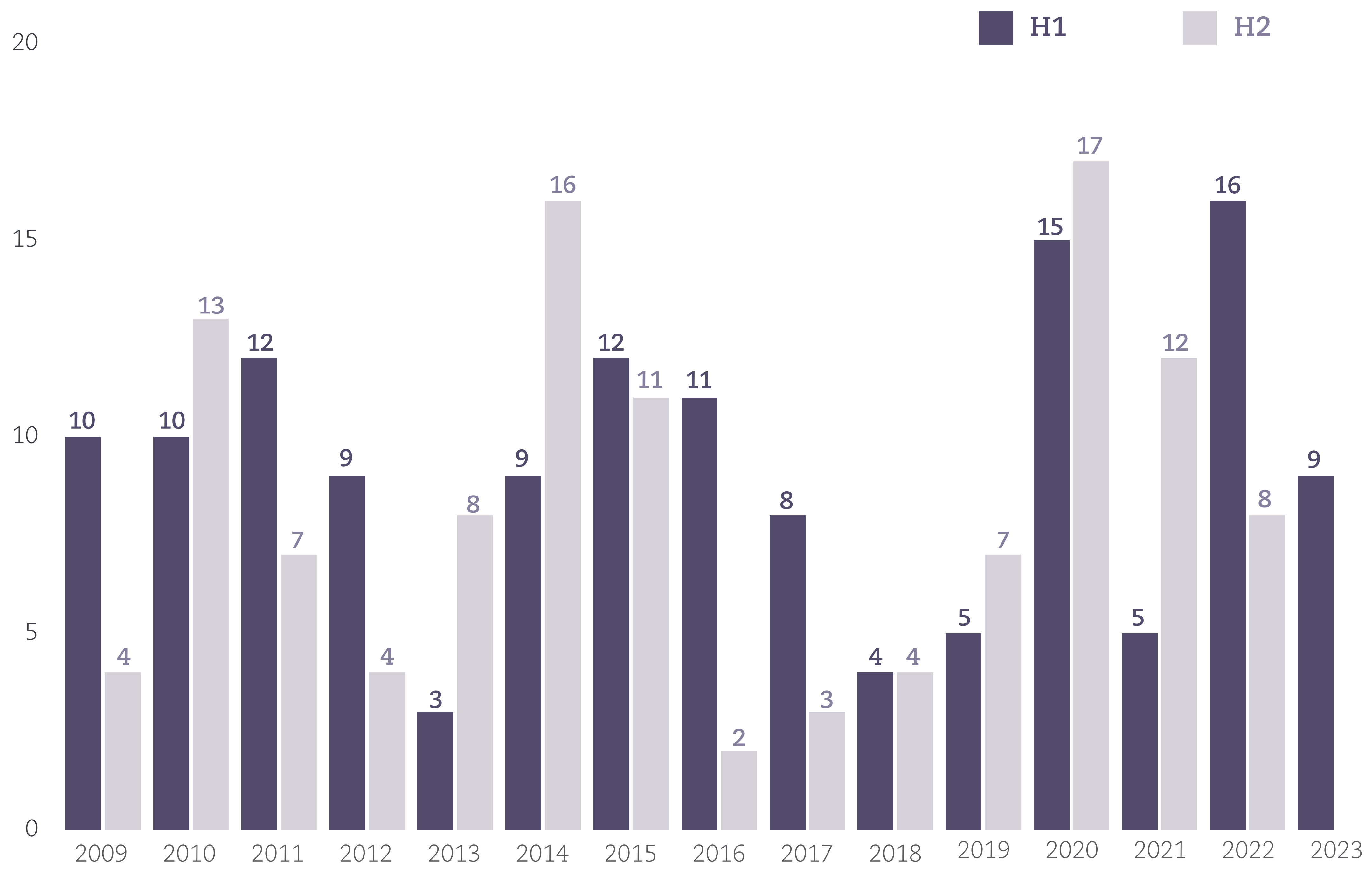
M&A dip in Asia Pacific
Volume of deals in APAC January 2009 to June 2023



Most active countries in APAC by number of deals: **Japan 14, Australia 3, China 3**

Source: Refinitiv

Deal activity in Middle East and Africa defies global trend
Volume of deals in ME&A January 2009 to June 2023



Most active countries in ME&A by number of deals: **Israel 2, South Africa 2, United Arab Emirates 1**

Source: Refinitiv

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About the Clyde & Co Insurance Growth Report

The Clyde & Co Insurance Growth Report is based on data by Refinitiv (previously trading as Thomson Reuters and Alacra) for completed mergers and acquisitions in the global insurance industry in the period 2009 to 30 June 2023 for businesses with the SIC codes: 6311 Life Insurance, 6321 Accident and Health Insurance, 6331 Fire, Marine, and Casualty Insurance, 6351 Surety Insurance, 6361 Title Insurance and 6399 Insurance Carriers, Not Elsewhere Classified. Additional input, analysis and insight was gathered from face-to-face and telephone interviews with Clyde & Co partners around the world during July 2023, supplemented by existing third-party research.

490

Partners

2,400

Lawyers

3,200

Legal professionals

5,500

Total staff

60+

Offices worldwide*

clydeco.com

*includes associated offices

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