

SMALL LIFE COMPANIES – A Survival Guide

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Hilton Birmingham Metropole Hotel

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Agenda

- q Workshop not a presentation
 - q Number of registered life companies
 - q Expense comparison
 - q Segmentation
 - q SWOT
 - q What are the issues?
 - q What are you good at?
 - q Think the unthinkable
 - q Smaller Companies New Business Strategy
 - q Open forum

YOUR CONTRIBUTION IS CRITICAL !

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**Number of Authorised Insurance Companies
(excluding General Insurance)**

- q FSA Annual Report (March 2003) – 214
 - 160 long-term insurers
 - 54 composite insurers
- q MR analysis - 177
 - 13 zero long-term liabilities
 - 9 pure reinsurers
- q All insurers owned by the same parent combined - 77

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Number of Registered Friendly Societies

- q Friendly Societies Commission (Nov 2002) – 232, now 219
 - 50% authorised to write new business
 - 37 Life Directive
 - 5 incorporated under Friendly Societies Act 92
- q Life Directive and Incorporated > 95% of total assets

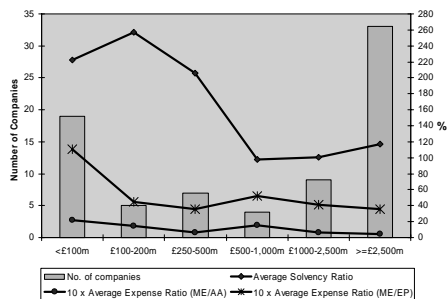
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What is a Small Company

- q Measure by group or individual company?
- q Different for FS and life companies?
- q CP195 with profits fund >£500m must comply. Does this define a small company? No FSA definition

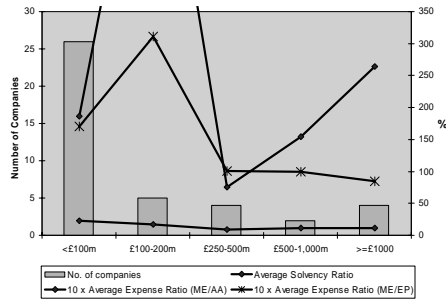
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Life Company Market – Insurers companies owned by the same parent combined

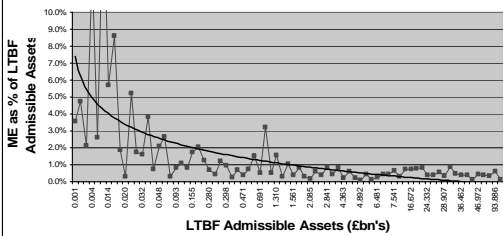


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Friendly Society Market



Maintenance Expense (ME) Analysis for Life Companies (31/12/2002)



Small is Not Necessarily Beautiful

q FSA Annual Report 2002 (1)

*"The life insurance sector includes many smaller firms. They are small in terms of premium income, but nevertheless, cumulatively, have substantial funds under management and serve a large number of policyholders. **Whilst their size does not automatically lead to problems, smaller firms are less likely to be able to benefit from economies of scale and diversification, and are potentially more vulnerable to financial strains**".*

Small is Not Necessarily Beautiful

q FSA Annual Report 2002 (2)

"We carried out a review of these smaller firms and the friendly society sector to assess a range of risks that might lead to financial failure. One concern was that **senior management may have neither the expertise nor the experience to identify and plan for such risks**. Where appropriate, we discussed problems and possible solutions with firms, with the emphasis on protecting policyholders".

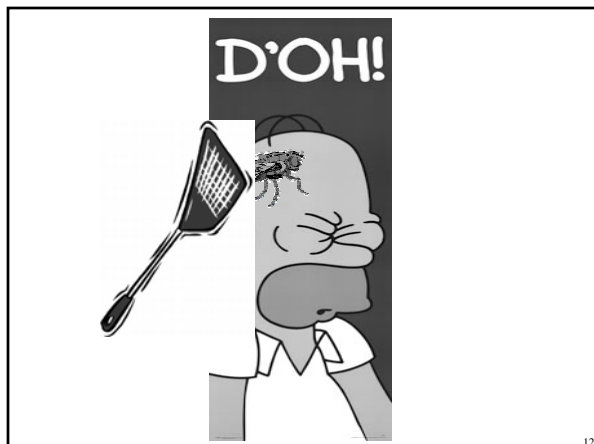
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Smaller Company Segmentation

There is not one type of small company

- q Part of retail franchise
 - M&S, Virgin
- q Part of bank franchise
 - NAL, Alliance & Leicester
- q Niche market player
 - Lutine, Cassidy Davies, PAFS (specialist risk)
 - Ecclesiastical, Police Mutual, Family (affinity, target market)
- q Strategic Licence for parent
 - BHA (PMI)
 - Pinnacle, Hamilton, Sterling (creditor)
 - Bankers Life (direct marketing)
 - Countrywide (estate agent)
- q Closed / For Sale
- q Other

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Large Company vs Smaller Company - SWOT

Strengths

- q Large
 - economies of scale
 - financial reputation
 - franchise value
 - diversification
 - reinsurance purchasing power
- q Small
 - bespoke product
 - speed to market
 - empathy with small customer niches
 - close to its distribution (know personally and weekly information)

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Large Company vs Smaller Company - SWOT

Weaknesses

- q Large
 - standard products across distribution channels
 - time to market and required new business volumes
 - system costs / competing priorities
 - legacy systems
- q Small
 - high fixed expenses
 - insufficient capital for rapid growth
 - risk concentration
 - limited access to support or expensive to obtain

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Large Company vs Smaller Company - SWOT

Opportunities

- q Large
 - multi-ties, banks, retailers
 - under insured masses
 - high volume IFAs
- q Small
 - market gaps
 - specialist skills
 - special relationship / personal touch
 - availability of license

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Large Company vs Smaller Company - SWOT

Threats

- Large - slow to change
 - management out of touch
 - hidden problems
 - high cost base
- Small - limited capital
 - regulatory pressures and past mis-selling issues
 - corporate governance disciplines

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Survival Guide

- What Are The Issues Facing Small Insurers Today?
- There Are Always Three Things To Do!
- So Remind Me..... What Are You Good At?
- Think The Unthinkable
- Some More Radical Solutions

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What Are The Issues Facing A Small Insurer Today?

Exactly The Same Issues As Large Insurers!

- Expense Over-runs
- Unstable Systems
- Unstable Staff
- Burden Of Regulation & Compliance
- Lack Of New Business

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What Are The Issues Facing A Small Insurer Today?

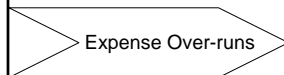
Before You Can Fix Your Business You Must Understand It!



- q What Is Your Business Model?
- q **Understand The Value Chain**
 - q Where Is Value Added.....Or Destroyed
- q Where Are The Bottle Necks And Pinch Points
- q What (Or Who!) Doesn't Work

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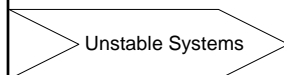
What Are The Issues Facing A Small Insurer Today?



- q **Fixed v's Variable Costs**
- q **Disproportionate Levels Of Overhead**
- q Technology
- q Wage Bills
- q **Excessive Property Costs**
- q External Providers
- q Lack Of Scale!

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What Are The Issues Facing A Small Insurer Today?



- q Old Legacy Systems
- q Redundant Technology
- q **Manual Work Arounds**
- q **Concentration risk - Only One Or Two People Know What Is Going On**
- q Lack Of Development
- q **Lack Of Flexibility / MIS**

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What Are The Issues Facing A Small Insurer Today?

Unstable Staff

- q Very, Very Loyal
- q Long Service
- q Never Worked Anywhere Else
- q **Fear Of Change**
- q **Small Numbers – No Contingency**
- q Depth Of Management Skills
- q **Commerciality**
- q Key Functions Already Outsourced – e.g. Actuarial
- q **Difficult to Attract Fresh Blood**

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What Are The Issues Facing A Small Insurer Today?

Regulation & Compliance

- q Some Concessions already Made By FSA
- q **Additional Strain On Already Overstretched Teams**
- q Disproportionate Costs
- q Management Distraction?
- q Lack Of Rigour Leading To Poor Decision Making
- q Doesn't Add Value For The Board

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What Are The Issues Facing A Small Insurer Today?

Lack Of New Business

- q Grow Your Way Out Of Trouble?
- q Cost Of Development
- q Management Distraction Again!
- q Take On Disproportionate Risks
- q **Small Potential Premium Size**
- q **Often An Excuse NOT To Take Hard Decisions**

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What Are The Issues Facing A Small Insurer Today?

Outsourcing Administration

- q Great Idea But Outsourcers Need to Make Money Too!
- q Small Fragmented Books Cannot Be Transferred Cost Effectively To An Outsourcer
- q Sort Out Your Processes Then Outsource
- q But Generic Processes Can Be Outsourced.....

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What Are The Issues Facing A Small Insurer Today?

Outsourcing Processes I

- q But Generic Processes Can Be Outsourced Efficiently.....
- q Facilities q Investment Management
- q HR / Wages q Product Design
- q Legal q Compliance
- q IT Management q Property – Sale & Lease Back
- q **Actuarial Services** q Rent An Office!

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What Are The Issues Facing A Small Insurer Today?

Outsourcing Processes II

- q This Will Be Difficult As It Fundamentally Changes The Nature Of Your Business
- q **Requires The Sacrifice Of Holy Cows**
- q Cannot Outsource Until You Have Sorted Out Processes
- q If It Leads To Cost Cutting It Must Inevitably Lead To A Reduction In Headcount
- q **Needs Strong Management To Manage Outsourcers!!!**

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What Are The Issues Facing A Small Insurer Today?



Or



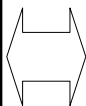
- q It Is Possible to Be Small And Perfectly Formed With The **Appropriate Level Of Attention and Skill**
- q However.....

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There Are Always Three Things To Do....



Grow => Lots Of New Business



Stabilise => Some New Business Or Controlled Closure



Decline => Uncontrolled Closure or Failure!

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So Remind Me What Are You Good At?

- q Identify What You Are Good At And Get Even Better!
- q Is This Enough to Allow You To Survive?
- q If Not What Do You Need To Do To Make It Enough?
- q What Are You Going To Do About It?
- q And.....
.....What If There Is No Way Out?

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Think The Unthinkable

- q Look Critically At Your Business
- q Get An External View From Someone You Trust
- q Sometimes This Should Be From Outside The Industry
- q Be Honest About Your Options
- q Look At The Upside As Well As The Down Side!
- q Is There Something Radical Which May Just Work?

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Think The Unthinkable – Case Study I – Family Assurance

- q More Than Just A Name
- q Quality People
- q Differentiated Products
- q Great Systems
- q Distribution Partnerships
 - q Bounty
 - q Building Societies & Banks
 - q Great Web Site
- q And....



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Think The Unthinkable – Case Study II – Reliance Mutual

- q Rationalised Products
- q Cut Overheads
- q Worked Property
- q Made Sensible Acquisitions to Spread Costs
- q Controlled Product Development

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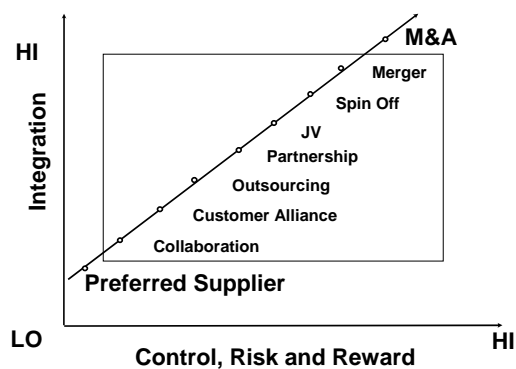
Some More Radical Solutions

Definition: Alliance

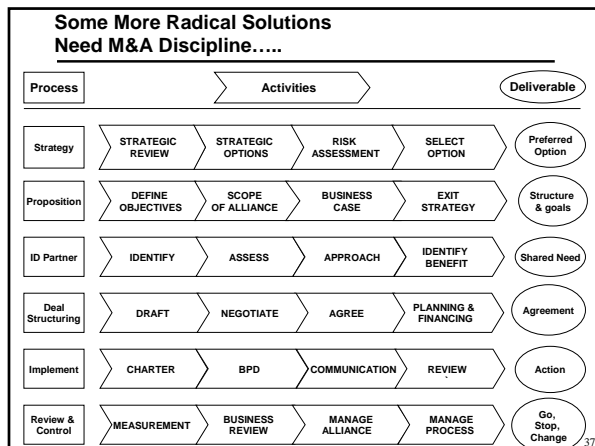
Co-operative arrangement where each party bears risk & shares in rewards

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Where Are You On The Curve?



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**Some More Radical Solutions
In Practice Very Difficult To Do.....**

- q Human Nature
- q Fear Of Change
- q Vested Interests
- q Complexity
- q Regulation
- q Policyholders / Members

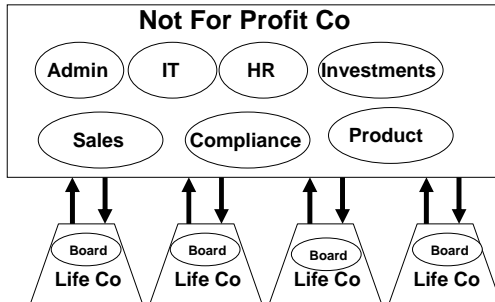
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**Some More Radical Solutions
A Utopian Dream?**

- q The Industry Saves Itself
- q True Sharing Of Resources
- q A "Not For Profit" Infra-Structure
- q A Truly Mutual Solution

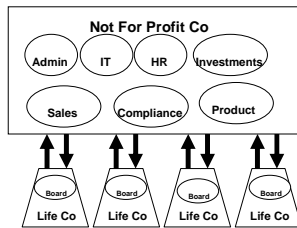
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Some More Radical Solutions A Utopian Dream?



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Some More Radical Solutions A Utopian Dream?



- q Owned By The Life Co's
- q True Shared Services
- q Fiduciary Responsibility Remains with Entity
- q Reduced Overhead
- q Scale
- q Outsource
- q Open Or Closed

Could It Work?

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Smaller Company New Business Strategy

Proactive Approach

- q Requires clear strategy and ability to deliver it
- q No right to exist
- q Delay will only make challenge greater

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Smaller Company New Business Strategy

Depends on

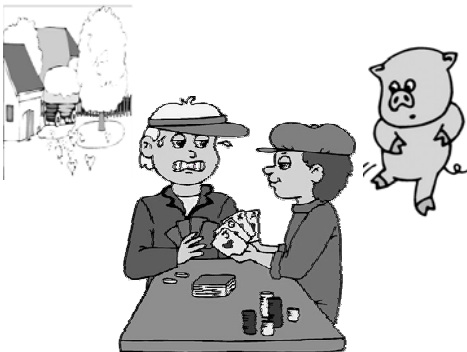
- Financial Strength + access to capital
- Volume of added value new business (ie after expenses + RoC)
- Intensity of competition in target sector / success of top players in sector
- Strength of differentiators / USP
- Quality of systems and management
- Flexibility of expense base
- Structure and FSA constraints
- Board / shareholder attitude

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Smaller Company New Business Strategy Expense Economics

- q Increased significantly due to regulatory requirements
- q Low inflation/investment growth uncovers excess expense charges
- q Outsource / buy-in specialist functions
- q Price caps force out even the largest insurers
- q Cannot compete on charges, must move off price line

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Smaller Company New Business Strategy

Geared risk from individual decisions

De-Risk – Avoid Shocks

- q Regulation – do not take on unquantifiable / uncontrollable risks
- q Regulatory capital – control new business volumes and find access to other capital sources
- q Systems investment – collaborate, use off-shelf solutions, or trial new products if downside can be managed
- q Insurance Risks – work with one/two reinsurers to manage volumes

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Smaller Company New Business Strategy

Understand Sustainable Value Add

- q Specialise in
 - Risk management (e.g. impaired lives, IP)
 - Customer niche (e.g. via parent, affinity, target market)
 - Product niche (e.g. group, creditor, LTC)
 - Service (e.g. immediate covers, one-day protection)
 - Capacity (licence, capital)
- q Be realistic in assessing effective demand versus supply
- q Additional cost < value add
- q Sufficient financial strength especially if risk concentrations

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The screenshot shows the homepage of The Children's Mutual website. At the top, there's a navigation bar with links like 'Search', 'Go', 'Our savings plans', 'Savings information centre', 'Family fun', 'Questions', and 'IFAs'. Below this, a large banner reads 'Welcome to the world of saving for children'. To the left, there's a sidebar with links: 'About us', 'Contact us', 'News and views', 'Legal information', and 'Site map'. The main content area features several sections: 'Whether you're just browsing today or looking for something specific, one thing is certain, you want to do the best for the child in your life.', 'Getting started' (explaining the Savings Information Centre), 'The Children's Portfolio' (focusing on day one and allowing families to put together a range of savings and investment plans), 'Baby Bond' (a free personalized information pack), and 'The Child Trust Fund' (a link to learn more about the Government's latest announcement). At the bottom, there's a footer with contact information and a disclaimer.

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Smaller Company Strategy - Conclusions

- q Understand your business
- q Focused strategy + absolute commitment to it
- q Limit size of individual risks & risk accumulation
 - both insurance and operational
- q Run lean business - collaborate with others for common systems, compliance and other specialist resources

- q Establish firm credentials with target market
- q Service few well, not many badly
- q Low-cost access to distribution
 - use other players' access to market (eg direct to distributors)
 - E-business solutions for a few like minded distributors
 - Focused / productive / controlled direct sales force

And finally

- q Control new business volumes

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The Actuarial Profession

making financial sense of the future

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