

THE FUTURE OF DISTRIBUTION IN SME  
COMMERCIAL GENERAL INSURANCE

The Impact on Underwriting and the  
Underwriter of the 21st Century

# Executive Summary

# Executive Summary

Today we find ourselves in a unique situation in the SME segment of the commercial general insurance market. Interviews with leading industry figures and CII members have revealed that the interplay between the current stage of the market cycle and broker consolidation is driving systemic change in the industry – change that will have significant impact on the underwriting function and the future underwriter. The change that is taking place is unlikely to be undone. This report draws on the results of those interviews, sets out the participants' views of the changes, and poses the question; how should insurers and underwriters be responding?

### **Why is this market different?**

Major consolidators have capitalised on soft market conditions to fully leverage their scale with insurers whilst securing significant market share of distribution in the commercial lines SME market. At the same time, distributors of all sizes are seeking to optimise their income, either through insurer panel rationalisation or through an expansion of their role in the insurance value chain – undertaking work traditionally done by insurers in the form of delegated authorities or via the formation of Managed General Agencies (MGAs).

Whilst the desire of distributors to capture more of the income available in the insurance value chain is a common feature of previous soft market cycles, the market has now polarised into a smaller number of powerful distributors. This suggests a fundamental change in the economics of the underwriting value chain that will extend beyond the current soft market. This has major implications for insurers, as they will be forced to re-examine their distribution strategies as well as the mechanisms by which they underwrite these lines of business.

### **So how are insurers responding?**

The challenges faced by insurers are having a knock-on effect on the underwriting discipline, and a number of divergent insurer strategies have emerged in response. Some insurers have decided to buy distribution outright, some have made investments in brokers, and others have made choices as to their partners in the market in the future. Whilst it is still too early to tell which strategy will generate most long term value, it is clear that insurers can no longer sit on the sidelines as the future market landscape is influenced by others, and that they need to make clear strategic decisions as to their positioning in this segment of the market.

As well as addressing the question of access to distribution, the current market conditions have seen a need for insurers to fundamentally re-examine their operating models for SME business, with a lower cost multi-channel distribution strategy increasingly becoming a necessity for those with scale ambitions.

Although the pace and scale of growth is uncertain, there is universal acceptance that the micro and small part of the market will increasingly become commoditised with more business migrating to direct, bancassurance, or affinity players via telephone and web channels. That said, larger SMEs still require face-to-face contact and regional brokers have traditionally demanded a local servicing network.

This research reinforces the notion that the different requirements of the diverse customer types in the SME sector must lead to segmented distribution strategies. It will also require differentiated product and segment service propositions to each channel – and recognition that insurer operating models will reflect the differential economics of each channel offering.

The importance of channel strategy is, and will continue to be, crucial and for the successful insurer, focus will be everything.

### **So what does this mean for underwriting?**

The blurring of the boundaries between insurers and brokers, and their roles in the insurance value chain, will lead to some lasting change. This will impact both the underwriting function and the underwriting role itself, and will create a number of exciting opportunities for underwriters within the market.

In the first instance, the commoditisation of micro and small commercial business will see underwriting evolve towards a personal lines model – with rules based underwriting and a different form of underwriter intervention, based more on data analytics than on traditional case underwriting. This model is likely to see larger, less geographically diverse centres of excellence replace local sales and service capabilities with a knock-on impact on the numbers and types of underwriters required in the market.

In the broker channel, the development of MGAs and the prevalence of specialist delegated authority arrangements will also have significant impact. Insurers will need to invest in a variety of new technical and commercial skills to ensure that case underwriters are fully equipped to deal with the demands of the future market. Portfolio underwriting and the auditing skills required to manage delegated authorities will become as important for more senior underwriters as the traditional technical case underwriting skills. In addition, trading and non technical skills will need to be refined to adapt to varying requirements at the different points of sale for this segment in the future. Good underwriting will continue to underpin insurer strategies and for more technical underwriters there will be opportunities to develop more widely diversified skill sets, and to adopt broader, more commercial roles as the market develops.

More entrepreneurial underwriters may consider that the opportunities lie elsewhere. Some are likely to be working not for insurers but within the broker market where new opportunities are emerging. Brokers are increasingly employing underwriting specialists, and will themselves need to invest in the training and development requirements of their new operating models if they are to ensure that the risk management and trading skills core to underwriting are not diluted.

Although the core values for many case underwriters will remain the same, it is likely that there will be an increasing requirement for portfolio underwriting to deal with the changing demands of the SME marketplace. The role will blend the technical skills of the traditional 'head office' underwriter, with the trading skills of the 'commercial underwriter'. On the one hand they will need to acquire new portfolios of business and on the other bring actuarial, capital, and statistical analysis to bear in the management of blocks of business on a portfolio basis.

The majority of respondents to this survey believed that the skills required for this underwriter of the future are already out there – but they exist neither in the right quantities nor in the right places to satisfy the demand of the market in the coming years.

The industry needs to act fast to evolve with the changing distribution dynamics and to broaden underwriting skill sets. As always, the winners in the market of the future will be those who are adapting to changing underwriting requirements now.