

Is it more important than ever for brokers to invest in schemes?

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Introduction

Introduction to schemes

Firstly, what is a scheme? There is no standard definition in the market, however, a scheme in essence is an insurance product that revolves around its defined customer. A scheme can be a similar type of business (customers all doing the same thing) for example cycle shops, hairdressers or can be led by an association, for example BMFA (British Model Flying Association) where everyone has a model plane to insure. Typically the SME market focusses on scheme business.

Why would brokers be interested in schemes? It gives them the opportunity to define a niche within their market for their brokerage, offering a unique product to their customers, in a sector which will offer USPs in the form of bespoke wordings, coverage or competitive pricing. Creating a competitive edge, new revenue stream, sometimes enhanced commissions and more control over issuing documents to customers, customer loyalty due to the unique product.

Why would customers be interested in a scheme? They get a product specifically designed for their business needs, allowing them to better protect their business as well as potentially benefiting from more attractive pricing, due to economies of scale.

Why have I chosen this topic?

Schemes business is close to my heart. Back in 2007, my first role in insurance was to set up the schemes team at Hiscox and I worked in that business for over 7 years. I set the team up after researching the sector; identifying how big the market was and the opportunity for brokers and insurers to partner together to deliver the best products to their customers in chosen sectors they are passionate and knowledgeable about.

The sum of the non-life insurance market in the UK is estimated in 2020 to be £80 billion and growing according to Statista, with predictions to be over £90 billion by 2023. The scheme sector continues to grow, it's harder to put a number on size of the schemes market, as there is no industry definition for a scheme, but after researching the main insurers book sizes I believe the market to be in excess of £8 billion and growing.

I have also chosen this subject as I can access insurers, brokers, broker websites, online resources and market updates to help with my research and I want to further my knowledge in this sector.

What do I want to achieve? The question I want to answer is: "Is it more important than ever for brokers to invest in schemes?", understanding why insurers, brokers and customers should invest and benefit from a scheme, what this means given the current market conditions and the changing economy. I have seen schemes to be exceptionally

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fruitful for brokers and insurers and more importantly customers, but I want my research to prove this and qualify if now is the right time for brokers to invest more than ever.

Schemes

Schemes play a significant part in the UK insurance industry and are estimated to be approx. 10% of insurance premium and growing. So let's establish why the sector is so significant and growing for both insurers and brokers.

Insurers interest

Over the last 10 years we have seen more insurers invest and grow in the schemes sector and I have researched into the core insurers, Aviva, Axa, Hiscox and RSA to find out why.

From my research Axa seem to have the most significant share in the market of broker schemes with a book in excess of £300 million. *'We know that offering a broad appetite and competitive price is no longer enough to differentiate us from the rest of the market which is why we've worked hard to develop a proposition that has growth and flexibility at its core.'* (<https://www.axaconnect.co.uk/commercial-lines/schemes-for-commercial-clients/>) – Axa schemes – December 2020.

The key driver here for Axa is creating a competitive edge in the market to differentiate them from competitors to help their business grow. Identifying that the current ways of offering products to customers is not enough.

From Hiscox *'...customers are becoming more demanding about the products and services they buy. We are living in a digital age where consumers have the power to research, review and buy online 24/7. Ensuring you are responding to these changing customer needs is crucial in helping you grow any business. In an increasingly homogeneous and competitive insurance market, an effective scheme helps to differentiate your business, targeting niche and specialist markets that are not covered or are poorly served by traditional insurance solutions.'* (<https://www.hiscox.co.uk/sites/uk/files/documents/2017-06/17311-uk-%20schemes-brochure-v2.pdf>) – Hiscox schemes brochure - 2017

From Aviva, *'Our dedicated and specialist schemes team has helped to bring over 300 individual schemes to market. We want to work with experts who have the measure of their specialist field.'*

When you partner with Aviva, we'll help you get the most out of your scheme:

- *Manage over £300 million of Schemes GWP*
- *Decision on appetite within 48 hours*

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- *Ability to launch scheme within 6 weeks*
- *Expert underwriters*
- *Dedicated and specialist team*
- *Governance and compliance support*
- *Award-winning claims service*
- *Marketing support'* (<https://connect.avivab2b.co.uk/broker/resources/product-support/aviva-schemes/#m-tabs-aXZJ0>) – Aviva schemes – December 2020

Of the insurers I researched I can see a lot of investment has gone into building specialist schemes teams within the insurance companies to support brokers with schemes opportunities on existing and new scheme ideas. This demonstrating the significance schemes now plays in the insurance market and the importance to insurers.

All researched insurers shared the same view suggesting that the change in customer needs, being more demanding of an enhanced competitive product is driving their interest in schemes and suggesting brokers reasoning is the same. A competitive market edge suggests it is only getting tougher to achieve and a way to provide an edge is by offering a schemes proposition to specialist markets.

In summary and reflection of my research this tells me that from an insurers point of view, schemes are an important part of their business and growing and a competitive edge is key to their growth in market share which schemes.

Brokers interest

Why should a broker invest in developing a scheme? Here are some of my personal thoughts after working in the schemes sector for a number of years:

- A solid income stream for the broker – supporting new and existing business to be more reliable and consistent
- Protects the broker from open market pressures – as broker has a unique offering that is tailored to customers' needs, therefore market leading product and price
- USP's and bespoke policy – easier to sell to customers as unique to them, for example, would you rather buy a shop policy or a shop policy tailored to your trade as a cycle shop with product enhancements linked to your specific risk exposure?
- Enhances brokers brand – by promoting expertise for the broker in a certain sector
- Cost effective – usually the broker has a delegated authority to enable them to trade efficiently with their insurer and customer.
- Specialist claims team – who understand specialist sector and wording

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This is my personal view, I wanted to verify this with broker research so I interviewed Martin Holden of Gleaming Insurance, a scheme broker who has schemes with RSA and Hiscox.

“Why should a broker invest in schemes?”

From my perspective, it was a way of distinguishing yourself from the rest of the pack, it creates specialism and a niche to allow you to really focus in and solve a particular sectors issues.

What is disadvantage of not having a scheme?

They risk becoming just another broker – there will always be room for good and successful commercial brokers, but a scheme done correctly and written for profit provides a certain degree of longevity.

Why did you choose to develop a scheme?

I like the numbers, I like data and I love digital – all those give a strong platform to develop a scheme and to transform one from a standard paper basis to online was a great challenge.

What benefit does it give you over open market trading?

It gives you value (specialism), rapid growth and a certain level of stability. Using technology and digital solutions, it also gives you savings and efficiency.

What percentage of your brokerage is schemes?

At present probably 90 %.

Do you think trading in schemes is more important than ever?

I think right now with what is available in terms of underwriting support and technology solutions it is a missed opportunity if you cannot develop your niche. Every broker will have someone working there with an “in” – someone who has strong links to a large group of people for which a scheme can be created.”

In summary, Martin believes schemes has grown his business significantly to where it is today, built around key associations with lots of members with similar needs. He worked in partnership with a key insurer to build a scheme with a bespoke product, specific to the customer’s needs, competitive pricing, with the right distribution model to sell online. A great success story and a big supporter of schemes being important to brokers to invest in.

I also researched a few local broker websites to see if there is scheme presence on their websites. One that jumped out to me was Hamilton Fraser, who specialise in cosmetic insurance and key words on their website that describe their scheme are flexible, specialist, tailor-made and expert advice – which summarises what a scheme means for them and great

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selling points to their customers. As a result Hamilton Fraser are one of the biggest cosmetic brokers in the UK. *'Hamilton Fraser Cosmetic Insurance was the first ever commercial insurance provider to offer medical indemnity insurance specific to the aesthetic industry back in 1996. We continue to support the industry by working with the leading organisations, manufacturers and distributors within the cosmetic sector and pride ourselves in playing an important role in raising standards across the industry. We can arrange competitive insurance for both traditional and more specialised cosmetic surgery practices. Our medical malpractice insurance policies are affordable and flexible and designed to grow as your cosmetic business develops.'* (<https://hamiltonfraser.co.uk/medical-malpractice-insurance/>) – Hamilton Fraser – December 2020.

This example confirms how important the brokers passion, understanding and expertise are in a sector, in growing a specialist scheme fit for their customer base.

The next question I wanted to answer is how many brokers invest in schemes as it feels there is more traction in the market with brokers investing in schemes. This was backed up by the Aviva schemes website, *'70% of brokers identify schemes as an area of growth, and many are already seeing the benefits. For a third of brokers who run a scheme, it accounts for 60% of their Gross Written Premium.'*

(<https://connect.avivab2b.co.uk/broker/resources/product-support/aviva-schemes/#m-tabs-PYhy6>) – Aviva schemes – December 2020)

In summary insurers and brokers interests are very similar. Like the insurers response, brokers demonstrate the importance of having a competitive unique product to sell to a specific customer base, understanding their customers better and the customers are receptive of this. The USPs of a scheme help them to grow their customer base and in return generate a solid income stream. This also allows brokers to run the scheme cost effectively which allows them to invest more time and effort to improve their return. The stats from Aviva are encouraging on the significance brokers identify with schemes as a key growth area and the overall benefits, backing up my view on schemes importance to brokers.

The SME market

Now to consider the end customer, how big is the SME market where insurance schemes typically play and is it a growing sector.

How big is the SME market?

The government website for national statistics tells me that there are 6 million business' in the UK, 5.94 million are small (0-49 employees) which is significant proportion of businesses

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in the UK and this is an increase on 2019 by 1.9%. This market has evidence of growth since 2000. (<https://www.gov.uk/government/publications/business-population-estimates-2020/business-population-estimates-for-the-uk-and-regions-2020-statistical-release-html>) - The Government website for National statistics - Business population estimates for the UK and regions 2020: statistical release – October 2020 (See Appendix 1)

The schemes sector is predominately made up of SME businesses therefore this is positive evidence that the schemes opportunity is growing which is positive for both brokers and insurers from this research.

Is the SME market in growth mode?

The government website tells us that there are more small businesses than ever and the industry is in growth mode, with new start-ups, and more small business than ever, however what does the growth in businesses really mean?

The small business official website also suggests that small companies are in growth mode and the website stats, *'this year should see record number of companies created, with an extra 84,758 businesses setting up in 2020 compared with 2019. This is equivalent to a 12.3 per cent increase year on year, which is the highest percentage growth since 2011 and the highest actual growth on record.'* This is all very positive, however, the website then goes onto suggest: *'Although on the face of it the research is good news, the reality is that many new companies are created by those who have lost their jobs because of Covid-19. There is also a question mark as to how many of the 59,538 companies created between June and August are even legitimate, given the widespread fraud which has gone on with criminals targeting the Bounce Back Loan scheme, which offers limited companies up to £50,000 interest-free for one year.'* (<https://smallbusiness.co.uk/2020-set-to-be-record-year-for-new-companies-created-2551479/>) - Small business website – December 2020

However, there is major conflicting evidence, the UK economy has contracted from early 2020 due to COVID19, Gross Domestic Product (GDP) is not increasing which is a sign that the economy is not in a position of strength. With the economy not being in growth mode this will have a negative impact on companies and ultimately peoples jobs. The UK has not been in this position for 11/12 years when our last recession was in 2008/2009 which was caused by the credit crunch, which was due to reducing confidence in bank leading as a result of bank liquidity.

So can this conflicting view of SME growth, but signs of recession be explained? The first half of this year, 2020 saw significant signs of recession with GDP declining, then the second half saw expectational growth. The BBC reports that *'what the figures capture is an economy shutting down and reopening again. However there is still a big gap between how the economy was doing last year, and where it stands today. Though the recession is over,*

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the economy is 9.7% smaller than it was before.' (<https://www.bbc.co.uk/news/business-52986863>) The BBC - November 2020

My summary of the above is that the reports and stats are conflicting, the government stats show that new company set up is in growth mode which is positive and could suggest economy booming with lots of new businesses popping up. However, when you dig deeper, this is a result of failing business setting back up again, some will be genuine and unfortunately some will be fraudulent. As a result the economy is actually smaller than it was before. Therefore my view is the SME market is not in growth mode as I first thought from the initial research.

With all negatives, there are positives, as a recession can actually be a good time to set up a business, from my research it shows that some well-known companies today, including Uber and Airbnb were set up in the last recession and some sectors will also thrive. Businesses have to think differently, be more resilient and entrepreneurial than ever before to ensure there business will last/thrive in a recession and beyond.

But is growth (or not in this case) in the SME market the single important reason why brokers should invest in schemes? I believe this is not of major significant importance as the SME market is still huge with lots of specialist sectors for brokers to focus on and some specific sectors will be in growth mode.

COVID19 impact

What is COVID19

Coronavirus, known as COVID19 is an infectious disease caused by a newly discovered coronavirus first found in China in December 2019. A highly infectious disease that is unprecedented, which spreads primarily through saliva droplets. Most people who contract the COVID19 virus will experience mild symptoms, however, those who have underlying medical problems or who are older in age the virus can be very harmful and unfortunately at the extreme end cause death.

What is the impact of COVID19 to SMEs

As a result of COVID19 virus being transmitted by human to human, it has spread across the world and COVID19 can be found now in every continent. The UK Government has worked to try and control the spread of the virus and to do that limited human interaction is key. As a result of this the UK has gone into many different lockdowns, ordering people to stay at home and largely that non-essential businesses have had to close for those periods of time or find other ways to trade with non-contact.

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In essence the smaller companies have been impacted mostly and The Bank of England tells us *'the Covid-19 shock has had a bigger impact on smaller companies than larger companies. Smaller companies are more likely than larger companies to operate in sectors that have been most affected by the shock (Chart A), such as accommodation and food, arts and recreation, and construction.'* (<https://www.bankofengland.co.uk/bank-overground/2020/how-has-covid-19-affected-small-uk-companies>) – The Bank of England – October 2020 (See Appendix 2)

There has been support for small business from business grants, to business rates relief, job retention scheme and other support. The Job retention scheme, widely known as furlough has been a great support to all business where the employer of a business has less than usual or no work due to COVID19 they could benefit from the government paying a percentage of their staff wages until the work comes back to limit people losing their jobs and mass redundancy, which would have further impact to the economy.

To put the impact of COVID into perspective, The Guardian quotes *'almost two-thirds of all businesses could be at risk of insolvency, according to official figures that reveal the UK could suffer "a flood" of bankruptcies over the coming months. The Office for National Statistics (ONS) said that 64% of businesses across all industries were at risk of insolvency last month, with 43% of companies running on less than six months' cash reserves.'* (<https://www.theguardian.com/business/2020/oct/28/uk-facing-flood-of-bankruptcies-over-coming-months-says-ons>) - The Guardian - October 2020

The summary here is that we hope the economy will kick start again in 2021 and support growth of the SME market as otherwise this will see the SME market continue to decline. Good news has been announced on a vaccine approval, which should support growth in 2021.

What does this mean to insurance?

First point to note is that the COVID19 pandemic resulted in significant financial loss for small businesses. Those businesses with Business Interruption (BI) cover made claims to their insurers, in addition to the Government support. A lot of insurers declined the claims due to coverage, suggesting this is an uninsurable event and their policies were not intended to cover such a pandemic. As a result the FCA brought a test case to the High Court with Insurers to ensure a quick and fair decision for insureds. The current state of play is the FCA and the insurers applied to the Supreme Court and was accepted and we await final outcome.

Overall insurance companies are financially stable and well prepared for major loss events as that is what they are set up for and they also purchase reinsurance to support such major losses. Each insurance company will be impacted differently due to their book mix and wording coverage. Insurers will need to respond to pandemic and Deloitte sets this out well

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in their paper with their recommendations to insurance companies *'identify the classes of business which are most exposed to the impact of coronavirus and rigorously model claims exposure and profitability impact. Evaluate potential brand risk exposure due to customer expectations vs policy terms. Develop a proactive strategy to respond.'*

(<https://www2.deloitte.com/global/en/pages/about-deloitte/articles/covid-19/understanding-covid-19-s-impact-on-the-insurance-sector-.html>) - Deloitte paper: Understanding sector impact of COVID19 – Insurance – March 2020

What this means in reality is that insurance companies need to evaluate the high risk areas of their book mix and response with premium increases, limits may be reduced and excesses increased to protect their profitability and stability. Insurance companies are already adding communicable diseases exclusions. This will impact end customers, as the insurance industry is in a hardening market and the COVID19 pandemic has exacerbated this further, with some or possibly all lines of business being impacted. As less insurers will want to write in high risk areas, therefore less capacity with more stringent underwriting and as a result higher premiums for the end customer:

'Characteristics of a hard market include:

- *Higher insurance premiums*
- *More stringent underwriting criteria, which means underwriting is more difficult*
- *Reduced capacity, which means insurance carriers write less insurance policies*
- *Less competition among insurance carriers'*

(<https://www.b4-business.com/article/insurance-in-a-hard-market-what-it-means-for-your-business/>) - B4 Building bridges between businesses - Insurance in a hard market – what it means for your business – November 2020 (See appendix 3)

In summary what this means is the COVID19 pandemic has sped up the hardening of the market that we have not seen for over 10 years. What this potentially means to small businesses is less insurance options for them, increased premiums with possible coverage restrictions. On the flip side if small businesses turnover is down due to economy impact, the insurance premium rate will still be high but premium down due to reduction in turnover.

What does this mean to schemes?

Due to the COVID19 pandemic and increased hardening of the insurance market we are seeing that most if not all insurers putting blanket premium increases across their general books of business to support risk exposure, cover losses and support rising reinsurance costs.

However, are schemes protected? Insurers underwrite schemes books of business in specialist sectors, these sectors are underwritten to the specific sector, given appropriate

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wordings and enhancements based on the detailed data both brokers and insurers have available. So why is this important, well this gives brokers with schemes and their end customers more protection as the scheme will be judged more on the specialist individual scheme performance, rather than the same broad brush that open market business will attract.

This ringfencing of schemes can be protective but on the flip side can still attract rate increases or changes as a result of performance. Importantly when a scheme is created it's underwritten by the insurer on its own merit of the overall performance of the specialist sector and therefore schemes will continue to be assessed with this approach on an annual renewal basis. Therefore if the specialist scheme sector is not impacted by the pandemic or hard market high risk areas it is more likely to be protected. Those schemes in sectors that are impacted for example the care sector will attract fairly the right rate increase needed, maybe higher than open market rates.

In addition to this, schemes are also slightly more protected from the terms and conditions they have applied being more favourable which limits significant changes to product and rate, again more favourable to general business.

In summary, schemes with proven track records are likely to be given more protection if with limited future threats to the scheme that could influence higher than average losses or claims trends than open market books of business brokers may have. However, this is not guaranteed, COVID19 pandemic or not, if the scheme is underperforming, insurers will take necessary corrective action to ensure the scheme is profitable for both insurers and brokers. Finally a note of caution, if capacity is being withdrawn from market due to hardening of the market to such a high level and increasing reinsurance costs continue, insurers will have to pass this on to the end customers and schemes regardless of profitability and security could be impacted.

The changing needs of customers

Customer buying habits

Customers buying habits and behaviours have been changing for years and we've seen a shift to more people buying online and customers are listening more to reviews and experience of others, gaining trust before they buy, demonstrating more informed buying behaviours. To add to this the pandemic has disrupted our lives in many ways and forced people to buy differently, from how they would usually shop in department stores to try and touch the products we are buying, to buying online without this experience but with only product summaries and customer reviews available. My view is that the growing use of

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purchasing online will be here to stay and data shows this growth over many years in particular with younger generation.

So what is the view of the impact of changing customers needs to the way we purchase insurance? Insurance Business UK states that, *'to remain relevant to consumers, insurance brokers need to focus on a couple of things. First and foremost, they must be ready to deal with prepared shoppers who are approaching the insurance transaction armed with independent research. Secondly, they need to make the most of insurance technology. And finally, they need to think about their digital store fronts and keep them updated and connected with the markets, so that the interactions across channels are seamless and efficient.* (<https://www.insurancebusinessmag.com/uk/news/breaking-news/how-the-changing-customer-mindset-impacts-insurance-brokers-225260.aspx>) - Insurance Business UK - How the changing customer mindset impacts insurance brokers – June 2020

The keys themes here are firstly the fact that those who purchase insurance are now more informed, they want a product relevant to them and purchase with confidence in the broker or direct insurer. As I have mentioned throughout my research, schemes do offer that specialism, being relevant to the sector and provide that USP to customers. With insurance a customer is buying the claims service and with schemes you are also buying a specialist claims service to the sector which is another major advantage and a key differentiator to standard market.

Secondly is technology, enabling customers to interact with brokers online, be relevant and also help brokers to understand their customers better. This is backed up in my research of insurers websites a key themes for 2021 and beyond is around acceleration of digitalisation. This is crucial with buying habits moving to online and having that presence will be an advantage over the competition. Scheme brokers who specialise in a sector, using relevant text to a sector will have opportunity for stronger google ratings and more exposure to potential customers.

In summary I feel this is more important than ever for brokers to adapt to customer changing needs, with brokers needing to respond and to add more value than ever to stay relevant to their customers. Again I see a positive link for schemes, as the focus on a niche area, having specialist knowledge and expertise to offer as well a unique product offering will set the broker apart in the market to engage customers. To summarise my research of recent customer trends, being relevant, accessible and specialised to customer needs is only an advantage.

Conclusion

Finally to conclude on why it is more important than ever for brokers to invest in schemes? I have really enjoyed researching this topic and found some surprises as well as confirming my personal thoughts.

- I want to start with schemes in general in the insurance market, my research shows that schemes are highly invested in by insurers and market share with brokers is also growing as more brokers see the value in schemes and as a result are developing and investing in schemes
- USP's of schemes were very clear, protection from open market pressures, as a scheme offers a unique product to customers, limits competition, promotes brokers brand/value and supports a solid income stream
- The SME market is in turmoil with the pandemic impacting growth in small business and placing the economy into recession. Yes this is very significant and many business will be impacted but I feel this negative finding is not strong enough to not invest in schemes now. In fact this puts more importance on brokers needing to add value to customers
- The pandemic has heightened the development of the hard market, whilst schemes do not have complete protection it does give broker and end customers some protection of profitability and not exposed to the open market broad brush changes
- Changing customer buying habits is important, I found this was naturally happening before the pandemic but the pandemic has heightened this. Customers are now more informed and are demanding more value and predominantly moving online to buy. So how can a broker react to this? They need to add value to end customers and again schemes can offer this competitive edge
- I have clearly demonstrated in my research that schemes is in fact a way to create a competitive edge in a specialist area, brokers can add value by focusing on a specialism and offer USPs to these customers which they are demanding.

Therefore my overall recommendation is that it is more important than ever for brokers to invest in schemes and add more value in the market to set themselves apart from competition and support more informed and demanding end customers. If brokers do not embrace schemes and add more value, brokers could be left behind or second choice to direct markets.

Word count

4,994

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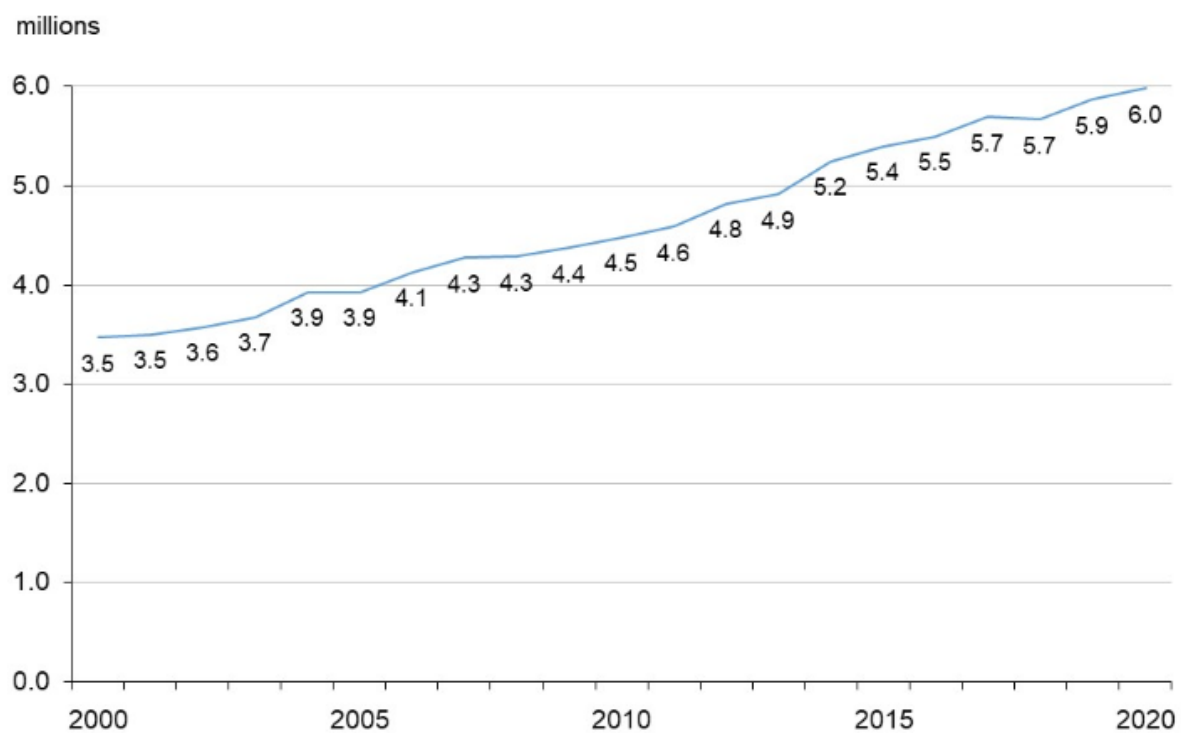
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Appendix

Appendix 1 – Evidence of businesses on the rise in the UK

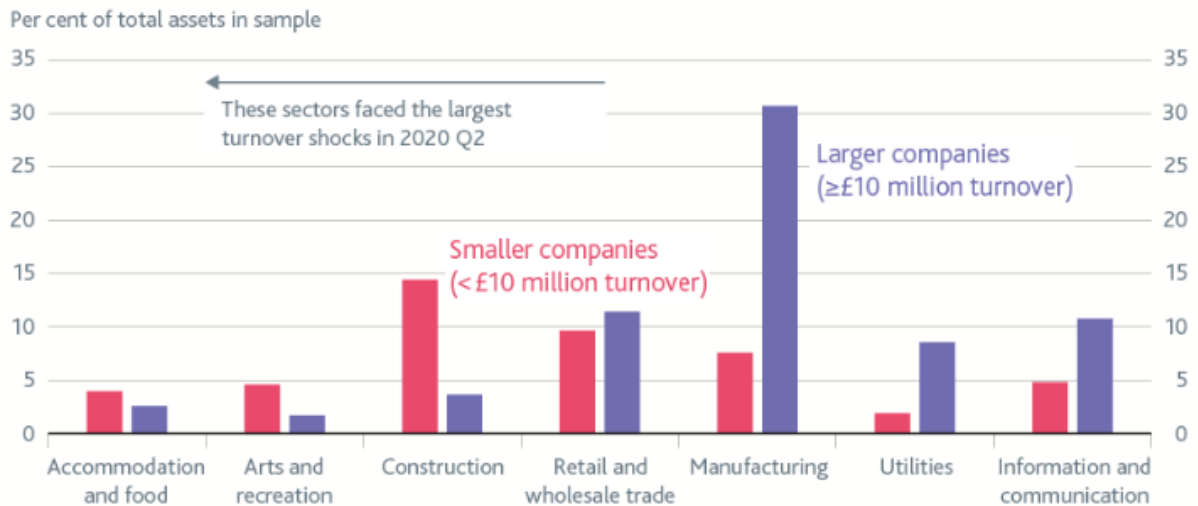
Figure 1: Number of private sector businesses in the UK, 2000 to 2020



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Appendix 2 – Impact of COVID19 to SMEs

Chart A: Smaller companies are more likely to operate in sectors vulnerable to Covid-19
Proportion of total assets among smaller and larger companies accounted for by firms operating in each sector, ordered by size of expected turnover shock



Sources: Bank of England, Fame (Bureau van Dijk), ONS, S&P Capital IQ and Bank calculations. See the [technical annex](#) of the [August 2020 Financial Stability Report](#) for more detail on the data and methodology.

Appendix 3 – The Insurance cycle

