

The untapped potential within the UK insurance market

InsurTech Thought Leadership

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Foreword

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As UK InsurTech lead, I spend most of my time with large insurers who are pursuing a digital agenda, and with younger InsurTech businesses through our unique Scale-up programme and collaborative partnership with StartupBootcamp.

When talking to both parties, one recurring theme is the untapped potential in the UK insurance market, particularly when compared to some of the dramatic changes seen in the banking industry in the past three to five years. There is a clear need for more innovation in the insurance industry, driven by increasingly demanding consumers, struggling legacy systems, and an inefficient use of ever more available data. This has created a clear divide within the industry between large insurers who are constrained by complex operating models, siloed divisions and legacy IT at one end, and more agile, customer-centric, but largely unproven InsurTechs at the other.

Facilitating conversations between these high risk young startups and the inherently risk averse insurance incumbents inevitably holds a number of challenges for all parties involved. However in order to realise the huge potential InsurTech holds we must bridge the gap that currently exists between them.

We would expect the scale of the opportunity and the amount of capital currently available within the venture capital (VC) and private equity (PE) markets to drive investment, growth and new entrants into the sector, and whilst we have seen a degree of VC activity and interest from larger, traditional PE firms, we have not yet seen the 'winners' and 'losers' in the market emerge. This can in part be attributed to the role of corporate venture capital, which may 'lock in' startups to a particular exit route at a very early stage (or at least create the perception of having done so). It can also partly be attributed to the general lack of maturity that still exists in the UK InsurTech market and, to some extent, in the market globally.

In early 2019 the PwC InsurTech team embarked on a journey to answer the following questions by conducting proprietary research with a selection of our InsurTech, Insurer and financial investor clients:

- How do InsurTechs, Insurers and Investors view the opportunities and challenges in the UK InsurTech market?
- What might the future look like for UK InsurTech?
- How much 'untapped potential exists in the market?



**We hope you enjoy reading
through our findings**



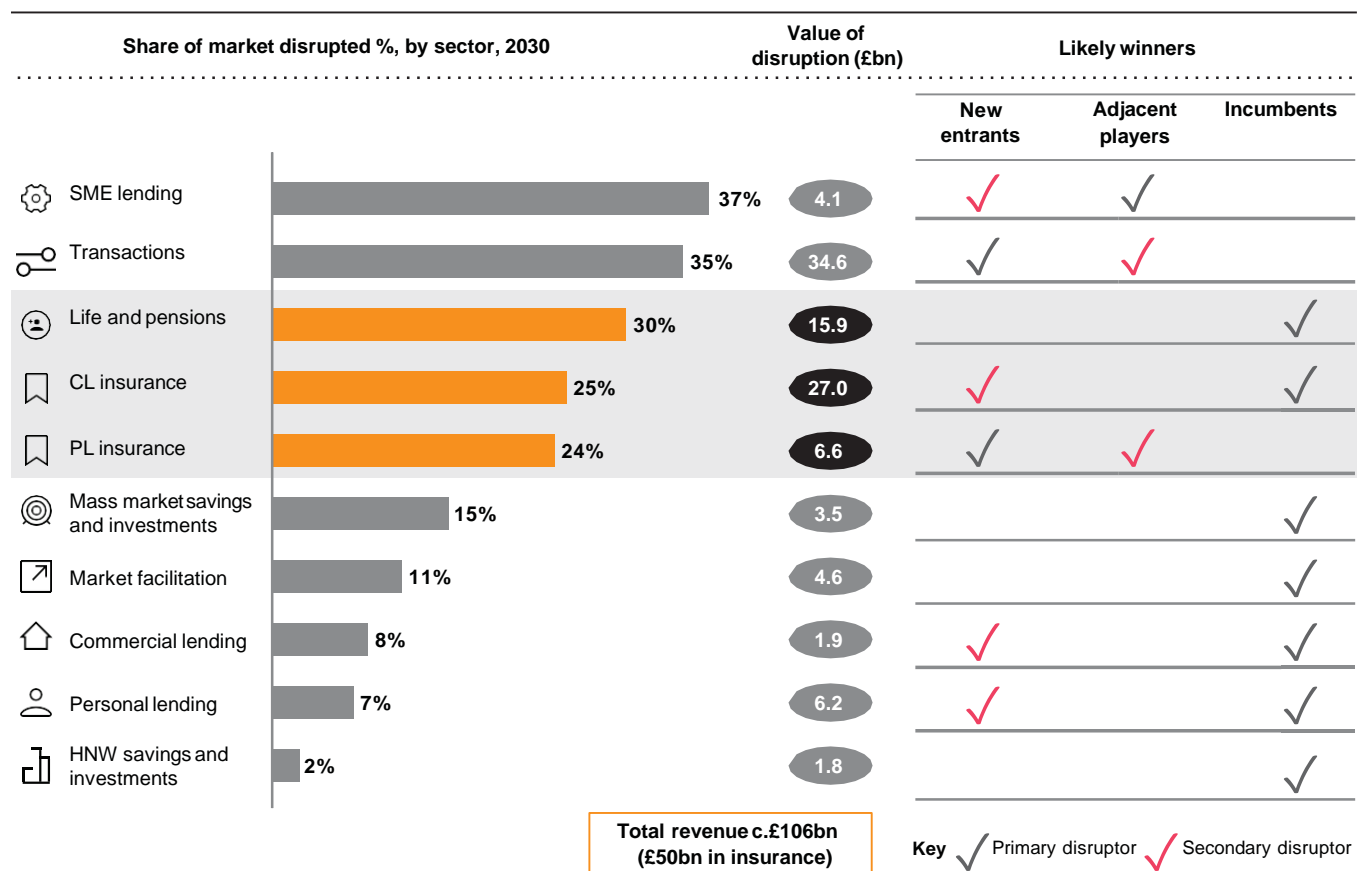
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The market today

The insurance sector represents some of the largest opportunities for future disruption with a potential for c.£50bn of revenue to be disrupted in the UK insurance market alone. The insurance market will soon follow the innovative trends of the banking industry, one example being the dramatic changes made possible by the introduction of Open Banking.

There are a number of technological advances that are catalysing disruption in the insurance industry.



Source: Strategy& analysis

54% of insurers are currently investing in artificial intelligence to increase efficiencies and better understand customers' needs

24% of insurers will make significant investments in augmented reality (AR) in the next three years to improve customer/employee experience

\$1bn invested in blockchain technology since its creation in 2009 to drive more secure transactions across a peer-to-peer network

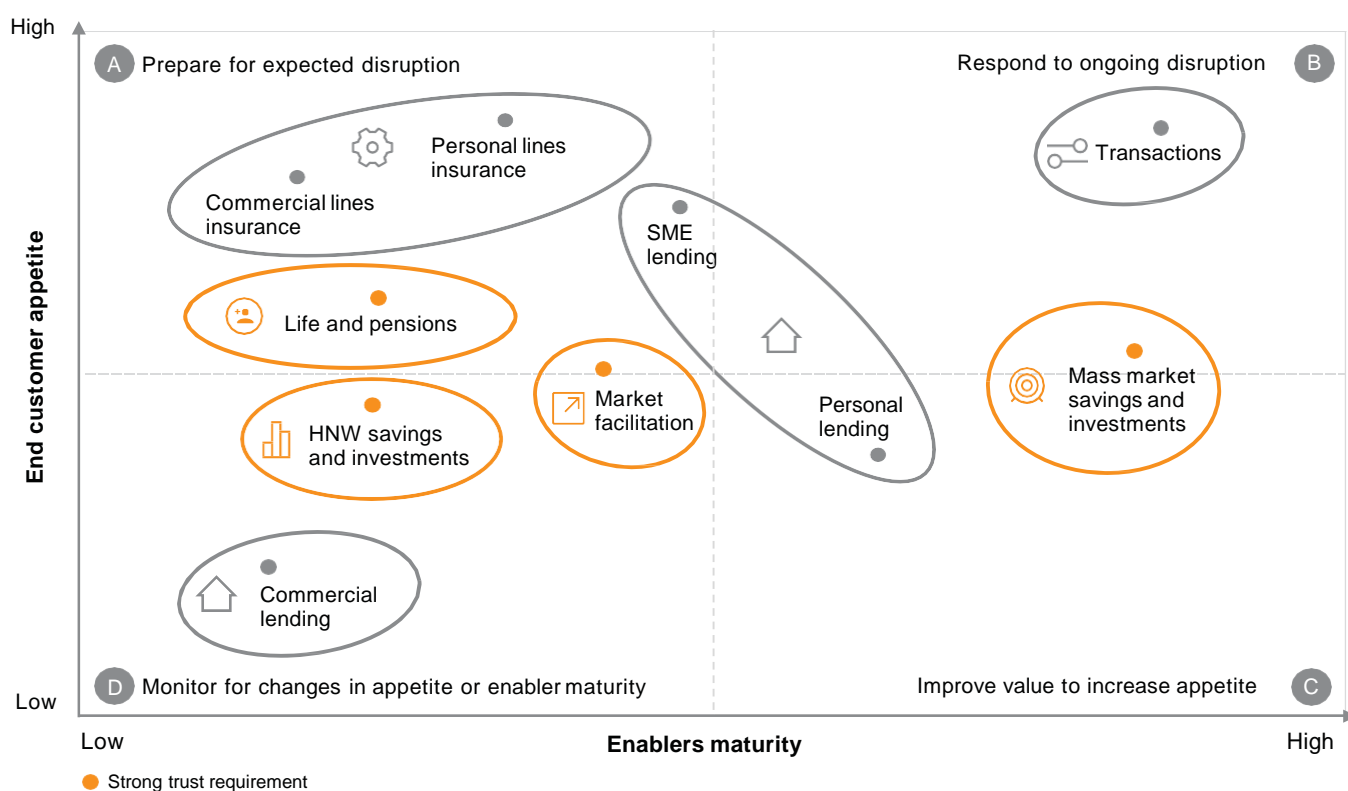
14% of insurers are expected to make significant investment into drone technology in the next three years

73% of insurers are making IoT investments today to drive connectivity and release new insights

13% of insurers say robotics will be the most disruptive tech to their business model within the next five years

\$3bn invested into InsurTech to provide complementary capabilities faster, cheaper and with better customer experience

75% of insurers are proactively taking steps to move legacy technology landscapes to more dynamic and flexible 'as a service' models



Source: Strategy& analysis

Similar to the banking market, the insurance industry has seen initial disruption in the retail segment, with 75% of InsurTech businesses serving retail clients. Innovation within personal lines insurance is all about hyper-personalisation and customer-centricity. These are attractive propositions to insurers, but ultimately, the personal lines sector is still struggling to provide the seamless omni-channel customer services that most customers have become accustomed to.

There is also a new customer entering the insurance market. The millennial has begun to take over from generation Y and this more digitally savvy customer is less brand loyal when it comes to financial products. They will continuously swap out products to fulfil their personal needs, and expect seamless switching services.

From our research, investment appetite exists within the insurance market and growth capital is available for the right opportunities. However few UK InsurTechs are yet to hit sufficient scale to warrant a large proportion of this capital, earmarked for growth investments. In many cases, seed capital has been provided, but growth is yet to come as InsurTechs struggle to gain traction past the initial pilot/proof of concept stage.

Growth opportunities for InsurTechs

The Insurance Industry challenge...

The insurance industry at every point within the value chain (from end customer to re-insurer) and life cycle of a policy (from initial enquiry to claim settlement) could benefit from additional information about their customers and the risk insured.

The insurance industry has to date only used basic automation to reduce costs and more advanced robotics to solve business problems and boost productivity (e.g. reliability and accuracy of high volume tasks).

The insurance industry is looking for cost effective ways to engage with and use technologies and scale those across often global organisations.

There is a new type of customer entering the insurance market, the millennial, who demands not only a great product but also flawless customer service. This customer is fluid in their insurance needs; they rent rather than buy (housing and transport), are willing to shop around and want to be recognised as having their own unique needs.

How InsurTechs can help...

The opportunity to use technologies such as IoT and drones to gain deeper insights into customers and their behavioural patterns, through more rigorous collection, exchange, and analysis of data is already proving invaluable in supporting faster and better decision-making processes across operations.

Technologies such as AI, with a combination of machine and deep learning models, can support the industry in moving past the simple streamlining and standardisation of processes, to a world of straight through processing. This will enable the development of new offerings, delivering operational enhancement and increased customer service.

Collaboration with InsurTechs provides opportunities for companies to complement their capabilities and allow for more innovative approaches, and for technologies to be tested before roll-out across the wider organisation. With the shift towards cloud-based 'pay as you go' models, achieving more transparent, cost effective and on-demand use of technology, this is opening doors for the industry to embrace this approach.

InsurTechs are perfectly placed to provide a hyper-personalised, on-demand service to this new customer given they are smaller, more agile and not tied down by legacy systems. Technologies such as augmented reality provide marketing opportunities and more proactive engagement.



What do InsurTechs want from the Insurance industry?

As a group, InsurTechs tend to view themselves as the catalyst for change within the insurance industry. They believe that through partnerships they can aid incumbent firms on their journey to innovate.

In general, InsurTechs do not have 'the answer' to an incumbent's problems. Rather they have tools and capabilities that can be utilised to find the answers, generate efficiencies and enhance existing processes and business models.

To allow this to happen, InsurTechs have several requests of insurers, although in the main they centre around working together in partnership rather than as two separate entities. Collaboration is key. This can be facilitated by the sharing of data and ideas between InsurTechs and incumbents, but trust must occur despite the potential for the InsurTech to have multiple business relationships within a single industry group.

InsurTechs are calling for more understanding from insurers about the types of businesses they are, the life-cycle stage they are in and the resulting working relationship that is needed to effect large scale change.

UK InsurTechs have shown some success, but many still struggle to get much beyond the 'proof of concept' stage of development. Insurers will trial them, show willingness to organise and run pilot collaboration, but then falter when moving to scale beyond this.

'Collaboration is key'



What do Insurers want from the InsurTech industry?

The insurance industry is aware of the need to change but incumbents are often limited by the realities of their size and the scale of their operations. In particular, the ever increasing burden of regulation, complexities arising from an array of legacy IT and a history of risk averse behaviour are all creating an environment which does not naturally lend itself to entrepreneurialism or fast paced change.

The inability to marry expectations of what is realistically attainable and the ease of which this can be achieved and replicated across a wider organisation leads to frustration for both the InsurTech and the incumbent insurer.

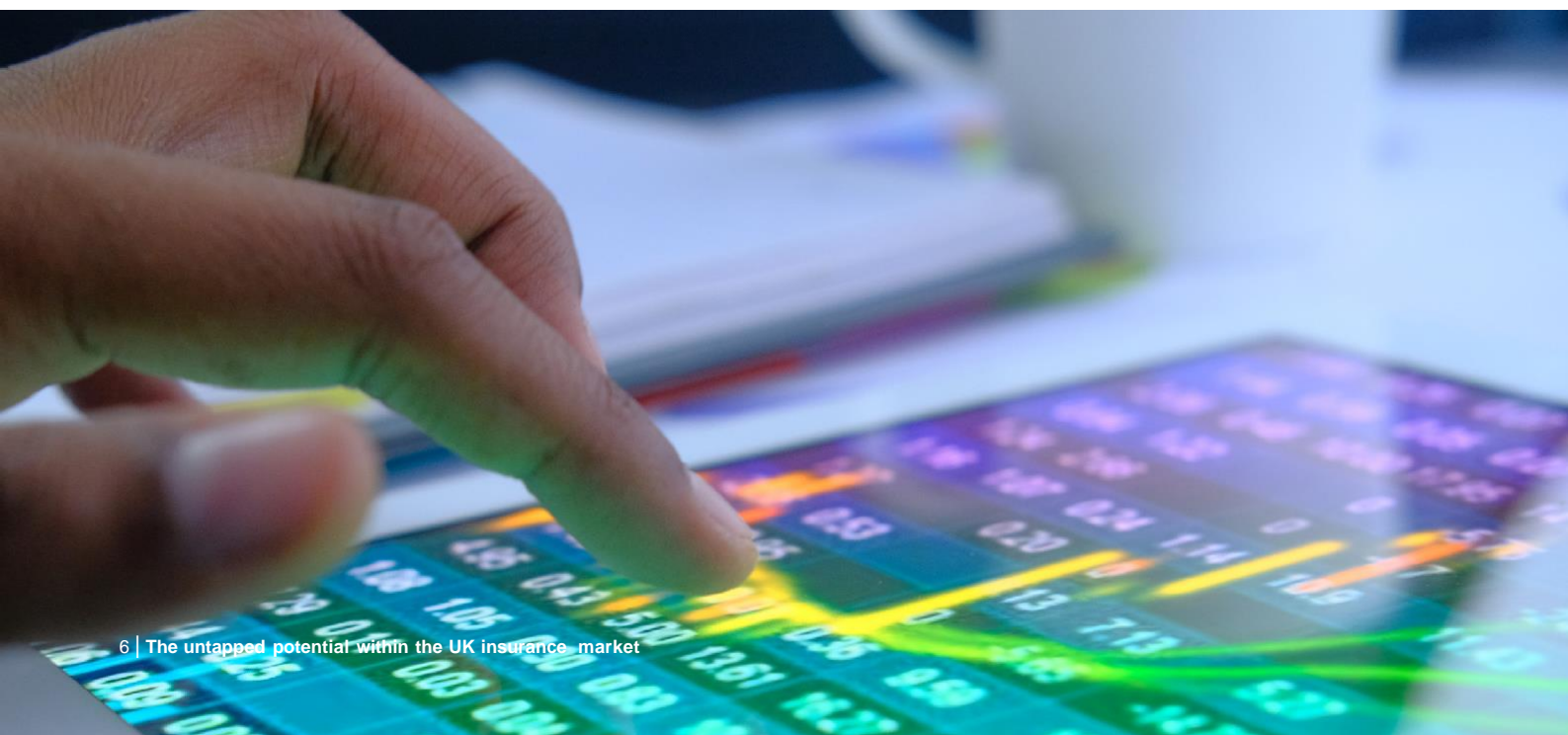
Insurers are concerned with replacing 'old legacy' with 'new legacy', and are seeking ways to drive down their combined ratios through better use of technology without contemplating an entire system rebuild or complete re-platforming of their operations.

InsurTechs are ideally placed to support this change, but will need to strike a balance between what can be done in an ideal world and what is practical for many of the incumbents they seek to collaborate with. InsurTechs need to focus on developing solutions that are scalable and can be implemented, integrated and supported by the chosen partner.

Currently most incumbents are running legacy systems and have agreed 'upgrade' plans in place with larger systems vendors. They are not therefore in a position to move quickly, trial new solutions, or shift their corporate culture to a less risk averse mind-set.

Incumbents are aware of the opportunities that InsurTechs represent, they are just unsure how best to interact as there is a degree of risk in being the 'first mover' that few are willing to take.

An open approach to collaboration in the insurance industry will foster an environment of innovation and bring an industry that has often been playing catch up to one that is on the cutting edge of change.



What do investors make of the market opportunity?

1 Underlying market dynamics are attractive and there is a clear opportunity to drive value in insurance through technology

The insurance sector is an attractive investment proposition for both VC and PE, particularly in the capital light areas of distribution and technology – the latter being seen as key to transforming and driving value in the industry

2 VC and PE investors are keen to deploy capital into InsurTechs, but need them to have achieved a degree of independent success

Investors see the market as still young, with many InsurTechs still at a very early stage of development – as they mature, grow and begin to establish themselves as successful, scalable businesses, additional capital pools will become available to support growth

3 InsurTechs need to focus on sustainable solutions that will generate long term profitability

For investors, InsurTechs need to focus on solutions for which there is a large addressable market that can be served profitably. Many have a preference for B2B solutions, although there remain areas of the B2C market which attract investment – in both markets, solving 'real' problems in profitable segments is key to underpinning long term success

4 Evolution not revolution is often the preferred focus for investment, as barriers to entry are perceived to be high

Insurance is a highly regulated industry and creating a true 'challenger' to incumbents is not without its difficulties. Much of the investment focus from VC and PE markets is on evolution rather than revolution, as investors have significant appetite for propositions which can drive improved efficiency and profitability for existing players

Bridging the gap



InsurTechs' point of view

- Incumbents underestimate the value an InsurTech could bring from a successful partnership.
- Incumbents need to embrace entrepreneurialism and be curious to maximise potential.
- There is only so much 'proof of value' achievable unless insurers share data.
- Better collaboration and partnership models are needed to proceed.



Insurers' point of view

- InsurTechs are ambitious and have high expectations about what can be achieved and at what speed. This can create 'culture clash' when dealing with insurers who have a well entrenched way of working and embedding solutions across the business.
- InsurTechs embrace emerging technologies and cloud-based solutions, which continue to prove challenging for insurers who are working with legacy IT systems requiring complex integration and poor data sources.
- InsurTechs need to present solutions to problems that actually need fixing from the insurers perspective*.
- Scalability is key. If a solution works for a specific problem then it needs to be leveraged across the whole organisation in order to maximise value and ROI.

Bridging the gap

Understand the reason behind the innovation

- 'Innovating' for the sake of it will only create an unending cycle of change and a constant churn of delivery partners (Startups, system vendors, etc.). Understanding the problem and fundamentally why change needs to happen will allow clarity from the start and a more meaningful and productive relationship between InsurTech and Incumbent.

Collaboration

- Once understood, in order to overcome the problem being encountered, sharing knowledge, expertise and even developing intellectual property together is key. This will allow all parties to gain access to the information, data and knowledge they need to add the most value to the partnership. Sharing knowledge and data between both parties should be seen as a way to enhance the relationship rather than a threat of the other gaining more competitive advantage.

Communication

- Sharing this collateral is great but it needs to be the right collateral. Having a two way open channel of honest communication between the InsurTech and Incumbent will clear any confusion and ambiguity around problems, solutions and ability to deliver together. This will allow clarity on what the problem to be solved is, what the solutions will be and what the conditions around this are (budget, time frame, etc.).

Continuous innovation

- There should be an environment of continuous innovation fostered between the InsurTech and the Incumbent and the relationship should not finish once the project is up and running and embedded in business as usual.

The future of Insurance

As can be seen, the insurance industry is complex and is facing a number of challenges. This calls for an evolution of the current set up of the incumbent, one in which InsurTechs will play a vital role.

Open insurance New entrants

- Open insurance is expected to break down access barriers within insurance, allowing more organisations access to more data. As a result, we should see increased competition from players not traditionally active in the insurance sector, whether they are startups attacking underserved niches or trusted non insurance brands moving into the insurance space. Either way, incumbents will need to be ready to react.

Evolving customer expectations Service propositions

- Service can be a differentiator, as evidenced by the inroads made by InsurTech businesses which already show a clear focus on customer needs. Service living up to customer expectations will become more important as the competitive landscape evolves.
- The need for continued personalisation and speed of service will shape the method of distribution.
- We expect to see further division between personal lines and commercial lines.

Breakdown of the value chain New business models

- The only place incumbents have competitive advantage is in the area of capital, being seen as a custodian of capital, having proper safeguards and adhering to regulations. New entrants will struggle to build and manage a balance sheet in today's regulatory environment.
- Brand is not a competitive advantage for the vast majority of insurers. Most insurance is already intermediated and the end customer is not brand loyal.
- We can see an insurance industry in which today's incumbents are the providers of capacity, with more agile, non traditional insurance providers owning the customer relationship and fulfilling other roles in the insurance value chain.



Conclusion

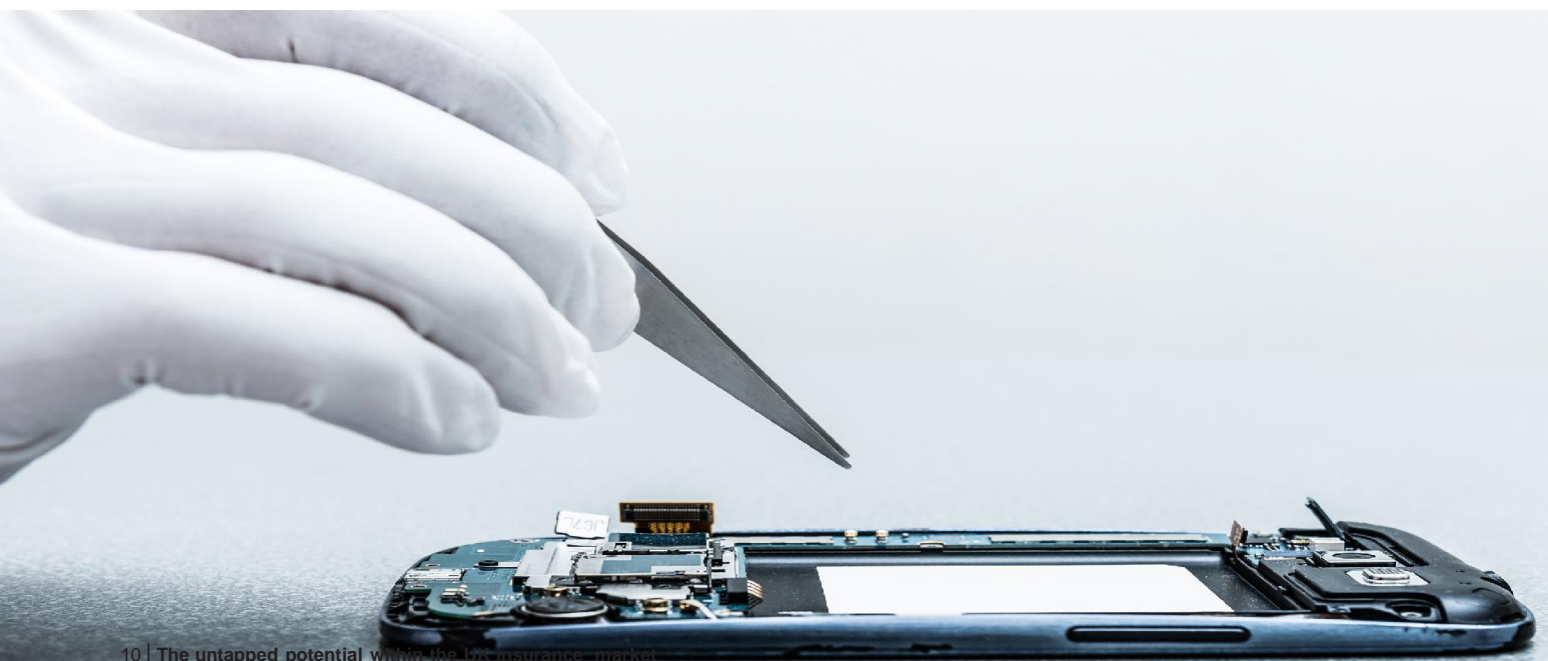
In conclusion, the insurance industry is poised for much needed change, and no doubt among InsurTechs and Insurers there are better ways of operating than those employed today. There is appetite for change, but a lack of understanding of how to effect change in the right manner, particularly when that change may well involve a fundamental shift in mind-set and there is no guarantee of success.

InsurTech, Incumbents and Investors all see significant opportunity to follow in the footsteps of the banking industry, bringing insurance into the 21st century with new, digital, agile business models that put customers first. We have to date however not seen any real disruptive success from startups who choose insurance as their primary market.

So if today's InsurTechs and insurers want to be the success stories of the future, they will quickly need to learn to work, grow and mature together. The evolution of this relationship needs to happen faster than it is today: customers are becoming ever more demanding and in many cases are apathetic about where their insurance comes from.

To succeed, insurers will need to 'know their customers' in a frictionless way – to predetermine what they need, to offer hyper personalised products, to properly tailor pricing to an individual's risk, and to manage claims faster and more effectively.

This requires an efficient back office, data-rich underwriting, and understanding of consumer behaviour along with an efficient claims process. Insurance needs to be about protection and risk prevention, sold on a real understanding of need and easily accessed by those who need it.



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