2016 EY Latin America insurance outlook
Market summary

A market in flux
Despite sluggish economic growth and troubling inflation in key markets, the 2016 insurance market outlook for Latin America remains relatively bright. The rollout of new insurance products and distribution approaches at a time of low market penetration should drive strong growth for insurers. Insurance premium growth is expected to rise by around 6%-7% in 2016 and possibly beyond should the economic environment improve as expected.

At the same time, the emergence of end-to-end digital capabilities is transforming the Latin American insurance market. This digital market disruption will force insurers to make rapid revisions to existing business models to stay competitive and build market share.

Customer expectations rising
Commercial customers will continue to require more sophisticated insurance solutions in 2016, including coverage for business interruption, cybersecurity, civil unrest, and errors and omissions. Latin American consumers, many of whom are young, cosmopolitan and tech-savvy, will continue to push for new insurance channels and services that fit with their lifestyle. To respond, insurers will need to simplify and adapt products for millennials, and sharpen their focus on mobile and social media interactions.

Evolving customer needs throughout the region are compelling insurance companies to rethink their strategies, processes and services. The rise of financial technology, or fintech, companies is causing insurers, particularly in the consumer insurance sector, to reconsider their business models and increase their investment in new digital technologies. Despite a desire to avoid conflicts with legacy models, insurers realize that flexibility, efficiency and innovation are critical for success in a more demanding marketplace.
Competition heating up
The liberalization of industry regulation across Latin America has opened insurance markets to wider competition. The abundance of insurance capital has intensified competition from various directions: from global insurers seeking a foothold in the region to local insurers looking to expand cross-country to entrenched insurers defending their turf. These competitive trends are keeping insurance rates flat through much of the region and, in some cases, pushing them lower. The most substantial rate decreases have been in non-catastrophe property.

Pockets of premium increases can be found in areas of instability, such as Venezuela. However, insurance capacity is very limited for Venezuelan political risk, with most risks dependent on the international reinsurance market.

As markets develop in Latin America, commercial demand is increasing for new forms of insurance coverage, such as environmental liability. The opening of the oil industry to the private sector in Mexico, for example, is exposing new oil exploration and production entrants to potential losses from environmental damages. But market capacity is still restrained in key markets, such as Brazil, where only a few insurers offer such liability coverage.

Growing contagion risk
The global economic slowdown is exposing the region to greater contagion risk. Lower demand for natural resources, such as oil, is dampening both exports and incoming foreign direct investment. Reduced demand from China, one of the largest export markets for Latin America, threatens the economic health of the region and its insurance markets. A prolonged China slowdown will endanger the relatively recent progress that Latin American countries have made in expanding their middle class, a phenomenon that has supported premium growth in excess of gross domestic product (GDP) growth.

Adding to economic worries, local inflation and associated currency devaluations have reduced insurer profitability. In the past few decades, Latin America has made substantial progress in stabilizing inflation in much of the region. But inflation rates now vary widely by country, with Venezuela (180%) and Argentina (17%) at one end of the spectrum, and Mexico, Chile and Peru at the other end, with rates below 5%. Brazil, the region's largest economy, has seen a worrying rise in inflation to close to 9% for 2015.

The strength of the US dollar in 2015 was driven partly by anticipation of an end to US monetary easing. When the U.S. Federal Reserve does eventually begin hiking interest rates, this may further dampen investment in regional emerging markets in favor of the US and other mature economies. Any further strengthening of the US dollar would also be problematic for a number of Latin American governments, corporations and financial institutions, all of which have large amounts of dollar-denominated debt. On the plus side, lower exchange rates may help make Latin American exports more attractive.
Continued market consolidation

Consolidation within the insurance industry is developing in a complex and circuitous path in Latin America. The 10 largest insurers for the Brazilian physical damage auto line of business (Automóvel Casco) have increased their market share as a bloc, from 65% in 2005 to around 84% in 2015. However, among the five largest insurers, there has actually been a decrease in market share, from 54% in 2005 to around 45% in 2015. Mexico’s Individual life insurance lines indicate more advanced concentration, with the top 10 already at 95% of the line in 2005 and the top five increasing to 81% in 2015 from 78% in 2005. But, again, this concentration masks some significant shifts; for example, the market share of the industry leader shrank substantially while that of the sixth largest insurer quadrupled to more than 20% in 2015.

Mergers affecting Latin American insurance markets in recent years, such as the recent merger between Chubb and ACE, have focused on driving growth and efficiencies. Another example is Colombia’s Suramericana, which recently acquired British Insurer RSA’s Latin America operations to expand its reach into other regional markets.

Greater regulatory change and complexity

The Latin American regulatory landscape is becoming more complex. The evolution toward risk-based capital and harmonization with global solvency standards is spreading across the region at different speeds of adoption. Mexico is in the regulatory vanguard, having adopted rules based on the second and third pillars of the European Union’s Solvency II in April 2015, while its Law for Insurance and Bonds Institutions will implement the quantitative pillar I in 2016.

Brazil has also developed a standard risk-based capital framework similar to Solvency II. Based on advancements of regulatory harmonization with Solvency II, the European Commission adopted provisional third country equivalence for Brazil and Mexico. While this enables insurers to operate in the EU without complying with all EU rules, it also allows EU insurers to use local rules to report on their operations in third countries.

Chile has also made progress on developing its regulatory model toward risk-based capital to achieve third country equivalence with Solvency II. Unfortunately, most insurers there have not established a robust risk management infrastructure. Farther behind, Colombia’s insurance regulation is undoubtedly moving toward the more risk- and economic- value-based Comframe.

In contrast, many other Latin America countries have been slow to modernize. They continue to follow traditional factor-based capital models that are consistently applied to all lines of insurance. For example, despite the Argentine regulatory authority’s recommendation for adoption of a risk-based capital system, there has been little progress to date. Solvency modernization and Comframe remain lower on the agenda than other issues, such as market growth and consumer protection.

Similarly, Venezuela’s regulators have not presented new solvency reform proposals since the enactment of the Insurance Activity Bill in 2010 (Ley de la Actividad Aseguradora, LAA). Although this law has improved reserve and minimum capital provisions, it has not moved solvency toward risk-based capital models or supervision. Rules pertaining to corporate governance and enterprise risk management remain uneven and lack a solvency focus.
Impact of external factors on the Latin America insurance market in 2016
(0 = Low impact, 10 = High impact)

**Technology**
Insurers in key markets are developing digital strategies and services to meet rising demands from customers and regulators for greater responsiveness and risk transparency. Investments in new digital technologies lead to revised operating models.

**Catastrophes**
Much of the region is exposed to storms, earthquakes and floods. Although predictive models have become more sophisticated, data adequacy remains limited. Reinsurance capacity and pricing are sufficient going into 2016, subject to potentially market-changing events.

**Economy**
The Latin American economy is expected to expand modestly in 2016. Mexico is slated for slow, steady growth, but Brazil will likely remain in recession. A slowdown in China and higher interest rates in the US could dampen growth further and raise currency risks.

**Inflation**
Inflation is a major threat for several countries, such as Venezuela and Argentina. Exchange rate deterioration from a stronger US dollar could accelerate inflation for Mexico and other countries that import substantially from the US.

**Competitiveness**
The marketplace generally remains competitive in Brazil and Mexico, but has not resulted in substantial price decreases. Throughout the region, competition is from both domestic and foreign insurers. Moderate downward pressure on prices will continue.

**Regulation**
In 2016, Mexico expands its Solvency II regulation to include the quantitative pillar. Other countries are moving slowly, or not at all, toward more detailed risk-based capital analysis and reporting.
Navigating through change: priorities for 2016

Winds of change are sweeping across the insurance market in Latin America. From regulatory reform and demographic shifts to rising competition and globalization, these megatrends are transforming the region’s insurance market. Taking advantage of these upheavals will require a rethinking of strategies, solutions and business models. But for companies quick enough to act in 2016, the growth opportunities in the consumer and commercial sectors could be enormous.

Developing a navigation chart for change:

1. Embrace digital transformation to meet rising customer demand
2. Stay on top of regulatory changes and market disparities
3. Develop the right talent and analytical tools to drive change
4. Penetrate the life insurance market through innovation
5. Target general insurance products to the rising middle class
6. Provide solutions for a more sophisticated business market
Taking advantage of digital shifts

Like other regions of the world, Latin America’s marketplace is undergoing a digital transformation. In 2015, e-commerce sales grew by more than 20% to $50 billion in the region, as digital channels became central to the marketing mix. Following the lead of the banking industry, insurers are now developing digital strategies and services to meet fast-changing consumer needs and to head off threats from fintech entrants to the insurance market. Companies that act now will be able to build market share and avoid falling behind the competition.

Accelerate innovation to meet changing customer demand.

The insurance market has outpaced economic growth in the region for the past few years, but there is still a huge opportunity to increase market penetration. As an example, an estimated 70% or more of drivers in Brazil are uninsured beyond the compulsory third-party limited minimum coverage they receive with payment of their road tax. Insurance market development, estimated using a percentage of GDP, indicates a 2.5%–4.0% insurance spend for Latin American countries compared with more than 6.5% for the US. In 2016, insurers should explore innovations in price efficiencies, connectivity and product fit to foster growth.

Develop an end-to-end digital capability that offers a positive customer experience.

Widespread, low-cost access to online and mobile technologies has raised customer expectations for digital services. Similar to the banking industry, digitization of insurance is following a path from online toward mobile use, with digital access now eclipsing other customer touch points. Building this capability will require significant investment, because it calls for an integrated platform that captures, analyzes and executes on retained data and the real-time customer conversation.

Compete on robust process efficiency of distribution and administrative services.

Competition is heating up in Latin America, with domestic insurers defending their markets from expansionist global and regional insurers. To stay competitive, insurers will need to further improve their operational, administrative and distribution systems. These systems will need to be scalable and agile in order to respond to rapid changes in customer expectations and boost cost efficiencies.

Build the technological infrastructure needed to drive digital transformation.

Built for less complex times, many legacy systems cannot support today’s digital market imperatives. To cope, insurers will need to shift from inward-focused legacy infrastructure to customer-centric systems that accelerate speed-to-market and provide a platform for ongoing innovation. Managing such a shift will be challenging since companies will need to balance the move to a digital world with the need to maintain, retain and/or migrate their legacy customers.
The move toward risk-based capital requirements
As Latin America’s role in global trade expands, insurance regulators are adopting global standards of governance, capital and risk transparency. Regulators across the region are increasing their oversight of the insurance industry, with many shifting toward risk-sensitive capital solvency standards and harmonization with the EU’s Solvency II quantitative reporting. Mexico is leading the move to risk-based capital solvency, with Brazil and Chile close on its heels. Rather than following piecemeal regulatory changes, forward-looking insurers should create their own vision for advancing risk transparency and capital management protocols.

Priorities for 2016

Partner with governments, regulatory organizations and other financial industry stakeholders. Sharp variations in market maturity, customer development and insurance regulation throughout Latin America prevent insurers from adopting a single trans-regional approach. Cooperation among insurance companies, government bodies, associations and other financial industries will accelerate the development of a more consistent insurance regulatory framework across the region.

Maintain diversification and flexibility. RBC- and Solvency II-styled rules are still evolving in the region. Although the impact on required measurements, reporting and required capital remains largely unknown, the industry is expecting and bracing for a jump in required capital. Product diversification and flexibility will help insurers reduce additional risk capital charges and lessen a potential increase in required capital.

Implement enterprise-wide risk management systems across regions and insurance products. Declining interest rates have prompted Latin American insurers to strengthen risk-adjusted profitability through enterprise risk management. Upgrading risk management may be the best strategy for creating and sustaining a competitive edge in saturated markets.
Develop the talent and analytical tools to drive change

Filling the capabilities gap
The Latin American insurance industry is making major strides in quality improvement and process efficiency, especially through the application of technology and talent. This is particularly true in the areas of financial reporting, underwriting and event-risk mitigation. Some insurers have become proficient at building portals and broker connectivity. Nonetheless, analytical capabilities and technical systems in Latin America are still not sufficiently robust to support impending market shifts.

Priorities for 2016

Use analytics to gain insight into customers and competitors. Until recently, Latin American insurers have made limited use of predictive analytics, applying it typically to underwriting. But this is changing, especially in Mexico and Brazil, thanks to advances in digital technology and data analysis. Insurers in the region are now better equipped to use analytics to drive customer-driven sales efforts and gain access to competitive intelligence.

Develop the right talent to guide the future. Driving innovation and digital transformation requires fresh thinking and new talent. Investment in recruitment, training and career development in recent years has raised the capabilities of insurance professionals in key Latin American markets. But as general and life insurance markets shift to younger customers, insurers will also need to attract young professionals to guide the future.

Manage catastrophic risk through advanced analytics. Hurricanes, earthquakes and floods are common threats to many countries in Latin America. To cope with these risk events, insurers and reinsurers need to improve catastrophe risk modeling and fill gaps in data availability. In 2016, companies will invest more heavily in data and real-time risk models to analyze and plan for these threats.

Enhance claims management through technology and analytics. As insurers in the region deploy advanced analytics, they will be able to re-engineer processes to achieve greater efficiency and effectiveness. Predictive analytics can optimize the claims process through the claim life cycle, while increasing data for both claims efficiency and customer experience. Analytics-driven intelligence will become a more valuable competitive tool.
**Penetrate the life insurance market through innovation**

**Room for sustained growth**
Latin America generates around $65 billion in annual life insurance premiums. Thanks to past economic growth, the region has seen the rise of a young, middle-class consumer market. But there is still substantial room for growth: except for Chile (at just more than 2% of premium as a percentage of GDP) and Brazil (at just more than 1%), life insurance penetration is less than 1% in each of the five largest country-defined markets.

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MAPFRE “The Latin Insurance Market Preview 2014” and The World Bank

**Priorities for 2016**

**Foster an enterprise-wide culture of innovation.** Insurers will need to turn creativity into a core capability by developing a culture of innovation. Success will require the support of top management to drive shared communication across the enterprise and ensure healthy collaboration between business units. Forward-looking insurers will invest in product experimentation and develop new metrics to gauge their progress.

**Broaden market reach through new distribution channels.** Increasingly, legacy methods for reaching customers are no longer fit for purpose. Customers in Latin America are demanding greater product transparency, broader availability and faster service delivery. In today’s changing marketplace, customers do not want to be “sold” insurance products, they would rather “buy” them. Giving customers the ability to buy insurance products directly can also help keep the costs down, another key concern of informed customers.

**Create innovative products to increase flexibility and understandability.** The need for financial stability is growing for Latin America’s new middle class of young consumers. But unlike older generations, these customers do not have a tradition of purchasing insurance products or an appreciation of their benefits. Offerings need to be flexible to provide value even within a lower range of acceptable price points. Crucially, product features and transaction processes must be easy for new customers to understand.
An emerging middle class is opening insurance opportunities

The emergence of the middle class in Latin America has been a boon to the general insurance market. Insurance growth has risen in high single and double digits as more individuals have purchased vehicles and other products. Nevertheless, the overall penetration remains low compared with mature insurance markets.

Priorities for 2016

Tap social media to understand customer attitudes and behaviors. Social media usage continues to increase, with penetration approaching 75% in Latin America. Given the limited availability of premium rating data in Latin America, social media can be a useful tool for populating consumer demographics, beliefs and behaviors through customer-insurer engagement and data capture.

Target customer segments through better use of data and analytics. Analysis of strategic data from social media will help insurers to identify profiles of high-potential customer segments. Insurers building customer-centric marketing activities will want to create a tailored approach for penetrating these high-value customer segments.

Expand two-way communication with customers. Today’s consumer wants better communication and service. Creating a dialogue with customers requires more advanced communication and listening skills to develop a strong insurer-customer relationship. By nurturing such customer relationships, insurers will be better equipped to design products that fit the needs of the emerging middle class in Latin America.
As business goes global, insurance needs become more complex
Companies in Latin America are becoming more sophisticated as they expand across borders and modernize their operations. In response to trade liberalization and foreign investment, local businesses are building more advanced international supply chains and risk management capabilities. Local insurers will need to play catch-up with global insurers now offering sophisticated risk management products in the Latin American market.

Priorities for 2016

Build market potential by offering more sophisticated commercial insurance. In recent years, Latin American companies have expanded their operations across the region and into global markets. As they increase their cross-border business, these firms are requiring more complex and alternative approaches to risk and capital management. Insurers are responding with greater capacity, expertise and innovation. Insurers that develop the right technical know-how and infrastructure will be in a strong position to take market share — especially as more countries embrace regulatory reform and harmonization with other regimes.

Enhance risk management service through customer collaboration. As regulatory and business complexities arise, the demand for innovative cost-saving solutions continues to increase. In today’s changing marketplace, commercial customers are increasingly seeking consultative advice and custom risk-mitigation initiatives from their insurers. But more sophisticated solutions require greater use of advanced analytics, skilled technicians and customer-facing professionals. Insurers would be wise to keep this top of mind as they enter 2016.
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