In the past decade, insurance companies have experienced some dramatic shifts. Many of the trends that we have discussed in previous outlooks have changed the shape and direction of the industry. Issues include increasing customer sophistication, growing use of technology across all aspects of the insurance value chain, greater collaboration and alignment with insurance regulators, and significant innovation in the products being offered.

In 2014, insurers in the Asia-Pacific region will continue to face slower economic growth, a lingering low-interest-rate environment and regulation that is wider in scope and severity at the national and regional level. However, the liberalization of trade barriers (as evidenced by the Shanghai Free-Trade Zone in the fall of 2013 and the 2015 target date for ASEAN integration) and the continuing increase in middle-class and high-net-worth consumers is highly favorable for the insurance industry.

As insurers in Asia-Pacific assess these challenges, they are responding with cost control and internal process improvements. Many are consolidating cumbersome legacy systems and implementing data analytics to build more efficient operations and improve underwriting and claims practices.

**Successful insurers in Asia-Pacific in 2014 will:**

- Deploy products to meet changing consumer needs
- Exploit pockets of higher growth
- Develop digital distribution strategies
- Get ahead of regulatory developments
- Implement data analytics for competitive advantage
- Identify areas for expense reduction
Deploy products to meet changing consumer needs

EY expects the Asia-Pacific region’s share of the global middle class to nearly double, rising from 28% in 2009 to 54% in 2020. The increasing individual wealth and aging population will create opportunities for insurers to introduce new products to consumers that protect their hard-earned financial and physical assets.

Health and non-life products

Demand for health insurance is expected to rise for several reasons: the aging population, strain on public resources and rising consumer affluence. Currently, 10% of the population in Asia is over 65 years old, but that number is expected to double within the next three decades, creating a need for various insurance solutions.

Many governments in the region, including those in India, Indonesia, Malaysia, the Philippines, Singapore and Vietnam, assume less than 50% of health care expenditures (an estimated US$197 billion in 2013, according to Swiss Re). The rest is covered by private insurance or paid for by individuals, creating an opportunity for private insurers to supplement the public sector provisions with their products.

In China, the establishment of foreign professional health insurance institutions in the country’s new Shanghai Free-Trade Zone has the support of the China Insurance Regulatory Commission (CIRC). This implies that high-end health insurance is increasingly important and further supports China’s growing interest in the global health insurance service system.
Across Asia-Pacific, the exponential rise in automobile ownership highlights the need for motor insurance. The number of privately owned automobiles in China exploded from virtually nil in 1985 to an estimated 120 million cars today — and is expected to grow to 200 million vehicles by 2020. At present, motor insurance is the largest non-life insurance line in the country. Compulsory third-party liability alone accounted for 72% (400 billion yuan) of China's aggregate non-life premium in 2012. Seven non-Chinese insurers have entered the third-party liability automobile insurance market since it was opened to foreign competition in 2012. Rising Asian affluence is not only supporting the automobile market, but it is also generating more travel abroad and a greater need for travel insurance.

**Savings products**

Regulatory changes are opening the savings market to new entrants. In China, for instance, the Securities Investment Funds Law liberalizes regulations to permit the formation of insurer-based mutual funds. The Asia Region Funds Passport is another key regulatory development, streamlining the process by which the fund managers of Passport members in one country market their savings products in other Passport member economies. Implementation is targeted for 2016.

As insurers consider opportunities in the savings market, they need to evaluate methods of product development and distribution. Forming a partnership with an existing fund manager to access a wider range of products is one channel; another is to offer internally developed and managed funds utilizing the existing sales force. Insurers also could build on existing bancassurance relationships. Studies indicate that nearly half (45%) of more than 470 banking entities across mainland China, Hong Kong, India, Indonesia, Japan, South Korea, Thailand and Vietnam offer investment-related life insurance or retirement savings products.

To succeed, insurers must evaluate the impact pure savings products will have on internal cash flows, capital and risk requirements. Systems may need to be built or integrated with existing processes to handle this new savings business.
Exploit pockets of higher growth

New pathway to China market

Shanghai’s new financially oriented free trade zone may prove a major opportunity for the city to become the financial capital of East Asia. China also hopes to transform Shanghai into a laboratory to restructure the country’s financial sector.

Both property/casualty and health insurers may benefit from the new free trade zone, which covers seaport and airport areas in Shanghai and offers favorable treatment for shipping companies. The increased volume of cargo and overall trade going through the zone will create a greater demand for cargo and liability insurance.

The challenge for insurers will be that the free trade zone is the first to specialize in finance in China. Regulations around the zone are complex, requiring an in-depth review to understand their implications and impact.

ASEAN new market and platform opportunities

A large number of customers and the potential for stronger economic growth in 2014 bode well for insurers in the ASEAN member states. With a population of approximately 600 million, ASEAN countries are expected to see stronger overall GDP growth than mature Asia-Pacific economies in 2014, according to the Asian Development Bank. This growth varies, from 7.7% and 7.5%, in Cambodia and Thailand, respectively, to 3.7% in Singapore.

Trade liberalization is creating new market opportunities in ASEAN countries, but insurers must be cautious about regulatory differences. Twelve new private insurers will enter their first full calendar year of operations in Myanmar in 2014, with large multinational insurers also establishing bases. Now that Cambodia permits foreign market entry, European insurers have established a presence. Insurers are advised to carefully consider their strategic rationale for entering new markets, as it is likely to take considerable effort and time for operations to grow and become profitable.
The more developed ASEAN economies of Singapore, Malaysia, Indonesia and Thailand will continue to attract insurer interest. In Singapore, the Monetary Authority of Singapore (MAS) has stated that it will continue to work with insurers to enhance specialty and reinsurance underwriting and broking capabilities. MAS also will assist insurers to expand their regional hubs and promote growth in emerging business lines like cyber risk insurance. Significant merger and acquisition (M&A) activity in Malaysia has led insurers to begin reinventing their business models. It will be interesting to see how the market reacts to these changes. Similarly, there is high interest in M&A opportunities, organic growth and operational improvements.

In 2014, insurers should identify and develop new market and platform opportunities, consider potential entry points in ASEAN countries or expand further into subregions.

**Develop digital distribution strategies**

Asia-Pacific accounts for 42% of the world’s internet users. Empowered insurance consumers rely on the web to research and buy insurance products. The use of aggregator websites increased 44% and 50% for motor insurance and home insurance, respectively, between July 2012 and April 2013. In India, the market for online life insurance is expected to increase from approximately INR2b in 2013 to INR80b by 2020. And in a recent survey of Japanese customers, 10.5% of respondents chose an online platform as their preferred future service channel, up from 2.9% in 2009.

Online buying trends are increasing insurer competition. Seven Japanese life insurers currently offer direct sales via the internet. In late 2013, as a step toward building a regional internet presence, Lifenet signed an agreement with Kyobo Life Insurance Co. Ltd. to establish an internet-based life insurance joint venture in South Korea. In China, CIRC approved the establishment of a joint venture between a Chinese insurer and two internet companies to sell policies nationwide. Two additional Chinese insurers are working with an e-retailer to sell their insurance products. A major life insurer in Australia decided in 2013 to acquire the remaining 90% of an internet life insurance comparison site to further its online sales growth.
Although technology is changing the way customers engage with insurers, our insurance consumer surveys indicate that personal interactions are still highly regarded. The reasons include the complex nature of insurance products and customers’ continuing need for advice. While digital distribution is growing within Asia-Pacific, insurers in 2014 will continue to rely on agents as the primary sales channel.

To improve customer experience, insurers need to provide more comprehensive support and training to distributors. They also need to better align their administrative systems with distributors’ back offices, streamlining application processing and improving other areas of customer service.

Mobile technology platforms are another prudent investment. Our global survey, Insurance and digital: the time is now, highlighted that Asian insurers are far more likely than their global peers to have mobile strategies for intermediaries. For example, one Japanese insurer in 2013 distributed more than 30,000 Windows-based tablets to its sales force to enhance communication between agents and customers. This helped streamline contract processing and led to a more paperless operation.

**Get ahead of regulatory developments**

As insurance regulations in Asia-Pacific increase in number and complexity, insurers must adopt the principles underlying these regulatory developments, such as solvency management, risk management and customer protection. This is good business practice and should be a part of insurer DNA throughout the organization.

**Solvency requirements**

The rigorous solvency requirements that are unfolding across the region will strengthen the industry’s collective financial stability. For example, Singapore, which is generally considered to have one of the more advanced regulatory schemes in Asia-Pacific, is expected to implement second-generation risk-based capital (RBC) regulations in 2014. Hong Kong, which has traditionally allowed insurers a high degree of freedom, in line with its free-market principles, also is expected to strengthen regulation. New RBC standards are likely to be implemented by 2016 or 2017.
Other countries are moving closer to a three-pillar Solvency II-style approach. For example, China's second generation insurance solvency regulatory regime, which is to be implemented by 2016, follows Solvency II's three pillars of quantitative capital requirements, qualitative controls and reporting/market discipline. Thailand, which introduced RBC recently, is now considering its second generation RBC requirements. And in the emerging markets in the region, countries like Myanmar are just beginning to grant operating licenses to insurers.

Higher capital requirements in several countries in the region, such as Indonesia and Sri Lanka, have compelled smaller, less capitalized insurers to consolidate, fueling the interest of global insurers to acquire these smaller carriers.

Although insurers will need to dedicate more capital and talent resources to comply with the stronger solvency standards in the region, such investments will create stronger insurers and a more financially sound industry.

**Risk management initiatives**

Growing regulatory pressures to improve risk management are being driven by the influence of the International Association of Insurance Supervisors (IAIS) on local regulators. Recognizing the benchmarks set by the Own Risk and Solvency Assessment (ORSA) in Pillar 2 of Solvency II is another factor. Strong risk management is a critical business practice for companies engaged in assuming risk. While some duplication may result from regulators' enterprise risk management (ERM) schemes and insurers' ERM processes, insurers that adopt risk management as a discipline will gain a competitive advantage.

IAIS has introduced a set of practices for ERM, including an ORSA requirement. This framework requires insurers to properly evaluate the amount of capital associated with risk levels. Insurance regulators in Malaysia, Singapore and Australia have introduced ERM standards with an ORSA requirement. In some jurisdictions, regulators have adopted the term internal capital adequacy assessment process (ICAAP), which is common in the banking sector. Both ORSA and ICAAP require the submission of written reports documenting insurer risk and capital profiles.
Insurers that embrace the principles behind ORSA to gain new insights into their risk exposures are in a sound position to identify and pursue a forward-looking approach. This may include changes to product pricing, reinsurance strategies and portfolio management.

**Global systemically important insurers**

In 2013, Ping An was the only Asia-Pacific insurer out of nine globally to be designated as a global systemically important insurer (G-SII) by the G-20 Financial Stability Board. Designation as a G-SII subjects an insurer to heightened group-wide supervision, additional capital requirements, recovery and resolution plans, and increased reporting requirements, all of which add cost. The potential for additional designees in the region is a concern, as is the possibility that the G-SII regulation will be applied at the national level. This trend is evident in the banking sector and has the potential to transcend into insurance.

IAIS has adopted a three-tier structure of insurance supervision, with G-SII requirements at the highest level and insurance core principles (ICPs) at the lowest level. At the intermediate level, IAIS intends to issue further standards for internationally active groups, including capital adequacy standards. These second-tier standards will include many more Asia-Pacific insurers and may also become a benchmark for local capital standards.

**Global accounting standards**

As insurers expand their geographic footprint in the region and seek capital from new sources, the ability to provide financial reports and statements to meet global standards will become a necessity. Identifying and understanding these changes will be difficult for insurers and a diversion from their focus on local or regional growth.

The eventual introduction of International Financial Reporting Standards (IFRS 4 Phase II) will require insurers in Asia-Pacific to report how they plan to implement these new accounting and disclosure changes and comment on how they will impact their...
organizations. In the case of Solvency II, the development of the new accounting standard for insurance contracts has been much delayed. Now that the comment phase for the revised exposure draft of IFRS 4 Phase II has concluded, discussions and negotiation will likely continue for several years before the exposure draft’s key points are finalized. This includes the presentation of premiums in the income statement, treatment of cash flows and the effect of changes in the discount rate used to measure insurance contract liabilities.

**Customer protection**

Insurers in the region are improving operational risk management to achieve higher levels of customer satisfaction. Compared with insurers in other regions, those in Asia-Pacific were ranked relatively low in reputation and confidence in our *Voice of the customer* survey. Agents and insurers pursuing aggressive top-line growth have long been perceived as mis-selling. This was coupled with complaints of poor claims service in the wake of the heavy catastrophe losses in 2011.

Regulators are addressing these concerns by intensifying the focus on customer protection. Examples include Singapore’s implementation of the Financial Advisory Industry Review recommendations, CIRC moving to increase consumer protection and South Korea forming an independent consumer protection agency to monitor claims dispute and sales activities. Other developments include the Insurance Regulatory and Development Authority in India tightening regulations on agent commissions and increasing oversight of policyholder protection, and Malaysia issuing a concept paper considering several reforms, including deregulation in some areas and tightening in others.

Compared with insurers in other regions, those in Asia-Pacific were ranked relatively low in reputation and confidence in our *Voice of the customer* survey.
Implement data analytics for competitive advantage

Big data analytics – the ever-increasing volume of internal data combined with external
data from social media and mobile devices – can help insurers gain a deeper understanding
of customers and related buying trends. Successful insurers in 2014 will apply data
analytics to make more targeted offers to customers in higher-margin segments. Analytics
will also help insurers and bancassurers offering other products to identify cross-selling
opportunities with these same customers.

Insurers leveraging advanced analytics to diagnose customer retention issues and lapse
rates can respond quickly with tactics to remedy these problems. A case in point is an
Australian bank that experienced high lapse rates in its life insurance portfolio. The bank
reduced this incidence by applying analytics to identify patterns, causes and solutions,
guiding a 7% profit improvement within 6 months.

Analytics also can improve the insurer-distributor relationship and underwriting. As
producers capture more data digitally at the point of sale, insurers gain a deeper insight into
the risk characteristics. This more granular view of insured risk attributes and loss costs can
be correlated with premium and loss data to inform pricing platforms and develop better
risk-scoring tools.

Other benefits include the detection of anomalous patterns across an array of variables to
identify claims leakage caused by fraud. The General Insurance Association of Singapore
estimated that the percentage of fraudulent motor claims paid in the country was 20%,
a surprisingly high rate since Singapore is widely believed to be one of the least corrupt
countries globally. Similar or higher rates have been estimated in other countries.

Successful insurers in 2014 will be those that adopt a comprehensive, cross-functional data
analytics strategy across the enterprise, as opposed to more fragmented strategies.
Identify areas for expense reduction

With profit margins under pressure from heated competition and dwindling investment income, insurers in Asia-Pacific must further reduce expenses to preserve profit. The largest expense-reduction gains will be derived from restructuring, process and productivity improvements, outsourcing and offshoring.

The rapid geographic expansion of regional Asia-Pacific insurers has fostered increasingly complex organizational structures and operational models. Companies with multiple profit centers and broad geographic scope often are undermined by redundancy and duplication of efforts. Obviously, more streamlined operations and simpler organizational structures are necessary to improve efficiency. Insurers can accomplish this by taking advantage of regional platforms and hub arrangements and implementing shared services. An example is Generali’s consolidation of operations in several Asian countries into a centrally managed unit. Insurers can also reduce distribution platform costs by combining agency support systems into a single infrastructure and restructuring their bancassurance sales forces.

Moreover, insurers are trimming expenses by implementing straight-through processing to reduce duplicate data entry across functional systems. A recent survey of global insurance IT spending by Celent indicates that Asia-Pacific insurers are implementing IT solutions to increase operational efficiency and are expected to increase their IT spend by 11.5% from 2013 to 2015.

Outsourcing and offshoring also contribute to expense savings. IDC forecasts that the Australian business process outsourcing (BPO) market will grow at a 5-year combined annual growth rate of 6.1%, and new offshoring options have emerged in the Philippines and China. Insurers that recommend and implement a business case for outsourcing or a shared services delivery model can achieve targeted cost reductions.

Conclusion

In 2014, the forces of change and the challenges and opportunities they create will require insurers to determine how to achieve profitable growth and best position their organizations to remain viable. Insurers will need to rapidly execute decisions and refine strategies to pursue the many opportunities in Asia-Pacific.
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