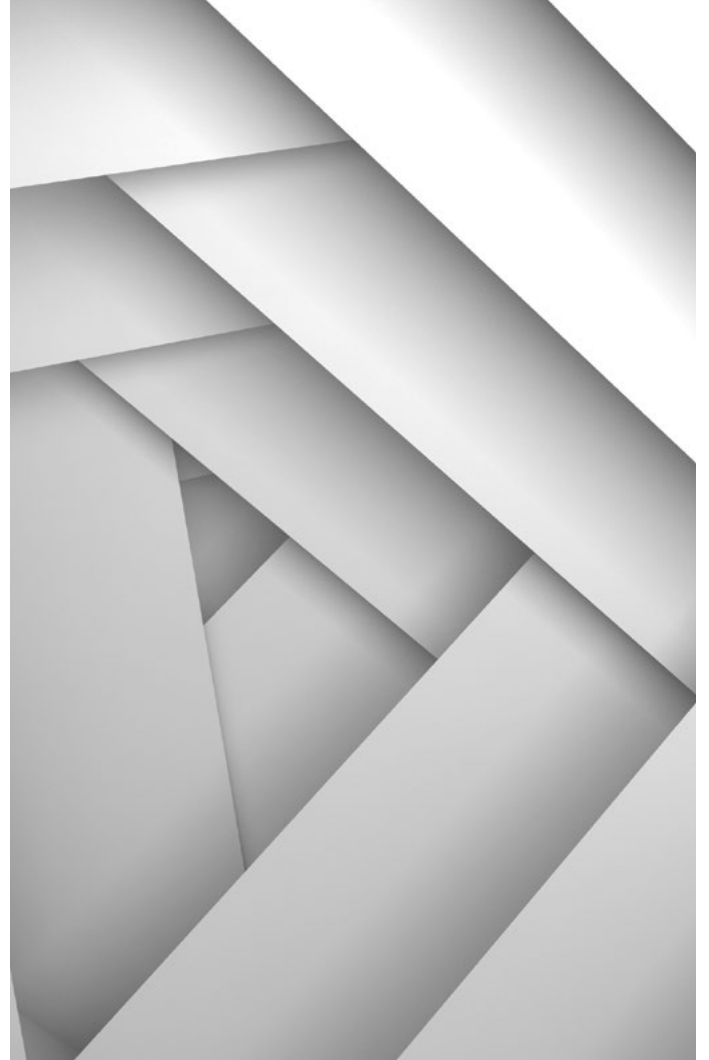


**2017  
Latin American  
insurance  
outlook**

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# 2017: a time of market transition



Despite the dramatic economic downturn in Latin America in the past three years, insurers in the region have remained profitable and are poised for growth. The success in this sector has been historically tied to high interest rates, rising disposable incomes and growing market penetration. While there are sharp regional variations in economic conditions and demand for insurance products, one common dominator is an underserved market in both the personal and commercial space.

The economic malaise of the past three years is expected to lift in Brazil, which represents about half of the insurance market in the region. A rise in disposable income will encourage consumers to insure more cars and homes and invest in life and health products, providing a boost to insurance markets. At the same time, new infrastructure and energy projects expected in some countries will bolster demand for commercial products. But with insurance growth tied to economic and financial performance, any trade and fiscal policy shifts under a Trump Administration could ultimately have negative consequences for personal and commercial insurance.

Against this backdrop, insurers will accelerate digital transformation to drive efficiencies, attract tech-savvy consumers and expand market reach. Regulatory reform will move at a different pace across the region, setting a new insurance compliance agenda around capital adequacy, cyber risk and InsurTech. Many insurers are already improving their ERM systems in anticipation of more stringent reporting and control requirements.

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## Fighting for economic renewal

Over the past few years, recessionary conditions have weighed heavily on key markets, particularly Brazil, Argentina and Venezuela. However, the regional economic downturn is expected to reverse in 2017, with the IMF forecasting GDP growth of 1.6%. A turnaround in commodity prices on both fuel and non-fuel products will help drive that recovery. However, some analysts, such as S&P, believe that economic growth in the years ahead will depend on the ability of key markets, such as Brazil, to address their economic imbalances and increase their investments in infrastructure.

The insurance sector has weathered the economic storm in the region relatively well, although premium growth has varied widely across countries. For example, premium growth in Argentina has risen sharply over the years, increasing by 41% between 2014 and 2015, due mainly to inflation. In contrast, slowing auto-insurance sales and increasing unemployment in Brazil have caused premium growth to fall between 2014 and 2016, from 11% to an estimated 10.3%. With its economy in crisis, Venezuela's premiums dropped by more than 25% in 2015, and they will likely fall further because of lingering economic and political concerns.

In 2017, Munich Re Economic Research expects real growth in life premiums to rise by just over 5% for the region, and property and casualty (P&C) premiums to increase by about half that rate, to just over 2.5%. Improving fundamentals in some countries, including subsiding inflation, rising income levels and stabilizing credit markets, will boost demand for home, car and commercial insurance. The demand for health insurance and pension products will also grow. Declining interest rates will dictate the profitability for insurers, particularly those offering annuity products.

But a US policy shift under a Trump Administration could undermine the region's economic rebound. A loosening fiscal stance in the US, combined with rising local interest rates, could limit the ability for Brazil, Argentina, Colombia and other countries to facilitate growth through looser monetary policies.

Meanwhile, the possible unwinding of NAFTA and the Trans-Pacific Partnership (TPP) would not only hurt Mexico but other countries that are dependent on US trade, such as Colombia, Chile and Venezuela. As a sign of what may lie ahead, the Mexican peso lost 15% of its value immediately after the US election.

Historically, high-growth potential has attracted global insurers, reinsurers and brokers to the region through M&A. With economic conditions likely to improve, international players may reinforce their positions, particularly in key markets such as Brazil. In 2017, Aon will be acquiring Brazilian health and benefits brokerage Admix, which has more than 1.4 million beneficiaries across 6,700 companies and places roughly BRL 2 billion in health and benefits premiums each year. Stricter capital requirements in the region could also trigger acquisition and consolidation to improve the financial position of smaller insurance firms.

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**“We are optimistic about the insurance business in 2017. A pickup in oil prices should help the economy, and firming currencies could drive stronger car sales. And a long-awaited turnaround in Brazil could boost other markets in the region.”**

Edgar Sanchez, Managing Director, Ernst & Young LLP

The impact of a new Trump Administration on local growth and market stability could influence the M&A environment. Global insurers, reinsurers and insurance brokers may hold off on investment plans until the direction of US policy becomes clearer.

### The M&A landscape

- ▶ There have been more than US\$12 billion in M&A transactions and more than 57 deals since 2011.
- ▶ In 2011, Zurich acquired a 51% stake in the Latin American operations of Santander for a total consideration of US\$1.67 billion as part of a 25-year strategic distribution agreement.
- ▶ In 2014, ACE signed an agreement to acquire Itaú Seguros Solucoes Corporativas from Itaú Unibanco Holding for US\$686 million, making ACE the largest commercial P&C insurer in Latin America.
- ▶ In 2015, AXA acquired SulAmérica large risks business for €40 million. The acquisition will fuel AXA's expansion in the Brazilian market and increase its growth prospects.
- ▶ In 2016, AON announced a deal to acquire Admix in order to build its position in the growing private health insurance market.

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## The changing regulatory landscape

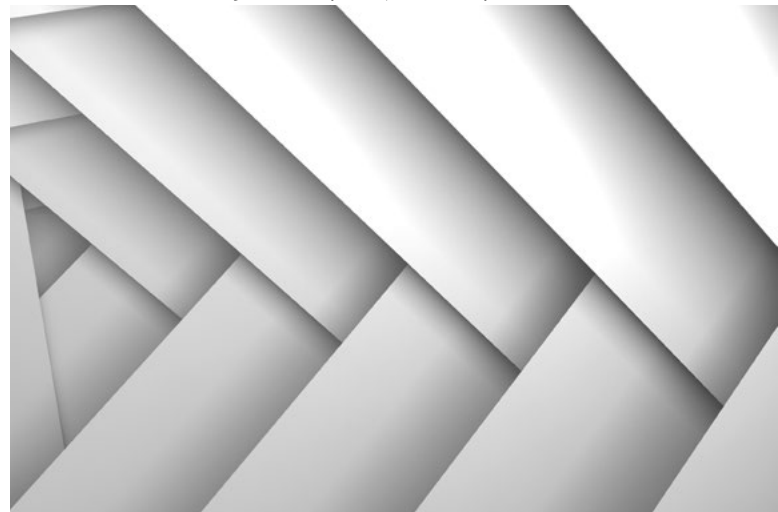
The Latin American regulatory landscape is diverse and progressively changing in line with international guidelines around solvency and other insurance issues. Risk-based capital rules are still evolving in many countries, as are regulations around cybersecurity and Insurtech. Mexico was the first country in Latin America to adopt a framework modeled after Solvency II, setting a standard for other economies to follow.

In Brazil, the European Commission granted provisional Solvency II equivalence for 10 years, effective from 1 January 2016. The Superintendência de Seguros Privados (SUSEP) is expected to regulate the Own Risk and Solvency Assessment (ORSA) fully in 2017, making it effective by 2019. This represents a major transformation of how insurance companies will operate, including a requirement for forward-looking solvency assessments and business decisions tailored to risk-taking choices. SUSEP is also considering new adjustments for eligible capital, including a liability adequacy test, mark-to-market asset valuations and tax adjustments. The aim is to avoid differences in the accounting valuation of the same assets (held-to-maturity, held-for-trading or fair value) that may result in an incorrect calculation of an insurance company's solvency or risk-taking capacity.

Chile is currently developing a risk-based capital approach modeled after Solvency II, which is still pending approval. Regulators in the country have already approved the ORSA, which companies will need to comply with next year. Similarly, Colombia is moving toward the more risk and economic value-based ComFrame, and significant tax reform is on the deck for January 2017. Peru, Uruguay and Argentina are taking a wait-and-see approach to implementing a risk-based capital system. While many rules are tightening in the region, insurance regulators in Argentina are considering giving more freedom to firms doing business with foreign reinsurers and are also working to eliminate rules requiring insurers to invest in specific instruments.

Meanwhile, legislative actions to improve cybersecurity have emerged across the region, either in the form of wide-sweeping rules on data privacy rights or as specific laws and codes of corporate conduct. Argentina, for example, has constructed a comprehensive legal framework for information and communications technology, including Law 25.326 on data protection. As digital access grows and cyber criminals expand their attacks through interconnected technology, cybersecurity will move up the regulatory agenda.

For insurers in the region, cybersecurity is more than a regulatory challenge; it is likely to evolve into a new line of business over time. Latin America faces cybercrime losses estimated at US\$90 billion a year, according to the Inter-American Development Bank. Yet four out of five countries do not have cybersecurity protection plans in place. Because of stricter regulations and high levels of exposure, financial institutions are among the early adopters of cyber insurance.



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## Tapping an underserved market

Although insurance growth is relatively high in Latin America, most of the population is still uninsured. Insurance accounts for less than 3% of GDP in countries such as Mexico and Colombia. It is only moderately higher in Brazil and Chile.

Low penetration rates are a result of several factors. First, most of the population is low-income and unbanked, and not yet viable consumers of insurance products. Second, while the middle class is growing, many of these potential customers are still accumulating household assets and do not see the value of insurance. Finally, distributing and selling products at an affordable price point has been challenging.

But all this is beginning to change. Indeed, almost half of insurers not currently serving the low-income market are planning to offer mass-market products, while 33% plan to offer microinsurance, according to the Microinsurance Network, an industry group. Bancassurance is providing the greatest access to microinsurance to date. As most insurance products are purchased through financial institutions, bringing people into the financial system is ultimately the key to increasing insurance penetration. At the same time, firms are developing third-party distribution models to connect with individuals who are neither financially connected to the banking system nor digitally connected. These include small brokers and banking correspondents.

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**“It is more than an insurance gap – it is a social gap. Many people are uninsured. Their cars are uninsured. They don’t have life insurance or even a patient plan.”**

Duarte Carvalho, Insurance Advisory Leader,  
Ernst & Young LLP

Insurers in Latin America are taking different paths to digital transformation, sometimes simultaneously. Many firms are using technology to reinvent their end-to-end activities – from customer interaction to back-office operations. By doing things faster, smarter and cheaper, they can provide customers with more affordable products suited to their needs. More forward-looking insurers are thinking beyond their legacy systems to drive business model innovation through greenfield projects or Insurtech linkups. For example, in Brazil, Bidu enables consumers to compare and purchase insurance online, and Seguro Auto Jovem is targeting the 18- to 24-year-old demographic, allowing drivers to track their behavior using a mobile app. With 70% of consumers now using mobile phones, insurers can also use digital technology to reach a broader market at a more affordable cost.

As insurers go digital, the talent gap in the Latin American insurance industry will widen. Insurance providers are actively seeking specialized skills in a range of areas, from digital marketing to risk modeling. Insurers also need to develop familiarity with the latest technologies, such as artificial intelligence, cybersecurity, telematics and the internet of things. However, low enrollment in technical-degree programs has been a problem in Latin America. As a result, insurers may defer digital plans or look outside their organizations for technical support.

Although the upside potential of the underserved market is enormous, it will take time to develop. In the short term, technology will not be enough to overcome economic dislocations and financial exclusion in key markets. In addition, the power of agents and brokers, and the lack of underlying information and customer transparency, could slow the development of Insurtech solutions.



## Impact of external factors on the Latin American insurance market in 2017

(1 = low impact, 10 = high impact)

<b>9</b>	<b>Economy</b>	Latin America is poised for an economic recovery, with premium growth outpacing advanced markets. But if the new Trump Administration acts to unwind trade agreements, the economic impact on Mexico and other export-led markets could be significant.
<b>8</b>	<b>Technology</b>	With most people now using mobile phones, digital technology will become an increasingly important way to reach customers. Insurers will also use technology to reinvent their processes, products and business models. Insurtech may provide a solution for the uninsured market.
<b>7</b>	<b>Customer expectations</b>	Efficiency, innovation and customer education are critical for succeeding in a region where consumers are uninsured. Digital access, mass market and microinsurance products, hybrid distribution channels and new business models will be key for meeting evolving customer needs.
<b>7</b>	<b>Regulation</b>	Risk-based capital regulations are still evolving in many countries, from Mexico and Brazil to Chile and Colombia. With digital access growing and threats increasing, data privacy and cybersecurity regulations will become more prevalent in the future.
<b>7</b>	<b>Talent</b>	To deliver on digital initiatives, insurers will need to attract data scientists, cyber-risk specialists and other digital professionals. But the lack of trained technical professionals will widen the talent gap for insurers, which may need to look outside their organization for support.
<b>6</b>	<b>Competition and M&amp;A</b>	Improving economic conditions and tighter capital requirements should buoy global and interregional M&A activity and partnerships, and lead to greater consolidation. The rise of Insurtech and microinsurance products will increase price competition.
<b>5</b>	<b>Cyber risks</b>	Insurers will be more vulnerable to cyber risk as they rely on digital technologies, such as wearable devices, telematics and cloud platforms. At the same time, cyber risk insurance will be a dynamic business line for commercial insurers.

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# Strategic road map for 2017



With continued disruption expected in the Latin American insurance market, companies will want to revisit their strategic plans in 2017. Over the next 5-10 years, the interplay of demographic, economic and technology trends will transform the insurance sector in Latin America. Preparing for these shifts now will be essential for future success.

- 1 Take customer centricity to the next level
- 2 Keep a close watch on emerging regulations
- 3 Put cybersecurity high on the corporate agenda
- 4 Use the latest technologies to drive performance
- 5 Rethink strategies to attract, develop and retain talent

# 1

## Take customer centricity to the next level

**Integrate systems to understand your customer fully.** In 2017, insurers should continue to draw on technology to integrate all customer, account and policy information to facilitate a true customer-centric approach. By pulling together scattered data, insurance teams will have access to data-driven insight across sales, underwriting and servicing operations to drive upselling opportunities. These new digital approaches will lay the foundation for other customer priorities: shifting from a product to customer approach and offering a seamless omni-channel experience.

**Use innovation to penetrate the mass market of uninsured consumers.** In 2017, insurers will also take greater steps to tap into the uninsured market beyond the bottom of the pyramid – the emerging middle market. While this is a longer-term strategy that will require greater customer education, insurers will draw increasingly on technology, product innovation and new business models to tap this underserved market. Jesus Palacios, Director of Financial Institution Ratings at S&P, cites an example in Mexico, where less than one-third of cars are insured. “Government efforts to make auto insurance mandatory will help. But the real issue is how you design, price and distribute products to meet customer needs.” Outside the personal sector, EY’s Carvalho believes insurers should also explore underserved commercial customer niches, such as small and medium enterprises (SMEs).

“In Mexico and Central America, we have a really big problem with service at the most basic level. Now, there are only three points of contact with the client – when you buy, when you bill, when you have a claim. The solution is greater contact through digital and other communication channels.”

Rodrigo Aburto, Financial Advisory Services,  
Ernst & Young LLP

“In markets like Brazil, insurance firms provide a full suite of products, including life, pension, P&C, residential and health. But insurers still average only around 1.3 to 1.5 products per person. If you are doing your cross-selling properly, you should have double or triple that number.”

Duarte Carvalho, Insurance Advisory Leader,  
Ernst & Young LLP

**Develop a blended high-tech, high-touch approach.** Latin American insurers will continue to leverage a variety of distribution channels, including bancassurance and banking correspondents; digital, broker and retail models; partnerships and affinity models; and direct telemarketing sales. But most insurance is still purchased through traditional face-to-face channels through a broker or a bank, making it difficult to build direct customer relationships. “Most insurers in Latin America don’t have a relationship with the customer,” explains Carvalho. “The broker or the bank has the relationship. That’s the main challenge for insurance companies – to actually engage with the customer directly without creating a major conflict with a distribution channel.” To overcome this barrier – and better serve customers who still do not fully understand insurance – insurers should explore hybrid approaches that blend digital access with traditional personal service. In 2017, Sanchez believes insurers will invest more in building customer engagement and product awareness through social media and other digital methods.

# 2

## Keep a close watch on emerging regulations

**Monitor and prepare for tighter regulations.** To cope with a growing maze of capital, data security and consumer protection regulations, insurers will need to develop well-honed systems for monitoring and assessing regulatory changes. Insurers should consider what emerging regulations will mean for costs, resources, skill requirements and business strategies. Having a fully trained compliance team that has familiarity with advanced analytical and cybersecurity testing techniques will be essential. Because of the far-reaching impact of these regulations, these teams should be involved in both operational and strategic decisions. Collaborating with governments, regulatory organizations and other financial institutions will also be important for achieving a more consistent insurance regulatory framework across the region.

**Sharpen your focus on risk management.** With risk-based capital requirements on the rise in Latin America, and continued market volatility on the horizon, insurers will need to embed risk management into their organizational culture. This should include linking agent and broker incentives to risk and loss results, and assessing what structural economic and market changes may mean for your business. Emerging regulations will put new pressure on domestic insurers to implement robust corporate governance, risk and compliance systems, and synchronize their three lines of defense with business operations, oversight teams and independent auditors. To comply with stress testing requirements and cope with future market shocks, insurers will also need to develop more sophisticated tools to conduct scenario and predictive analysis and build greater resiliency into risk management strategies.



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**“Insurers should be aware that regulators are also going to access newer technologies to control and scrutinize insurance transactions better. Insurers need to be able to provide the information regulators are asking for in an efficient way.”**

Alejandro De Navarrete, Insurance and Real Estate Sector Leader, Ernst & Young LLP

# 3

## Put cybersecurity high on the corporate agenda

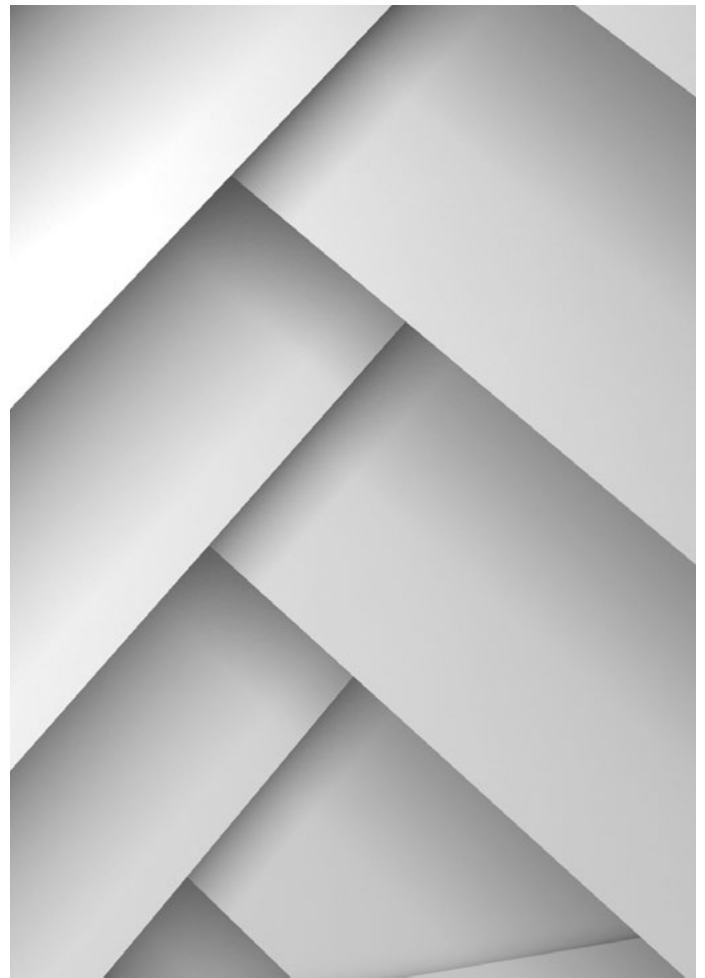
**Develop a best-of-breed cybersecurity strategy.** Cybercrime has become increasingly expensive. According to Febraban, the Brazilian Banking Federation, it now accounts for 95% of losses for Brazilian banks. At the same time, regulators across the regions are developing more stringent regulations around the protection of personal information. As insurers advance their digital agendas, understanding the evolving cybersecurity landscape and building cybersecurity into a core competency will be essential. One element should involve a comprehensive review of a data governance framework and ongoing assessments of security risks across multiple channel touch points, including third-party distributors. Says EY's Cavalho, "Best practice leaders are doing penetration testing, attack simulations and predictive analysis to achieve swift response times to cyber attacks." While cybersecurity may eventually open up new product opportunity for insurers, S&P's Palacios believes that local companies, at least for now, will prefer to invest in their own protection systems.

**Be aware of the ever-changing digital risks.** New and ever more dangerous, and costly, cybersecurity risks are emerging every year. Evaluating these risks will be important to verify data privacy, reduce cybercrime costs and avoid reputational damage. Cyber criminals are increasingly attacking enterprises through the less secure home systems of their employees. With the proliferation of smart devices, insurers will also need to educate their workforce and customers on data privacy and cybersecurity leading practices. At the same time, they will need to pay attention to the use of interconnected technologies that can expose their enterprise and products to greater cyber risks. Cloud platforms, telematics, wearables, mobile apps and the internet of things are just some of those technologies. And evolving technology and cybercrime techniques make protection a moving target.

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**"Are insurers covering all their cyber risks? Probably not. One area of weakness is exchanging data across distributions channels that are not proprietary. One of the biggest risks is that you may have cyber attacks, not on your base, but on your partner's base."**

Duarte Carvalho, Insurance Advisory Leader,  
Ernst & Young LLP



# 4

## Use the latest technologies to drive performance

**Build greater agility and efficiency by upgrading legacy systems.** One of the key challenges for insurers is the pressure on margins from high distribution costs, outdated legacy systems, low productivity and growing incidences of fraud. In 2017, insurers will accelerate the digitization of their end-to-end operations, from underwriting and policy administration to billing and claims management. At the same time, insurers will gain greater control over internal and external data across their enterprise and upgrade their analytical capabilities for leveraging that data. These steps will not only reduce costs, they will support go-to-market strategies, enable product innovation and facilitate the future use of smart automation. This transformation will take significant investment for many insurers, since their current technology platforms are not scalable.

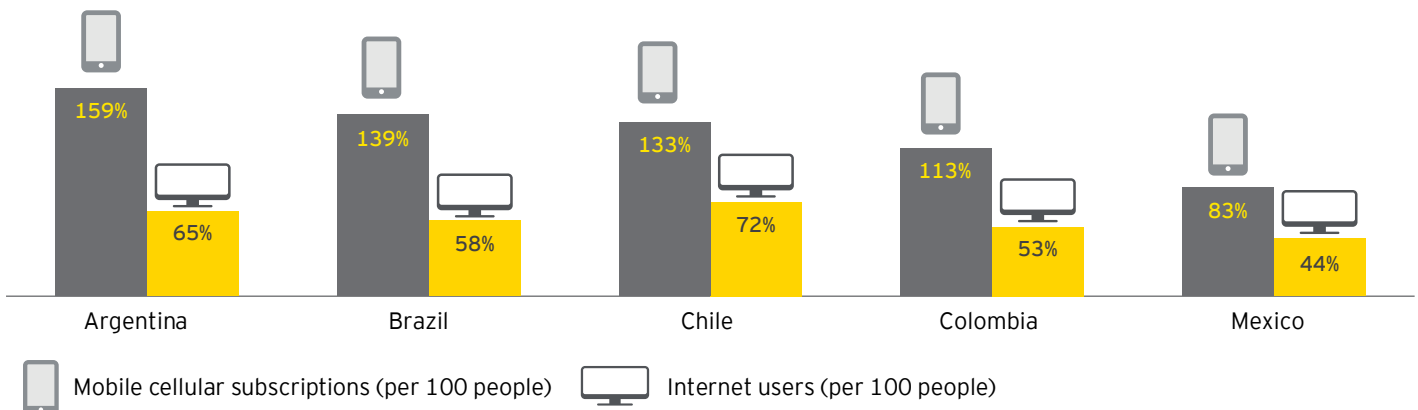
**Reinvent business strategies and models through digital transformation.** Insurers in Latin America are starting to turn to technology to reinvent how they sell and distribute products. This move to technology-enabled business model innovation will grow tremendously over the next few years as financial institutions invest heavily in digital distribution. "In Brazil, at least two of the largest insurance groups are setting up digital business models, completely apart from the legacy ones," says EY's Carvalho. "One

of those new Insurtech companies, Youse, was launched in May by Caixa Seguradora. It is now offering residential, automobile and life insurance direct to customers through online and mobile access, and will add other products in 2017." Insurers should monitor emerging Insurtech products and business models next year and be ready to invest in those approaches that show the most promise.

**“ Legacy systems of many insurance companies, particularly in Mexico and Central America, are not equipped to meet basic reporting requirements. It will take much more than a Band Aid solution to build the type of systems necessary to meet the reporting requirements of Solvency II.”**

Rodrigo Aburto, Financial Advisory Services, Ernst & Young LLP

The varying use of digital technology across Latin America



Source: World Bank.

# 5

## Rethink strategies to attract, develop and retain talent

**Have a clear view of the future of work.** Attracting and retaining specialized talent will be critical for Latin American insurers as they explore the application of new digital technologies, address new market risks and opportunities, and come to grips with rising regulatory pressures. 2017 will be a good time to take a hard look at future work needs in a time of market transformation. In-house knowledge will be required in many aspects of technology, direct online marketing, risk management, compliance, data analytics and cybersecurity. Having a strategic view on the future of work, and which tasks will be done by machines or people, will be important not just for assessing talent requirements, but also for improving the future job satisfaction of your staff.

**Develop a strategy for filling talent gaps.** Assessing your future talent gaps will require a full appraisal of retirement trends, automation plans and new business demands. Matching retirement cycles with automation plans can be a good way to avoid employee disruption. Tapping talent from other sectors, such as banking, technology or consumer markets, can also help fill talent gaps and provide a cross-pollination of fresh ideas. "In Brazil, we clearly had a talent gap," says Carvalho, "But then an interesting phenomenon appeared. The banks downsized their operations, and a lot of well-trained executives that had been working with the banks started to move over to insurance companies." No matter how insurers fill their talent gap, developing internal programs to support the professional development of employees and provide them with the skills for the future will be a top strategic priority.

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**"You have good people, but not enough people. You also have a gap in everything that is related to the customer experience, from customer engagement skills to product design. These skills will need to be developed over the next few years."**

Duarte Carvalho, Insurance Advisory Leader,  
Ernst & Young LLP



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