Investment Performance, Guaranteed Products and Regulation are main worries for Luxembourg Insurers.
About the survey

The CSFI’s latest Insurance Banana Skins 2019 survey, conducted in association with PwC, interviewed 927 practitioners, regulators and observers of the insurance industry across 53 territories. It aims to understand what insurance stakeholders see as the biggest industry threats over the next two or three years and their order of significance. A record number of participants from Luxembourg contributed this year.
The 2019 edition of our survey charting the top risks in the global insurance sector highlighted Investment Performance, Guaranteed Products and Regulation as the three biggest concerns for insurers in Luxembourg.
The biggest concerns of Luxembourg insurers

Luxembourg insurers (1) listed Investment Performance, Guaranteed Products and Regulation as their top three concerns. These differ markedly from the rest of the world’s insurers who listed Technology, Cyber Risk and Change Management.

“Contrasting views of key concerns for Luxembourg players compared to global respondents (2) is not totally surprising,” commented Matt Moran, Insurance Industry Leader at PwC Luxembourg. This relates in part to the specifics of the Luxembourg insurance market but also reflects that other territories have needed to embark on more radical transformation earlier in the cycle.

“The weight of wealth-insurer activity, which colours the Luxembourg survey with the challenge of providing Guaranteed Solutions in the seemingly never-ending low interest rate environment, coupled with Investment Performance, rank as top concerns.”

Technology appeared for the first time in 2017 and moved from number three to the top spot in the global survey. However, whilst just number 6 in Luxembourg, Mr Moran believes the trajectory of this concern will continue to rise locally.

“The need to enrich client experience, including digital transformation, and also to reduce the “cost-to-serve”, points Luxembourg insurers towards further investment in technology,” he said. The level of participation in the survey was unprecedented with 27 stakeholders from the Luxembourg insurance market providing their input. Mr Moran thanked those who took part and predicted that the survey outcome would evolve further. “With so many global and international tier one non-life market players establishing EU headquarters in Luxembourg over the past 24 months, the Luxembourg ecosystem is expanding significantly,” he added.
The Insurance Banana Skins is usually proven to be a valuable tool to capture anticipatively the relevant industry risks.

The fact that global and local perceptions on some risks like Climate Technology and particularly Human Talent differ, then, is surprising. It’s worth mentioning that the latter has been identified as a key topic in Luxembourg, regardless of the industry. This divergence could mean that Luxembourg insurers are overlooking these risks, or that they are comfortable with their plan to address them.

To Carlos Montalvo Rebuelta, PwC Partner and EMEA Insurance Regulatory Leader, (formerly Executive Director of EIOPA, the European Insurance and Occupational Pensions Authority), the overall take-away of the contrast is that the top one, two and three items — Investment Performance, Guaranteed Products and Regulation — are related to each other in that they represent risks vis-a-vis the Luxembourg insurers’ business model. It is about current model priorities or shorter-term thinking i.e. “How can the industry generate revenue today”, rather than, “How can the industry generate revenue tomorrow”.

“Points one-three are closely interlinked, i.e. investment performance gets more attention than the top three global banana skins, technology, cyber risk and change management,” Carlos Montalvo Rebuelta adds.

Anthony Dault, Insurance Partner, PwC Luxembourg, suggests that this goes some way to explaining why cyber risk is only listed at ten and is actually down two places in Luxembourg. “The thinking may be that any concern over cybersecurity is moot if insurers think they may be going out of business anyway as they cannot deliver.” Or, “Who’s going to attack me if my business is gone?”

In summary, what Luxembourg insurers are expressing is their worry about investment performance. In this there is truth: if they don’t do well, they may eventually be out of business.

“Investment performance is the number one thing that is keeping Luxembourg insurers up at night,” says Carlos Montalvo Rebuelta. “Why? Because margins are narrowing within a negative interest rate environment. It’s harder to make money. That means you need to take on more risk (market and conduct) to be active and profitable with the products you are selling. That is the biggest difference between Luxembourg and global. For example, investment performance is only listed as risk five on the global survey.”

“Conduct risk embedded with the current macroeconomic conditions, now that is something new that I find this interesting,” Carlos adds. “Why? Because not all new products developed under the current scenario can add value to clients. But then the question remains, what are the right products for clients in this type of environment?”
Non adaptation to social change is a risk

Social change as a risk is ranked relatively low, not only on the Luxembourg insurers’ list (20) but also on the global insurers’ list (18). This is somewhat of a red flag.

“Quite frankly, we don't see a sense of urgency on this topic from the big players and this while pressure from social change is a fact. This means Luxembourg insurers are thinking of their today priority-client but not necessarily of the client of tomorrow,” says Carlos Montalvo Rubelta.

It comes down to the basic idea that whatever took an insurance business to where it is now, will not take it to the next step. There is a risk of not thinking of new ways to do business that ponder and consider demands linked to social change and behaviors shifting at a rapid pace.

Carlos Montalvo Rebuelta says, “What I see in the industry is that topics around social change are amongst the biggest drivers affecting how we do business. People’s expectations (clients) have changed a lot. The new normal is changing. People want things easily and instantly.”

Due to social change, people are less docile when they feel unsatisfied. To that, we need to add the urgency variable that is taking over life in general. For instance, we need to look at the influence of Amazon with its 24h delivery, which is becoming the new standard. Instant gratification, positive user experience, ease of procedure, these are what people want more and more.

By placing too much concern on points one, two and three, Luxembourg insurers are anchored in the now, ignoring the longer-term risk of social change impacts and the things that will attract future clients. Insurers (in fact companies in most industries) need to come up with a new model of competitiveness.

This will require new commerce and a cheaper and better product offer. These are real risks, and if the giants in the industry don’t move, they could become obsolete.

In addition, some risks such as cyber, sustainability and climate change among others, which only a short time ago were labelled as emerging, can no longer be seen that way, because they are becoming an integrated part of business, and this will also force change. The changing expectations of clients is a big potential banana skin fundamentally going forward. The key is to ask which one of these areas represents an opportunity instead of a risk.

Fairer conditions needed to attract and grow portfolios

With the old insurance model, what we will see in terms of product development is a 15 to 20% rise in insurance costs using an old portfolio because it has subsidised the purchase of a new one. Or in a nutshell, legacy clients are paying higher rates in order to substitute the lower rates needed to attract new clients. However, insurers need to offer these better conditions for new clients to keep growing portfolio. The question of unfair treatment is then raised as well as pressure from supervisory and regulatory constraints. The clear warning is that
change is coming. What will the impact be on business models? How will the way business is conducted change?

At the same time that social change is being underestimated, another big dependant factor for how insurers will do business going forward is long-term investment.

Regulation

“In respect of regulation (three) and political risk (five),” says Anthony Dault, “it should not be surprising that Luxembourg insurers continue to put these at the forefront, and not particularly in respect of the costs associated (the biggest Directives and regulations have now been processed in national legislation). However, we are in tumultuous times today, where the Freedom of Services framework (a pillar of the EU market) is being strongly “challenged” in various locations, and with a trend for certain countries to fold in on themselves and protect their national champions. This is definitely a big challenge for Luxembourg insurers and one that requires unity at all levels and beyond the mere local industry, but it has to be said that there is a strong component of dynamism in the way that Luxembourg insurers conduct their business.”

Reputation is linked to delivering on promises

Reputation is listed as 21 on the Luxembourg insurers’ risk list yet much higher at 13 on the global list. As said previously, when analysing banana skins, it is interesting to look at risks that can be turned into opportunities, and there is potential here. For example, reputation (quality service which leads to enhanced trust) represents a potential opportunity for Luxembourg today versus the giants who are adopting the Amazonisation approach. If and when newcomers enter the market with lower pricing, they may not offer the same quality service (reputation), giving Luxembourg insurers a differentiator — quality.

“I like to see the opportunity side of every risk. When I see how low reputation is on the list I wonder if Luxembourg industries are on the safe side of the risk or are not preparing via services and branding for the competition that is coming.” Carlos Montalvo Rebuelta

Finally, some other take-aways from the Luxembourg banana skins’s responses worth noting.

The risks listed as four, eight and 18 — Change management, Human talent and Quality of management — are the insurers expressing, “We have to adapt or we are in trouble.”

In fact Human talent is listed as risk eight on both the Luxembourg and the global insurers’ list. There is a growing difficulty to attract people, partly because insurance is perceived as conservative and old fashioned — not sexy! This is a risk in an age characterised by human capital wars and rapidly changing career landscapes that require rapidly-changing skill sets. Insurance is as old as business itself but this does not necessarily attract fresh young talent.
## Luxembourg Insurance Banana Skins 2019
(versus Luxembourg 2017 survey)

1. Investment Performance (up 2)
2. Guaranteed Products (no movement)
3. Regulation (up 2)
4. Change Management (no movement)
5. Political Risk (used to be political interference?)
6. Technology (down 1)
7. Interest Rates (down 6)
8. Human Talent (down 1)
9. Macro-economy (up 6)
10. Cyber risk (down 2)
11. Climate change (new)
12. Cost reduction (up 1)
13. Credit Risk (new)
14. Brexit (up 8)
15. Business Practices (up 4)
16. Competition (down 3)
17. Corporate Governance (up 1)
18. Quality of management (down 9)
19. Capital availability (up 1)
20. Social change (down 1)
21. Reputation (down 5)

## Luxembourg Insurance Banana Skins 2019
(versus World Banana skins 2019)

1. Investment Performance (world is 5)
2. Guaranteed Products (world is 14)
3. Regulation (world is 6)
4. Change Management (no movement)
5. Political Risk (world is 11)
6. Technology (world is 1)
7. Interest Rates (world is 10)
8. Human Talent (world is also 8)
9. Macro-economy (world is also 9)
10. Cyber risk (world is 2)
11. Climate change (world is 6)
12. Cost reduction (world is also 12)
13. Credit Risk (world is 17)
14. Brexit (world is 21)
15. Business Practices (world is also 15)
16. Competition (world is 7)
17. Corporate Governance (world is 19)
18. Quality of management (world is 16)
19. Capital availability (world is 20)
20. Social change (world is 18)
21. Reputation (world is 13)

Off the top 21 list is Quality of Risk Management (was 14 in 2017), Product development (was 17 in 2019) complex instruments (was 21 in 2019).
Top 5 Risks by Sector and by Region

**Life**
1. Technology
2. Investment performance
3. Regulation
4. Cyber risk
5. Change management

**Brokers/Intermediaries**
1. Cyber risk
2. Change management
3. Human talent
4. Technology
5. Climate change

**Non-Life**
1. Technology
2. Cyber risk
3. Climate change
4. Change management
5. Regulation

**Composites**
1. Cyber risk
2. Technology
3. Change management
4. Regulation
5. Investment performance

**Asia Pacific & Europe**
1. Technology
2. Cyber risk
3. Climate change
4. Change management
5. Investment performance

**Reinsurance**
1. Cyber risk
2. Climate change
3. Technology
4. Investment performance
5. Regulation

**North America**
1. Technology
2. Cyber risk
3. Change management
4. Human talent
5. Regulation

**Latin America**
1. Technology
2. Change management
3. Cyber risk
4. Climate change
5. Competition
Your contacts

Matt Moran
Insurance Leader, PwC Luxembourg
+352 49 48 48 2071
matt.moran@lu.pwc.com

Anthony Dault
Insurance Partner, PwC Luxembourg
+352 49 48 48 2380
a.dault@lu.pwc.com