2016 EY Canadian property and casualty insurance outlook
Market summary

For Canadian property and casualty (P&C) insurers, 2016 will be a time of uncertainty and change. On the one hand, the sharing economy and regulatory headwinds will continue to disrupt the industry over the next 12 months. On the other hand, consolidation and changing customer expectations will lead to innovation in how insurers conduct their business.

Weak macroeconomic fundamentals

Sluggish economic growth, continued decline in the Canadian dollar and a weakness in the oil and gas industry are having an impact on most sectors, including financial services and insurance. Interest rates will likely remain low in an effort to spur investment and growth, even as markets remain volatile. This is in sharp contrast to the US situation, where the economy has rebounded and interest rates have risen.

Consolidation and intense competition

Multiple factors influence the ultra-competitive nature of the Canadian P&C sector. Consolidation is expected to continue. For example, Aviva Canada’s acquisition of RBC General Insurance earlier this year shows that leading Canadian insurers will not relent in their quest for growth and an improved competitive position. Aviva said the transaction would increase its gross premiums written in Canada by approximately C$800 million. Last year, Aviva Canada was tied for second place with Desjardins Group in market share rankings compiled by MSA Research based on 2014 direct premiums written and presented on a pro forma basis.

Recent acquisitions have also underlined that insurers are looking to add to their distribution channel mix, with the goal being an omni-channel approach to optimize growth and meet customer demands. The net result is that smaller insurers will have a hard time competing and are forced to take on cost containment initiatives to compete against the size advantage of leading insurers. Examples of cost containment strategies include system upgrades, process automation, offshoring and claims strategic sourcing. The other option remains focusing on niche markets.

Legislation is now in place in Canada for demutualization. But it is currently unclear if this will lead to accelerating competition in the market.
Customer expectations rising
Commercial lines: Commercial customers will continue to require more sophisticated insurance solutions in 2016. This includes coverage and product enhancements for:

- Cybersecurity
- The sharing economy
- New technologies like drones and telematics/sensor-based technologies
- Errors and omissions
- Simplified insurance and integrated digital attributes for small and medium-sized commercial insurance

Personal lines: Tech-savvy Canadian consumers will continue to push for new insurance channels, products 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. Customer expectations are being influenced by what is going on in other sectors.

Insurers continue to implement customer analytics for both personal and commercial lines to better understand customer expectations and respond to these evolving expectations. Insurers are beginning to change their focus from a product focus to a customer-centric focus on multiple levels: business model, operating model, organizational culture, processes/systems and data warehouses that allow for this change in focus.

Accounting uncertainty and regulatory change
Regulatory and accounting changes continue to challenge insurers. These include the need to implement risk management processes and increased control functions organizationally. Uncertainty around telematics, internet sales, sharing economy, self-driving cars and automotive advances adds another layer of complexity.

Insurers have implemented ORSA and international regulators are moving ahead with further development of Solvency II and IFRS. The changes to the capital factors in the 2015 Minimum Capital Test have implications for
Companies investing in technology, equities and foreign investments. The return on these investments must be weighed against the increased capital demands.

In 2016, a P&C insurer must pay particular attention to the evolving IFRS rule changes: IFRS 4 (insurance contracts) and IFRS 9 (financial instruments). The delay in the issuance of IFRS 4 will most likely result in a delay in the IFRS 9 implementation, which is otherwise effective 1 January 2018. This will result in insurers implementing later than other financial institutions. At the same time, insurers must address the evolving accounting environment, which entails the provision of more extensive, precise and detailed disclosures.

**Technology innovation**

Digital technology will continue to transform the P&C industry in the coming year. Millennials and mass-affluent consumers, in particular, are seeking the latest digital tools, such as on-demand insurance apps. Meanwhile, insurers are establishing omni-channel platforms to reach and service customers more effectively. At the same time, insurers are exploring the use of new technologies like telematics, in-home and building sensors, drones and other geographical information systems. While their current adoption is not widespread, early adopters have made clear that these technologies are ready for integration into market value propositions and standard operating procedures. While the impact of these technologies is an emerging area, advanced analytics, such as predictive models, combined with cloud and on-demand technologies, will provide insurers with the instruments to re-engineer front and back offices.

But digital innovation also carries greater risks. Digital technologies make insurers more vulnerable to financial fraud, data theft and political activism. Privacy breaches are becoming a bigger concern as insurers gain wider access to sensitive financial data. Even the use of social media is exposing firms to reputational risks.

**Ontario auto reform**

Ontario auto reforms are causing market instability due to the outcome of the 15% premium rate reduction imposed by the provincial government. Ontario has some of the richest policy benefits in the country and as such is exposed to increased fraud risk or exaggerated claims. While customers will benefit from the rate reduction, there is significant potential for insurers’ profit margins to be reduced if claims costs are not controlled.
Impact of external forces on the Canadian P&C market in 2016
(0 = Very Low impact, 10 = Very High impact)

Technology
Digital technologies, such as social media, telematics and analytics, are redefining the insurance market. The impact will affect most business areas, from marketing and distribution to customer service and pricing models.

Competitive landscape
Competition will heat up as established insurers act fast to capitalize on game-changing market shifts. Challenges will also come from non-traditional sources, such as FinTechs, offering innovative digital solutions.

Customer expectations
Services in other digitally enabled industries are causing consumers to demand more personalized experiences from insurers. With the greater opportunity for comparison shopping on the web, the impact will likely be significant.

Economic and financial conditions
Uncertain financial and economic conditions will continue into 2016. Slow economic growth, decline in the Canadian dollar and weakness in the oil and gas industry are major downside risks for insurers.

Regulation
In 2016, insurers will need to stay on top of changing regulations, implementing risk management processes and increased control functions. In particular, changes to capital factors will have implications for companies investing in technology, equities and foreign investments.

Cyber risks
Digital transformation will expose insurers to higher risks from fraud, data theft and political activism. With greater access to sensitive data, privacy breaches will become a bigger worry, as will reputational risks from the use of social media.

Catastrophes
The numerous natural and man-made disasters of previous years have been less prevalent in the last year. Despite this fact, globally, climate change and natural disasters are a constant challenge for P&C insurers.
Roadmap for transformation: priorities for 2016

In 2016, P&C insurers will need to build a roadmap for strategic transformation aligned to new customer imperatives. Refining legacy products and approaches is not enough – what is required is a fresh outside-in approach that starts with the customer and carries through to digital trends and market shifts, both inside and outside the insurance industry.

Specifically, leading insurers will focus on the following pathway to change:

1. Transform operations to drive efficiency, reduce costs, accelerate growth and improve the customer experience
2. Shift from a product to a customer experience orientation
3. Position your organization for digital leadership
4. Develop and attract the right talent to drive change
5. Prepare for the next wave of M&A activity
6. Create a culture of continuous innovation
7. Drive performance through analytics
8. Make risk management a key priority
Many Canadian insurers are still struggling with legacy processes and systems. These inefficient patchworks of back-office systems and processes have evolved through acquisitions, partnerships and a lack of investment in new technology. With some technologies dating back as far as the 1990s – and even the 1980s– these systems and processes are no longer fit for purpose in a marketplace where rich customer experiences, rapid innovation, quick response times and actionable insight are paramount.

In 2016, top-performing Canadian P&C insurers will need to transform their operations to provide an integrated customer experience across all channels and customer touch points. This transformation will require breaking down silos and will play out across many areas of the enterprise – IT, finance, customer service, sales, marketing, distribution, claims, underwriting. All are directed to achieving multiple organizational objectives: driving efficiency, reducing costs (both indemnity costs and expenses), accelerating growth, improving the customer experience, improving speed-to-market and managing risks.

Priorities for 2016

Accelerate core insurance operations transformation
For P&C insurers to stay competitive, they need to transform their distribution, policy administration, billing, claims and sales functions.

To make the transformation journey successful, companies need to choose the right vendor solution and version, plan properly, think long term, understand the impact of scope, proactively address the common risks and consider a flexible development methodology. Despite the importance of moving ahead with core insurance operations transformation, insurers should not lose sight of their back-office operations (e.g., finance, HR). Back-office system implementations are also important in achieving a competitive advantage.

Enhance efficiencies through digital technology
Insurers have access to a growing array of technological solutions for maximizing processing efficiencies. Understanding how these solutions can be used throughout the value chain and successfully integrating them into the broader organizational ecosystem can help insurers add value and achieve their organizational goals.

Fast-track transformation through shared services and outsourcing
Leading insurers seeking to fast-track operational transformation are turning to outsourcing or shared services capabilities. The advantages of insurance outsourcing are numerous: cost savings, increased process efficiency, better document management and allowing staff to focus on value-added tasks and activities.

However, certain key success factors need to be considered for business process outsourcing to be successful. These can include defining key performance indicators (KPIs) and service level agreements (SLAs), very carefully choosing the right business process outsourcing vendor, ensuring top management commitment and understanding which functions are the best candidates for outsourcing to realize organizational objectives.
Putting the customer first
Changing customer needs and expectations are making many of today’s insurance services less relevant. With a few notable exceptions, the traditional product suite has been relatively static and has not kept pace with evolving risks. Customer expectations are being influenced by what’s going on in other sectors.

Faced with certain constraints such as few interactions with their customers and the nature of the insurance product, which is sometimes complex and influenced by regulatory constraints, insurers are trying to stay relevant to their client base.

Priorities for 2016

**Think outside-in, not inside-out**
To adapt to this fast-evolving marketplace and differentiate themselves from competitors, insurers must enhance their service capabilities while developing products better able to serve new customer needs and behaviors. By providing services that build on the customer experience and changing expectations, insurers can foster stronger, more holistic relationships with clients and ultimately improve policy retention and generate higher margins.

**Take a value-added, advisory approach**
Customers are increasingly looking to their insurance providers for risk advice, not just insurance products. To enhance their brand and improve performance, insurers must be ready to provide customer-centric services to satisfy these new expectations. Insurers will need to analyze their clients’ exposures and develop risk-mitigation strategies and insurance coverage tailored to their needs. The rise of real-time risk data in both personal and commercial lines provides an opportunity for innovative insurers to address uncovered or mispriced risks.

**Shift from a transactional to a relationship perspective**
Focusing on improving the customer experience is an important growth lever. Accelerating growth begins by moving from a transactional to a relationship view of the customer.

Rather than focusing on the number of products customers buy, insurers should weigh the strength and length of their customer relationships. Personalizing sales and marketing strategies and enriching the customer experience is critical to making this shift, which insurers are driving through better use of data and analytics.

**Expand two-way communication with customers**
Although customers want a wide array of self-service options, today’s consumers also want 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 Canadian consumers.

**Expand distribution channel**
Customers are looking for more choice in the way they communicate and receive services from their insurers. Companies should expand the distribution channel and communication channel mix to offer customers a choice across the insurance value chain.

Customer expectations vary from low-touch to high-touch depending on the type of transaction. Insurers need to understand how customer expectations and needs vary across the value chain. Delivering according to the needs of different customer segments requires a planned approach to distribution and communication channels.
Position your organization for digital leadership

Preparing for further digital disruption and taking advantage of digital shifts

Like many other countries, Canada’s marketplace is undergoing a digital transformation. But, many traditional insurers still show a low level of digital maturity, struggling to develop digital strategies that enhance the customer experience, extract efficiencies and drive future growth.

As digital service models become more common in other industries, the P&C sector will need to align to the rising expectations of consumer and commercial customers. Digital technologies, such as mobility, social media and telematics/sensor-based technologies, will continue to disrupt all parts of the P&C value chain – from client acquisition to claims and servicing.

From a customer experience perspective, self-service portals and mobile applications can enable customers to choose how they want to interact with their insurance carrier throughout the value chain. Enabling front-line employees with mobile tools is an additional lever that can help insurers offer a better end-to-end customer experience from sales and underwriting to billing and through to claims.

Following the banking sector’s lead, 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.

Lay the groundwork for digital transformation

To meet changing expectations of diverse stakeholder groups, insurers need to digitize interactions with customers, employees, distributors and suppliers. As back-office systems are being readied, leading insurers should not wait for full integration, but should instead push forward with next-generation portals, redefining customer experience, data access, queries and navigation.

Building new distribution channels and working closely with existing distribution partners to enhance the customer experience is a strategic imperative.

Rethink products and customer interactions for the digital marketplace

Insurers will need to reimagine their products and services from the customer’s viewpoint, rather than an inside-out perspective. Becoming more customer-centric will require insurers to recast many aspects of their business, from organizational culture and structure to performance measurement. The winners will be those insurers that compete on a customer’s perception of value, rather than on price alone.

Build the technological infrastructure needed to drive digital transformation

Built for less complex times, many legacy systems cannot support today’s digital marketplace 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.

In 2016, insurers must continue to invest in back-office systems to enable digital enterprise platforms. These should be designed to allow for future expansion, omni-channel distribution and an improved customer experience, while minimizing customer service costs and protecting against escalating cyber risks.

Priorities for 2016

- Lay the groundwork for digital transformation

- Rethink products and customer interactions for the digital marketplace

- Build the technological infrastructure needed to drive digital transformation
Coping with a widening talent gap
Existing insurance teams often are not prepared for today’s fast-changing digital marketplace. But filling the talent gap can be challenging, since the insurance industry is not often the first choice of new graduates from top postsecondary institutions. With finance, technology and consulting attracting most of the promising graduates, a talent chasm is forming in the P&C industry. Insurers must be proactive in recruiting and retaining next-generation innovators and leaders — while retooling existing teams with new skills.

Develop new roles to facilitate change
As insurers embrace innovation and adopt more advanced digital platforms, they will need to establish new business roles to drive these initiatives. For instance, the stronger focus on analytics is increasing the demand for data scientists, professionals who can apply predictive analytics and other sophisticated quantitative tools to support underwriting and claims-handling processes.

Create an environment that rewards innovation
A culture of innovation will help attract millennials and entrepreneurial talent with fresh perspectives. Bringing in new ideas and skills will be essential for insurers pursuing technological innovation in an industry not known for change.

Priorities for 2016

Develop new roles to facilitate change
To acquire and retain this new crop of talent, insurers will need to set up reward systems and career paths to incentivize innovation and risk-taking in alignment with new strategic imperatives.

Expand risk advisory capabilities
Customers are increasingly interested in working with true risk advisors and finding insurance solutions that match their lifestyles. Traditional product approaches directed at individual risks are falling out of favor as customers seek more holistic solutions.

In 2016, insurance teams will need to develop expertise in wealth and risk advisory, such as bundling insuring of homes, cars, boats and jewelry, and the liability associated with them as part of a value-add wealth management service.

Make diversity a strategic imperative
Inclusiveness is about much more than creating an open and equitable environment based on race, culture, gender, sexual orientation, age and physical ability. It’s about embracing the different ideas, perspectives, skills and experiences that diverse individuals bring to the table — and putting them together to address familiar problems in new and innovative ways.

In today’s highly competitive global economy, workplace diversity is no longer a “nice to have” HR policy. It’s a business imperative with a bottom-line impact.
A growing talent gap
Consolidation in the Canadian P&C market will continue in 2016 and beyond. In each of the past six years, the market has experienced at least one major transaction, and the trend continues in 2016.

Insurers are looking for growth in a mature market as well as scale advantages and adding to their distribution channel mix. The key driver has been the underlying transformation of the sector. Large-scale M&A is playing its part as one of the key enablers of transformation – not the only enabler by any means, but one of the key ways of accelerating the journey toward a desired future model.

Priorities for 2016

Acquisition pipeline and alternatives
Given that the Canadian P&C market has been in consolidation for several decades, the number of acquisition targets is diminishing. However the Canadian P&C market continues to be very fragmented. For insurers seeking to gain a competitive advantage through M&A, this requires having a well-defined process for identifying potential targets. Strategic goals can also be accomplished through acquisition alternatives, such as building distribution capabilities via partnerships and acquiring IT capabilities through investments in insurance service firms.

Build an effective post-merger integration plan
Regulatory and IT complexity is making it more difficult for insurers to integrate multi-country operations. These challenges are multiplied when M&A activity crosses borders or regulations change during an acquisition. That’s why the creation of a sound integration plan – weaving together finance, IT, legal, actuarial and other internal processes – should be a key part of an insurer’s M&A strategy.

Companies involved in M&A should assemble the necessary building blocks to create single technology platforms, self-service customer portals and omni-channel distribution systems. Replacing duplicative technology, outdated service centers and first-generation mobile-enabled distribution will remove cost redundancies and inefficient processes.

Take steps to protect against tougher competition
Insurers that refrain from the M&A frenzy will require a strategy to compete more effectively against larger, better-capitalized companies. Recruiting human capital will become paramount, as will accessing distribution that provides high-retention, profitable business.

M&A activity in 2016 will make insurers vulnerable to takeovers, particularly those with the potential to provide an acquirer with greater product diversification, wider market access, stronger analytics and increased cost efficiencies.
Create a culture of continuous innovation

The rise in usage-based insurance, digital distribution channels and other disruptors is shaking up the industry. Widespread data availability and advanced analytical techniques are enabling new market entrants to absorb risk that was once the exclusive territory of insurers.

Priorities for 2016

**Explore new technologies and startup models**
Competition is heating up as an array of new entrepreneurial companies offer services that were once the exclusive domain of traditional insurers. To cope, insurers will need to adopt, acquire or even fund new technologies and experimental models that may even compete with their existing businesses. Recently introduced P&C insurance products, such as insurance for cyber risk, ridesharing and drone exposures, suggest that insurers can rise to the innovation challenge.

**Be prepared to cannibalize parts of your business, before your competitors do**
The P&C insurance industry has not been known as a change leader. A growing asset base is a vital sign of stability for clients. But as a business grows, more processes are added, creating bureaucratic layers that stymie innovation. To offset these institutionalized barriers to change, insurers will need to develop a culture of innovation that allows for internal competition.
Disparities in frequency and severity trends among insurers highlight the importance of data and analytics in driving underwriting results. Harnessing large volumes of data from real-time sources can help insurers develop new products, refine pricing strategies and reduce customer churn. When combined with a robust operating strategy, advanced analytics may lead to increased underwriting profitability and provide a valuable market differentiator.

Analytics can be used to drive improvements throughout the insurance value chain, including:

- Customer management and customer analytics
- Marketing
- Product and service development
- Distribution management (broker/agent selection and performance management) and sales
- Underwriting and pricing
- Policy administration and customer service
- Claims

Priorities for 2016

Understand how analytics can drive value across the value chain and product line

The first step in making effective use of analytics is to understand what the use cases are.

Insurance companies have historically been data rich and, as such, the first step is to determine what has changed and how the organization can add value by using analytics. This can be done by understanding that new types of information exist (e.g., customer data, unstructured data) as well as the concrete use cases that can be applied to add value. This includes an understanding of both value chain and product line perspectives.

From a value chain perspective

Insurers that understand how advanced analytics can drive value throughout the insurance value chain are in a position to differentiate themselves. This can help identify some higher-value initiatives where analytics can be applied to drive profitability and growth. Once there is a common understanding of how analytics can help drive value, insurers need to make the investments needed to develop strong analytical capabilities across the traditional organizational levers: talent, technology, processes and organization structure.

Apply analytics for the homeowners and commercial markets

In 2016, personal lines insurers will increasingly apply analytical capabilities to the homeowners market. Greater adoption of technological innovation in the home creates an opportunity for both real-time risk assessment and pricing strategies.

Using analytics to manage commercial market risks

As risks rise, small business owners are seeking broader insurance coverage and a simpler sales process. Insurers with the analytical capabilities to manage evolving risks and the technological know-how to create an automated sales experience will be better equipped to meet fast-changing customer needs. The experience in using analytics in the small commercial market will provide insurers with a blueprint for gaining efficiencies in the larger commercial market.
Complex and volatile landscape
Economic, financial and political uncertainty, combined with interconnected global markets and disruptive technological change, has created a more complex and volatile landscape for insurance firms, heightening the need for best-in-class risk management. Faced with a challenging environment and driven by regulatory demands, insurers have made risk management a C-suite and board-level priority, with risk managers being held accountable for improved financial performance and value creation.

Priorities for 2016

Keep on top of changing regulations
Emerging regulatory regimes include calls for greater uniformity at the provincial, federal and global levels. But the ultimate form of these requirements is far from settled. This also includes less traditional regulatory themes like digital distribution, usage-based insurance and related sectors like drones and the sharing economy.

More than ever, insurers will need to stay on top of shifting regulatory frameworks, communicate the industry impact and respond to changes as they emerge.

Watch for emerging risks, such as cyber-attacks
With access to growing volumes of sensitive data, insurers large and small are seeking greater cyber risk protection. Corporate boards are becoming increasingly aware of the damage a cyber-attack can cause, including potential liability at the board level and destruction of reputation and brand. Risk managers will be tasked with staying ahead of the ever-increasing sophistication of hackers.

Remember, protection is only as strong as the weakest link in the chain
Even if an insurer is well insulated from cyber-attacks, its outside vendors and other partners across the value chain may be vulnerable. Partners, including software vendors that have access to an insurance company’s systems such as its underwriting platform, can inadvertently provide hackers with a conduit to valuable company data. Risk managers must be careful with data released to third party vendors and partners for any reason, especially when that data is subsequently returned to the company.
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