Assurances et gestion des risques
Insurance and Risk Management

UK General Insurance: Changing Distribution Paradigm

Shishir Kumar

Volume 76, Number 4, 2009

URI: https://id.erudit.org/iderudit/1091871ar
DOI: https://doi.org/10.7202/1091871ar

See table of contents

Publisher(s)

Faculté des sciences de l’administration, Université Laval

ISSN

1705-7299 (print)
2371-4913 (digital)

Explore this journal

Cite this document

Kumar, S. (2009). UK General Insurance: Changing Distribution Paradigm. *Assurances et gestion des risques / Insurance and Risk Management*, *76*(4), 75–107. https://doi.org/10.7202/1091871ar

Article abstract

UK General Insurance industry is going through structural changes. Increased regulatory burden and rising operating cost are forcing all insurers to reduce the cost and improve the efficiency. In addition, increasing commoditization of underwriting and insurance products and proliferation of “me too” distribution channels are further making it difficult. Hence, insurers are embracing innovative operating model to retain cost. Direct or Virtual distribution- internet- is playing larger role due to lower cost model. Companies are using direct channel as a complimentary to the traditional channel. However, given its associated advantages and consumer willingness will put forth as a dominant distribution channel.

Assurances et gestion des risques, vol. 76(4), janvier 2009, 75-108
Insurance and Risk Management, vol. 76(4), January 2009, 75-108

UK General Insurance: Changing Distribution Paradigm

par Shishir Kumar

ABSTRACT

UK General Insurance industry is going through structural changes. Increased regulatory burden and rising operating cost are forcing all insurers to reduce the cost and improve the efficiency. In addition, increasing commoditization of underwriting and insurance products and proliferation of "me too" distribution channels are further making it difficult. Hence, insurers are embracing innovative operating model to retain cost. Direct or Virtual distribution- internet- is playing larger role due to lower cost model. Companies are using direct channel as a complimentary to the traditional channel. However, given its associated advantages and consumer willingness will put forth as a dominant distribution channel.

RÉSUMÉ

L'industrie de l'assurance de dommages du Royaume-Uni est actuellement dans un processus de changements structurels. Le fardeau de la réglementation toujours croissante et les coûts d'opérations qui augmentent sans cesse obligent les assureurs à réduire les coûts et à améliorer l'efficacité. De plus, l'augmentation de la titrisation des produits d'assurance et la prolifération des canaux de distribution traditionnels rendent la situation amplement difficile. En conséquence, les assureurs adoptent actuellement des modèles novateurs de rétention de coûts d'opération. La distribution directe ou virtuelle (via internet) joue un plus grand rôle en raison des modèles de réduction de coûts. Les sociétés d'assurance utilisent en

The author:

Shismir Kumar is working as Deputy Principal, Shining Consulting (Strategic Management Consulting Firm), Bangalore. He has expressed his own views, not the organization associated with. He can be reached at: analyst.shishir@gmail.com.

plus les canaux de distribution directe, qui jouent un rôle complémentaires aux canaux traditionnels. Toutefois, les avantages tarifaires et l'attrait grandissant des consommateurs à l'égard des canaux de distribution directe devraient favoriser cette voie au regard de toutes les autres.

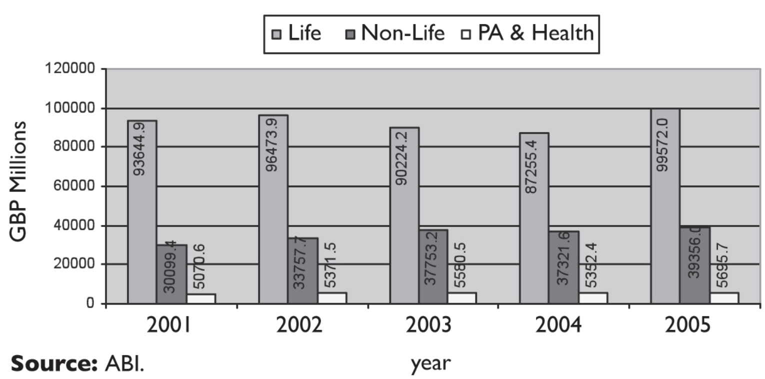
1. INTRODUCTION

UK General Insurance industry is characterized by increasing commoditization of underwriting and insurance products and proliferation of distribution channel. Currently, industry is going through structural changes. It is because of increased regulatory burden and rise of internet, which are forcing all players to reduce the cost and improve the efficiency. This is forcing them to think carefully about their operating models. Companies that succeed in reducing their costs by embracing innovative new operating models and achieve greater scale, the future looks promising. Otherwise, they will be forced to withdraw from the industry.

2. THE MARKET

The UK insurance industry is the largest in Europe and third largest in the world, after the US and Japan[1]. UK accounted 8.6% of the total worldwide premium income in 2005. The market consists

FIGURE 1
MARKET GROWTH



Source: ABI.

of companies, Lloyd's underwriters, brokers and intermediaries and their clients.

The following graph illustrates the relative sizes and growth rates of the UK life, non-life (non-marine) and PA/PMI sectors over the period from 2001 to 2005

3. MARKET STRUCTURE

UK insurers comprise limited liability (ltd) and public limited companies (plc), publicly quoted and privately owned stock companies and mutuals. Companies may be publicly quoted (Norwich Union/Aviva, Royal and SunAlliance), owned by foreign insurance groups (AIG, Axa, Zurich, Allianz Cornhill)[2], mutuals (BUPA, NFU Mutual) or owned by banks (Churchill/Direct Line, Esure)

There are also a number of important financial services groups in the UK market which combine banking and insurance services such as Royal Bank of Scotland (RBS)[3], Halifax Bank of Scotland[4]. Other insurers, such as Zurich and Prudential, have set up their own banking operations.

4. MARKET CONCENTRATION

According to the ABI, a total of 50 composite insurers and 836 purely non-life insurers are authorized to carry on business in the UK in 2005. Top 5 insurers control 55.5% of the market share[5], where as top 10 insurers accounted 70.7% of the market share.

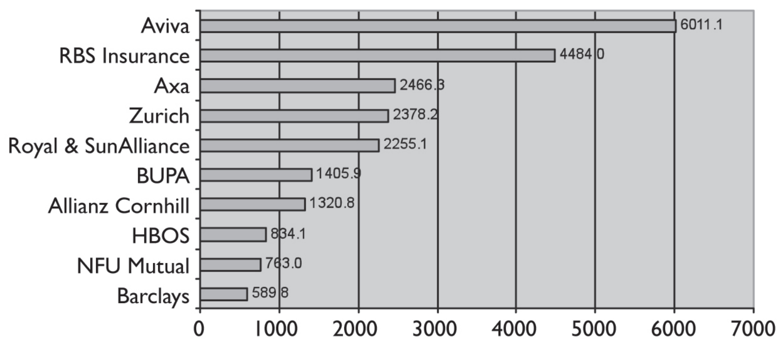
TABLE 1
MARKET CONCENTRATION

	2002	2003	2004	2005
Top five insurers	51.4	56.1	56.5	55.5
Top 10 insurers	70.6	71.2	71.9	70.7
Top 20 insurers	51.4	84.5	85.4	84.0

Source: ABI.

The top 10 insurance groups in the UK (based on net written non-life premium in 2005) were as follows:

FIGURE 2
LARGEST NON-LIFE INSURANCE COMPANIES

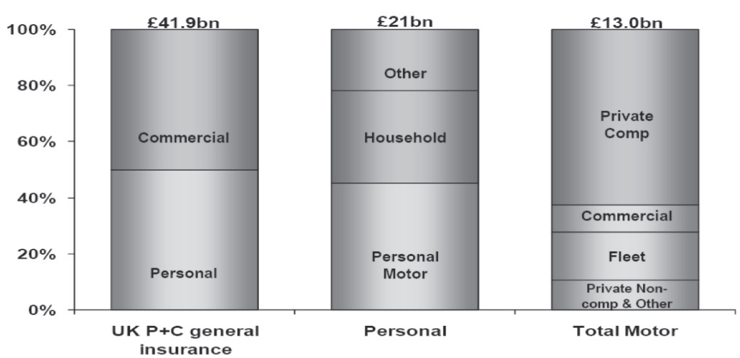


Source: ABI.

5. MARKET SEGMENTATION

The UK general insurance has been segmented into two lines of business: personal lines and commercial lines.

FIGURE 3
OVERALL UK P&C GENERAL INSURANCE MARKET 2004

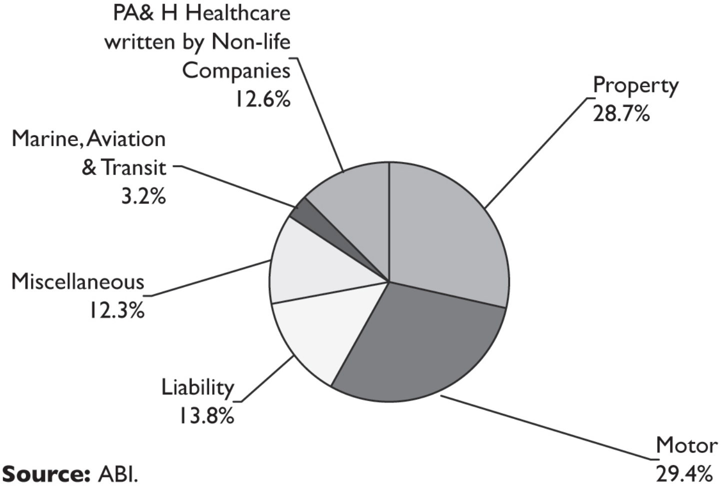


Source: ABI.

6. MARKET-SHARES BY NON-LIFE SEGMENTS[6]:

Motor insurance is the largest segment in the UK General Insurance. In 2005 motor business accounted 29.4% of the total non-life market, to GBP 13.22bn (USD 24.07bn). It was followed by the property segment, which accounted 28.7% of the market share, resulting to total GWP of GBP 12.92bn (USD 23.52bn).

FIGURE 4
MARKET SHARE BY SEGMENTS



Source: ABI.

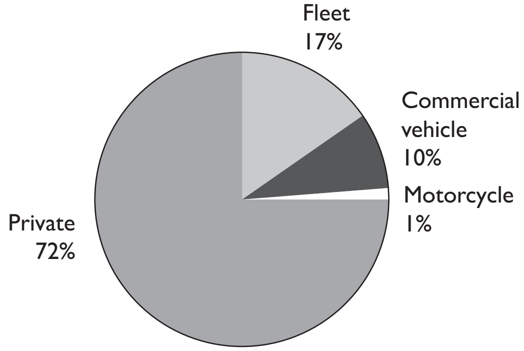
7. UK MOTOR MARKET

Total motor GWP is approximated at £13bn in 2005, with private motor insurance accounting for the largest portion of premiums at 72%

The UK motor insurance market is relatively mature with underlying product becoming increasingly commoditised. The basis of competition is therefore predominantly price, however, brand equity and structure of terms and conditions are also playing an important role.

FIGURE 5
PERSONAL MOTOR VEHICLE LARGEST SEGMENT

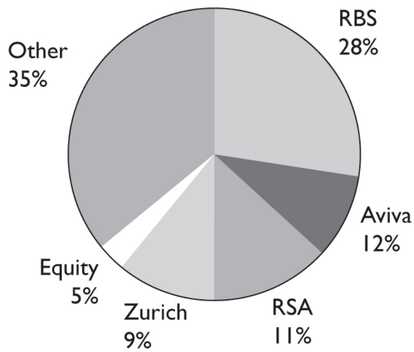
UK motor insurance product mix (% GWP)



Source: IAG (based on FSA returns and Datamonitor).

FIGURE 6
TOP FIVE CONTROLLING 65% OF MARKET

UK motor insurance product mix (% GWP)



Source: IAG (based on FSA returns and Datamonitor).

8. DISTRIBUTION CHANNEL

UK non-life market has one of the most sophisticated multi-channel insurance distribution systems in the world. The major insurers have multi-channel distribution network. But, customer prefers distribution channels as per the purchase complexity, product characteristics, channel attribute, and customer segment. Following graph illustrates the channel preferences.

FIGURE 7
CHANNEL PREFERENCES ILLUSTRATION

Product characteristics

	Low	High
Complexe	Advisory	Advisory driven
Simple	Commodity-driven	Commodity

Channel attributes

	Image	Advice	Service	Convenience	Price
Individual		✓	✓		
Institutional	✓			✓	
Affinity	✓			✓	
Direct				✓	✓

Customer segment profile

	Individual	High	Institutional	Direct
High end	✓	✓		✓
Middle		✓	✓	✓
Low end				✓

Source: Accenture Analysis.

High involvement products need more advisory services whereas low-end, commodity products can be bought directly. Hence, it can be construed that complexity of the product is directly proportionate to the advisory services

9. GENERAL INSURANCE SALES BY DISTRIBUTION CHANNEL: PERSONAL LINE

TABLE 2
DISTRIBUTION CHANNEL - PERSONAL LINES

Personal lines % share the premium	2001	2002	2003	2004	2005
Independant intermediaries	41	33	31	31	32
-National brokers	12	11	10	10	12
-Chain brokers/telebrokers	12	5	5	5	5
- Other independents	18	17	16	16	15
Company agents	13	10	8	8	6
- Direct sales force	7	6	3	3	2
- Tied agents	7	4	5	4	4
Direct selling	27	30	32	31	31
Banks, building, societies	11	14	15	13	17
Utilities/retailers/affinity gps	5	11	11	15	13
Others	2	2	2	2	2

Source: ABI.

10. GENERAL INSURANCE SALES BY DISTRIBUTION CHANNEL: COMMERCIAL LINE

TABLE 3
DISTRIBUTION CHANNEL - COMMERCIAL CHANNEL

Personal lines % share the premium	2001	2002	2003	2004	2005
Independant intermediaries	80	85	84	84	82
-National brokers	50	52	54	54	50
-Chain brokers/telebrokers	8	3	5	5	5
- Other independents	21	29	24	25	28
Company agents	6	6	6	5	5
- Direct sales force	5	5	5	4	4
- Tied agents	1	1	1	1	1
Direct selling	12	7	7	7	8
Utilities/retailers/affinity gps	1	1	2	2	3
Other	1	1	1	1	1

Note: due to rounding some totals may not equal the breakdown.
Source: ABI.

11. DIRECT HANDLING

Direct relationships between insurers and their clients, through tied agent, account for only a small part of total sales. In 2005 only 1% of commercial risks and 4% of personal lines business were sold in this way.

Company sales representatives have been most active in the household market generally selling insurance door-to-door to lower-income families in conjunction with life and savings products, but the use of this channel has declined mainly in the personal line, whereas it is facing stagnancy in the commercial line of business. As far as its presence in the personal line is concerned, it has been declining for the last five years. In 2005, it was controlling 2% of the total sales whereas 7% in 2001.

12. DIRECT CHANNEL

Companies are using direct channel[7] as a complimentary to the traditional channel. All the major composite insurance companies have set up direct operations to complement their traditional broker and agency distribution networks. The leading direct writer is Direct Line (owned by the Royal Bank of Scotland), with other companies including more th>n (Royal & SunAlliance's direct arm), Norwich Union Direct (Aviva), Admiral and Cornhill Direct (Allianz).

Direct sales penetration is mainly confined to standardized or low involvement products like household, motor, personal accident, creditor, pet and travel. However, direct selling is facing pressure from corporate partnerships and aggregators. These players have introduced a new form of intermediation into the market, which in the case of aggregators, is geared towards satisfying consumer desire for transparency with respect to market offering, namely with respect to price. Companies are now targeting SME commercial line of business through internet channel. For example, the establishment of on-line trading platform Hiscox's Inscribe[8], which offers professional indemnity contracts for management consultants and IT providers[9].

13. INTERNET CONSUMERS

Internet access amongst the UK population is very high with an estimated 14.3 million domestic users in May 2006, over 57% of households. Over two-thirds of all adults have used the internet and more than 60% have bought or ordered something on-line.

Those buying financial services online in the UK are predominantly young, with higher than average household incomes, belonging to socio-economic groups A, B or C1 and living in urban areas[10].

14. BANCASSURANCE

In 2005, bancassurance[11] accounted for 17% of the personal lines market by premium. Banks have a number of competitive advantages in the provision of insurance products. First, they have much better information on individual consumers—seen as key to pricing risk effectively. Second, the banks may be able to bring enormous economies of scale, particularly if they are part of a major global network. Banks and building societies are very important for the distribution of household business because of their control of the mortgage market but in addition a number of the larger institutions actively cross-sell household contents, motor, personal accident, travel, creditor and domestic appliance breakdown policies to their customer base.

Some of the main (non-life) bancassurance links include: Halifax Bank of Scotland, Lloyd TSB, Royal Bank of Scotland[12], Norwich Union etc.

Halifax Bank of Scotland	Owns direct writers (esure is the risk carrier for Sainsbury's Bank) and Firts Alternative; St Andrews Insurance (creditor)
Lloyds TSB	Owns Lloyds TSB General Insurance
Royal Bank of Scotland	Owns Direct Line/Priviliège and Churchill/ NIG; UK Insurance Partnerships is a generic insurer whose products are sold under other brands
Norwich Union	Strategic partner of banks Abbay, HSBC and Barclays

Source: AXCO.

15. AGENCIES

Agents comprise employed company sales representatives and tied and semi-tied agents working on a commission-only basis. The major insurers in the UK utilise an array of different insurance distribution systems and an increasingly important one is the affinity group[13]. The concept of affinity has been expanded to encompass the customers of a range of retail outlets. Examples include retailers Asda, Marks & Spencer, Tesco[14], Sainsbury's, Debenhams and Superdrug as well as the Post Office.

Some insurers (such as UK Insurance Partnerships, the leading white label insurer and part of the Royal Bank of Scotland Group) have been established solely to offer generic insurance products ("'white label" products) under the brand names of others. In addition, some mainstream insurers sell their own branded products but will also underwrite for other (sometimes competing) distributors who feel the strength of their brand can also be used for selling insurance.

Many affinities such as supermarket chains outsource almost everything, including underwriting, pricing, policy and administration and claims management to a single insurance provider, while limiting themselves to providing customer leads and controlling point of sale. The rationale behind placing customer-facing services such as claims management in the hands of utility, companies could improve the quality of their customer service while lowering costs by accessing economies of scale. Company such as Barclays outsources insurance products from Norwich Union. Hence, it capitalizes on supply chain efficiency and product innovation, such as pay-as-you-drive, of Norwich Union. However, there is few limitation of sourcing/ outsourcing from a single vendor. The disadvantage of sourcing from a single insurer is that it is unlikely to provide all customers with coverage as some will fall outside of the criteria employed by the single underwriter of the insurance products.

In an attempt to address these concerns, many companies are pursuing several strategies simultaneously. One such hybrid solution is that adopted by Bradford & Bingley, which has established an insurance panel for underwriting, pricing, policy administration and claims management, but also buys in insurance products from Legal & General. Adoption of such a hybrid strategy avoids the risks posed by an excessive dependence on a single underwriter; it means that customers lack a single point of contact for all the products they have purchased. For example, the household insurance purchased from an affinity is likely to be sourced from a different provider than the car insurance supplied by the same affinity[15].

16. INSURANCE BROKERS

Insurance brokers are the dominant sales channel in the UK accounted for 55% of all general business premiums in 2005. Separately, it accounted 32% of the personal line and 82% for commercial line. Moreover, it plays vital role in the commercial line of business. In personal line, it seems that it is losing ground to retailers, banks and others, who offer “white label” insurance products. Independent intermediaries are dominating the commercial line of business due to huge complexity involved. However, direct-selling and company agents’ market-share have been consistent over the years. But now, brokers are looking to have their own products carrying their own brands.

Non-stereo type Distribution Channel

17. TIE-UP WITH GYM

PruHealth, which run under the tag line «a healthy saving on your health insurance», have solidify their presence in the health insurance market. The core of their philosophy is to incentivise better health for customers. PruHealth offer a new approach, rewarding their healthy customers with lower premiums and bonuses. PruHealth also offer customers upgraded gym memberships as a reward for being healthy.

18. INTERMEDIARIES' COMMISSION

Commissions paid by insurance companies have been reduced from an average of 20% to between 12.5% and 17.5%

Household	12.5% to 15%
Commercial property	15% to 17.5%
CAR/engineering	15%
Private motor	7.5% to 2.5%
Motor fleets	7.5% to 10%
Employers' liability	5% to 10%
Public liability	15%
Professional indemnity	20%
Personal accident	25%
Marine cargo	20%

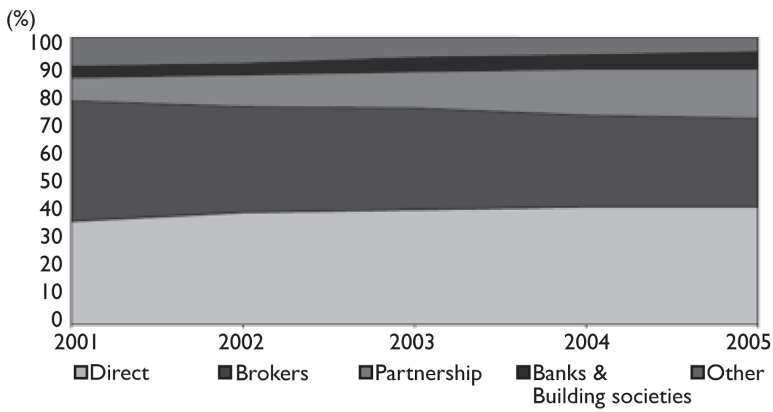
Source: AXCO, derived from ABI.

19. DISTRIBUTION TREND IN PRIVATE MOTOR INSURANCE

Generally, private motor insurance is perceived as a commoditized product because of low involvement. Therefore, it becomes easier for a person to easily adapt direct channels. The direct channel operates on a lower cost model, and the associated cost savings can be passed on to the consumer by way of reduced pricing.

In the private motor insurance business, share of broker channel is declining. Brokers accounted 42% of sales in 2001 and declined to 31% in 2005. Datamonitor, a consulting firm, predicts that there will be declining trend in the near future.

FIGURE 8
PRIVATE MOTOR INSURANCE BY DISTRIBUTION CHANNEL (% GWP)



Source: Datamonitor (based on ABI, Ipsos and MORI statistics.

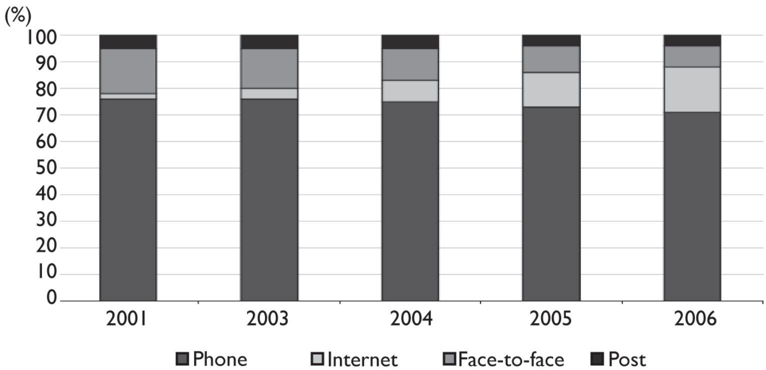
Direct channel capitalized on the opportunity provided by brokers. Share of direct channel increased from 36% in 2001 to 41% in 2005. The direct writers also made heavy investment on advertising, particularly television campaigns. Typically, direct insurers spend the majority (>60%) of their budget on motor insurance.

20. THE AGGREGATOR

The increasing popularity of internet, has given rise to aggregators. In the UK, major insurance brands have given in to quoting on aggregators[16]. In the UK, the majority of motor insurance sales are still arranged by phone (71% in 2006), however, the Internet is rapidly growing.

Datamonitor estimates that the percentage of online new sales [17] has risen from 32% in 2005 to 36% in 2006 on an industry-wide basis. Several players (including direct insurers, brandassurers and large telebrokers) report a greater portion (>50%) of new sales are now being sourced from online distribution.

FIGURE 9
MOTOR INSURANCE BY TYPE OF PLATFORM

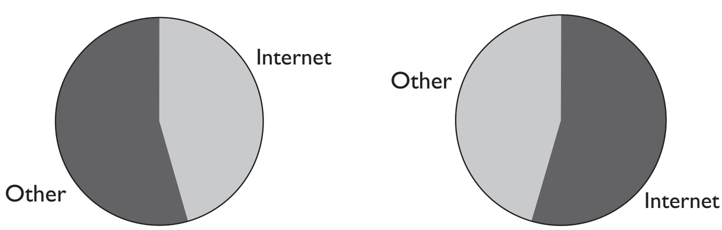


Source: Datamonitor, Credit Suisse estimates.

FIGURE 10
INTERNET SALES

Internet sales rising consistently...
Internet share of new business (1Q05)

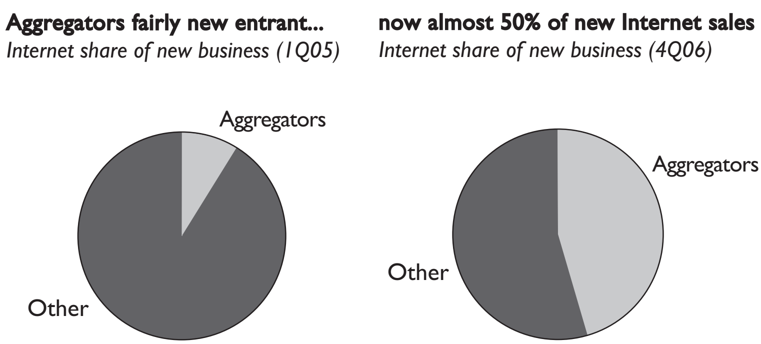
now more than 50% new business sales
Internet share of new business (4Q06)



Source: Admiral (sales where there is an Internet component - but could be completed over telephone), Credit Suisse estimates.

Rising trend in the internet sales has resulted in the growth of aggregators. But, the pace of growth is rapid. Aggregators were a fairly new entrant in the market in 1Q05, accounted for around 10% of new sales on the Internet. Aggregator's sales rose and accounted for around 55% in the 4Q 06.

FIGURE 11
AGGREGATOR'S SALES



Source: Admiral (sales where there is an Internet component - but could be completed over telephone), Credit Suisse estimates.

Admiral's confused.com controls around 60% of the aggregator market. Considering the growth potential, the number of aggregators has also been growing steadily.

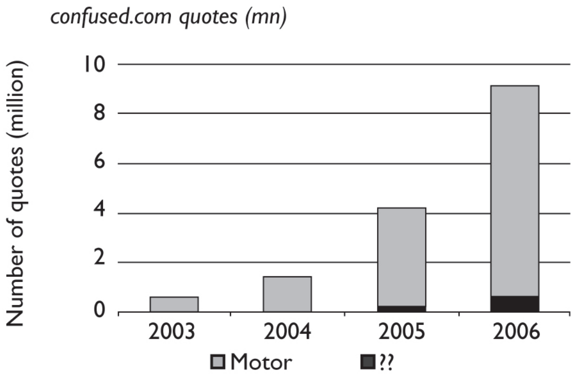
FIGURE 12
NUMBER OF AGGREGATORS RISING

Source: Company data.

21. AGGREGATORS FOR BROKERS

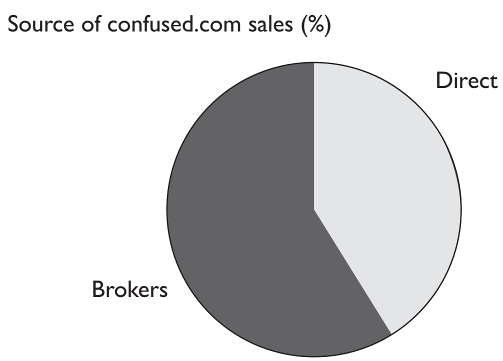
In addition to companies, brokers are also featuring heavily on the aggregator's websites in the UK. Hence, an insurer could effectively be quoting multiples times (at different prices) on a single quote. In the case of aggregator confused.com, brokers made up over 50% of sales for 2006.

FIGURE 13
AGGREGATOR GROWTH STRONG



Source: Admiral, Credit Suisse estimates.

FIGURE 14
TOP FIVE CONTROLLING 65% OF MARKET



Source: Admiral, Credit Suisse estimates.

Price is the key driver of online quotes on its aggregator website[18]. This means that it channel allows new entrants; both broker and insurers; to more easily enter the market and operate at the lower cost.

Aggregator sites are also gaining popularity with affinities that sell directly to the aggregator and can often actually compete with their own insurance partner.

22. AGGRAGATOR: THE PROSPECT

Credit Suisse estimates that the percentage of market quoted by aggregators should continue to grow rapidly from around 40% of the market in 2006 to around 70% by 2010F. Credit Suisse bases this analysis on the reported quote experience of confused.com (60% share)[19] and make adjustment for this number for the remaining 40% of this market. Key assumptions with respect to these forecasts are detailed.

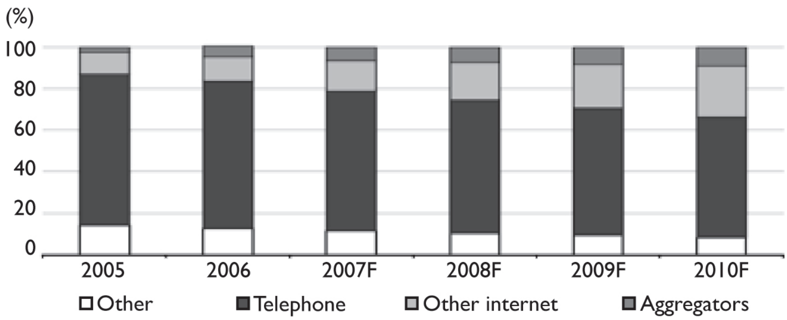
TABLE 4
ESTIMATES OF AGGREGATOR QUOTES AND SALES

	2005	2006	2007F	2008F	2009F	2010F
Aggregator share of total sales						
Number of cars ('000)	29,954	30,240	30,542	30,848	31,156	31,468
Growth (%pa)		1%	1%	1%	1%	1%
aggregator quotes ('000)^	6,833	14,250	16,388	18,026,	19,829	20,820
Growth (%pa)		109%	15%	10%	10%	5%
% of market quoted by aggregation*	**23%**	**47%**	**54%**	**58%**	**64%**	**66%**
Aggregator conversion rate (%)	10%	11%	12%	13%	13%	14%
% of total business sold by aggregators	2%	5%	6%	7%	8%	9%
Internet share of total sales	13%	17%	21%	26%	29%	34%
Aggregator portion of total Internet sales	18%	30%	30%	29%	28%	26%

Source: DVLA, Datamonitor, Credit Suisse estimates, *includes a 20% of adjustment for double count in that one customer could source quotes from multiple aggregator, ^actuals based on confused.com quotes assuming 60% market share.

The conversion rate of aggregators was at around 11% in 2006. It is because consumers often look to aggregators only to get an initial range of pricing and depth of providers and often complete their transactions with the underwriter direct; either by going directly to their website or on the phone; at a later date or with other insurers that do not participate on the aggregator's website. It is considered to be major stumbling block in the growth of aggregator. Despite these challenges, conversion rate would increase modestly, about 10%, in the years to come.

FIGURE 15
AGGREGATOR QUOTES TWO-THIRDS OF THE MARKET BY 2010F



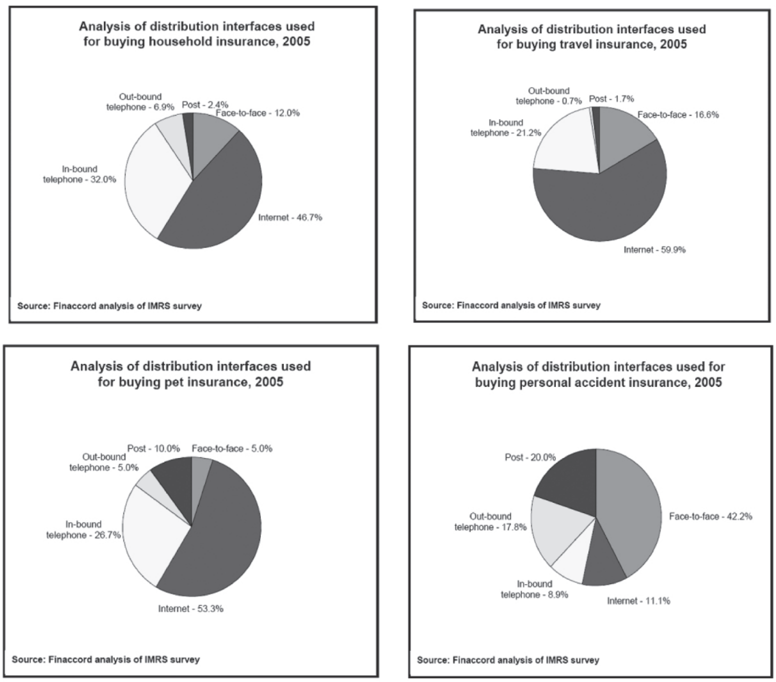
Source: Company data, DVLA, Datamonitor, Credit Suisse estimates, *based on quote volume experience of dominant aggregator (60% share) confused.com.

Overall, Credit Suisse estimate the Internet share of total sales to continue to grow, reaching around 35% of total sales by 2010, of which aggregator will account two-third (66%) by 2010.

23. DISTRIBUTION TREND IN OTHER SEGMENTS

According to the Finaccord's research, direct channel contributes significantly to the sales of household, travel, pet, and personal accident insurance products. Within the direct channel, internet contributes significantly to household, travel, pet insurance product, except personal accident insurance. However, there are few noticeable points. For example, personal accident, which is a low budget product, but it needs more advice. As a result, face-to- face channel controls 42.2%.

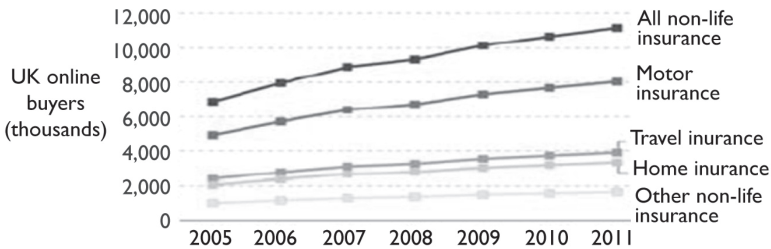
FIGURE 16
DIRECT CHANNELS DISTRIBUTION



24. DISTRIBUTION TREND IN ON-LINE: THE PROSPECT

According to Forrester, a consulting firm, there is a gradual growth in the number of online buyers for non-life insurance products in the UK. Though online contribution to motor insurance trend seems to be growing on y-o-y basis, it is growing at the reduced rate[20].

FIGURE 17
NON-LIFE: UK ONLINE BUYERS



Number of online buyers

All non-life insurance	6.880	7.946	8.396	9.330	10.140	10.665	11.160
Motor insurance	4.953	5.721	6.405	6.718	7.301	7.579	8.035
Travel insurance	2.408	2.781	3.114	3.226	3.549	3.733	3.906
Home insurance	2.064	2.384	2.669	2.799	3.042	3.200	3.348
Other non-life insurance	1.032	1.192	1.334	2.400	2.521	2.500	2.674

Source : www.actuaries.org.uk.

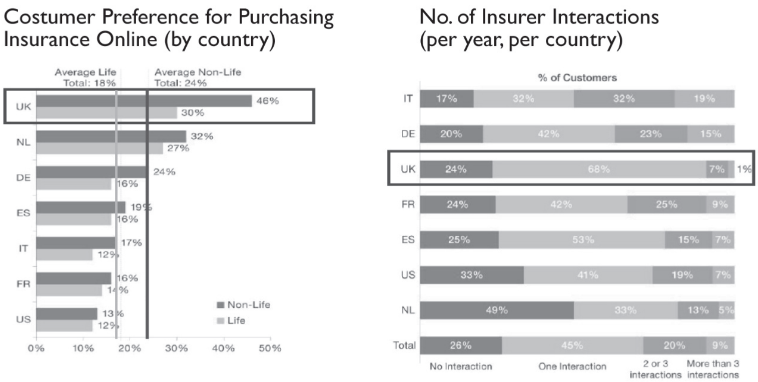
25. CONSUMER BEHAVIOR

Consumer behavior changes as per the complexity of the product. Online channel is primarily used for the commoditized/ standardized product, which needs low involvement. Following graph illustrates the channel preferences as per business line:

In UK, majority of the customers are buying online insurance than other countries and has the lowest level of insurers interaction. Non- life insurance products contribute more than the life insurance product. It is because the nature of complexity involved with the life insurance products

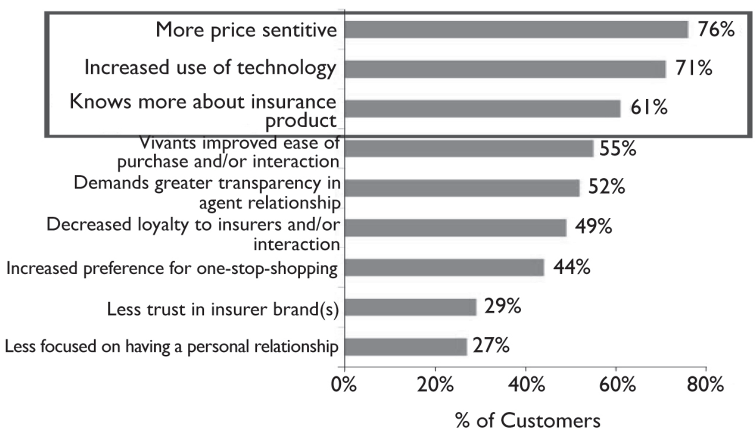
In addition, customers have also become more sensitive towards price. Personal relationship plays lesser role while buying low involvement insurance product.

FIGURE 18
CHANNEL PREFERENCES AS PER BUSINESS LINE



Source : www.actuaries.org.uk.

FIGURE 19
CHANGING CUSTOMER TRENDS (PAST 5 YEARS)

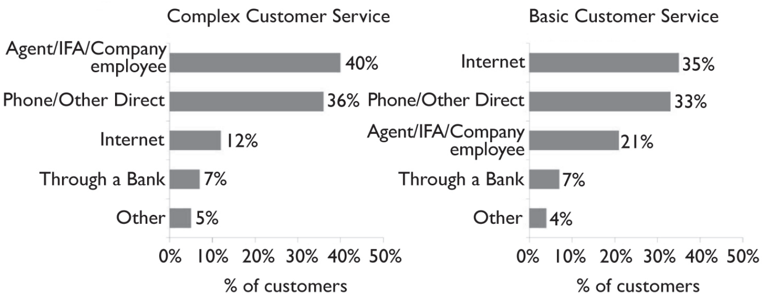


Source : Capgemini Analysis, 2006.

Increased price-sensitivity, tech usage, and knowledge about insurance products have made customers more demanding and less loyal. Customers' reluctance towards brand preference could lead to commoditization

Though customers are using multiple channels, personal relationship is preferred for the service for high involvement products.

FIGURE 20
CUSTOMER CHANNEL PREFERENCES FOR RECEIVING CUSTOMER SERVICE



Source : Capegemini Analysis.

26. CONSOLIDATION

In the last few years the broker landscape has undergone a substantial rationalisation, with a number of important mergers and acquisitions among the leading companies. Activity since 2001 has been at a much lower level, however, with limited mergers or acquisitions among the larger companies. Company such as Aetna entered into an agreement to acquire Goodhealth Worldwide[21] for increasing its presence in the UK market. In addition, it is also noticed that banks are eyeing insurers. For example, Banco Santander's took over Abbey to pursue extensive international insurance in the UK market. It is because banks want to capitalize on better information availability about individual customer, which is key to pricing risk effectively, and to bring economies of scale[22]. However, such moves are very limited.

27. BROKERS' CONSOLIDATION

According to IIB, over 20% of brokers may be sold in next three years to insurers[23]. Insurers are buying brokers not only as a purpose of investment, but also to secure influence over retention of large block of business. It is also because it allows the insurer easier access to its preferred risks, provides a higher degree of control over customer service, and supplies the insurer with an alternative revenue stream. In addition, it prevents the intermediary falling into the hands of a competing insurer or a consolidating brokerage. These moves also reflect a wider trend within the general insurance industry of buying into intermediaries to support growth plans. However, analysts feel that it could lead the unfair competition.

There was a surge in acquisition activity mainly among medium-sized broking operations. Regional companies like Towergate and Oval have been particularly active and a new regional broking power has emerged in the form of Jelf. Insurance Australia Group has bought Equity Insurance Group for GBP570 million, to establish the its presence as a leading player in the UK motor insurance market, and secure it access to consumers via a wide range of distribution channels. Insurance Australia Group further increased its UK presence with the acquisition of Hastings Insurance Services. Allianz also acquired Home & Legacy and Premierline Direct[24].

AXA is pursuing broker's acquisition strategy aggressively. For example, AXA's broking division, Venture Preference, has acquired two commercial brokers, the Davis Group and Smith Grayburn Young (SGY) Insurance Services[25]. Groupama UK has also acquired a majority shareholding in Lark Group Limited[26], which is one of the UK's top 50 insurance brokers and in the top 10 independent brokers.

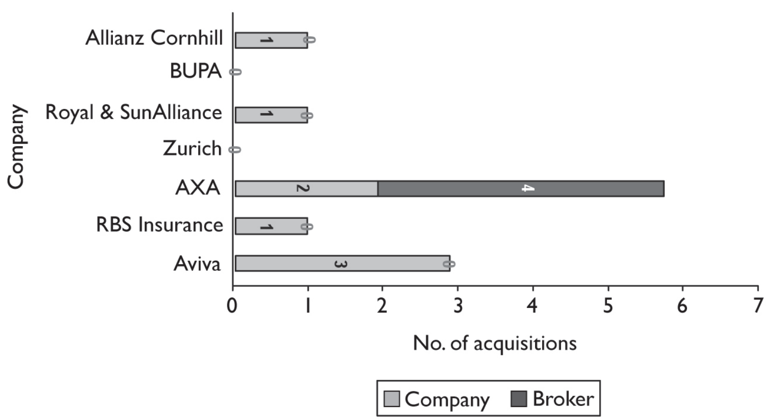
To thwart the move of leading insurers, brokers are consolidating to safeguard their interest. Big brokers like Saga and the AA have agreed merge their assets into a new holding company. The aim is to bring some of Saga's best practices and skills to the AA[27]. Private Health Partnership, a health insurance broker, has purchased the medical insurance portfolio of Home Counties Healthcare, a medical insurance company[28]. Chase Templeton, one of the leading insurance brokers in UK, has acquired Preferred Medical, the private medical insurance specialist, to increase its presence[29].

28. DISTRIBUTION TREND IN THE LAST 5 YEARS[30]:

Brokers' consolidation: Changing landscape

M&A has become norm to stay ahead in the competitive UK General Insurance market. Companies are preferring acquisition route to strengthen their presence in the existing UK General Insurance market. But, there is a shift in the trend towards broker's acquisitions.

FIGURE 21
ACQUISITION IN THE LAST 5 YEARS



Source : Compiled from various sources.

In the last 5 years, insurance major AXA made 6 acquisitions, of which its brokers' acquisition accounted 66%. It clearly reflects that there is a shift towards acquisitions of brokers. AXA is focused on the broker's acquisition to secure influence over retention of large block of business. For example, AXA UK has acquired commercial brokers such as Davis Group, Smart & Cook, Ignition NBS and multi-channel advisory business of Thinc Destini. AXA is followed by Aviva in terms of number of acquisitions. Contrastingly, Aviva is not focused on the brokers' acquisitions to propel growth. However, the trend doesn't seem to be pervasive within the insurance space. It could be an augury of future acquisition trend, which could be perceived as a predatory move by the brokers.

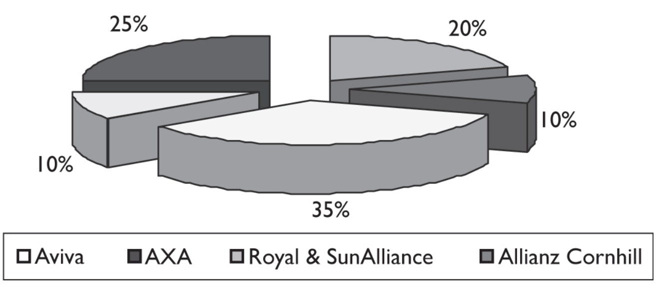
In the last 5 years, RBS made merely single acquisition. RBS acquired Churchill. Though RBS has made merely single acquisition, it was strategic. It acquired Churchill, which enhanced its portfolio. It was complementary to the RBS product portfolio. In direct channels, Churchill's strength in home insurance will balance Direct Line[31]'s strong position in motor insurance. Both Churchill and Direct Line have expertise in the distribution of general insurance products through partners, under their brands. Churchill, which also owns NIG, has a strong presence in commercial insurance products for SMEs, broadened the general insurance portfolio of RBS.

On the other hand, Zurich and BUPA don't seem to be interested in inorganic growth. For example, health insurance major BUPA is focusing on the core health insurance business. It has sold its sell its 25 UK hospitals to the European private equity firm Cinven and corporate childcare business to Emergency Child and Home Care Limited, part of the Family Care Company. It shows that BUPA is concentrating on its core health insurance business and focusing on organic growth.

29. CORPORATE PARTNERSHIP

In these days of rapid consolidation, insurers have realized that corporate partnership does have its place in this dynamically changing market. Insurance companies are making partnership with the corporate to fuel the growth. It plays vital role in securing huge business and retaining it for a longer period of time. It helps each-other to leverage on their strengths.

FIGURE 22
CORPORATE PARTNERSHIPS IN LAST 5 YEARS



Source: Compiled from various sources.

In the last 5 years, Royal & SunAlliance has made maximum, about 7, corporate partnerships, followed by Allianz Cornhill and Aviva. For example, Royal & SunAlliance made corporate partnership with Swinton, Caravan Guard, Westinsure, Towergate, COBRA Network, Paymentshield, Aquarius etc. Partnership with Swinton was the first major move into the pet insurance broker market for R&SA. These partnerships will increase the penetration by taking advantages of corporate client's base.

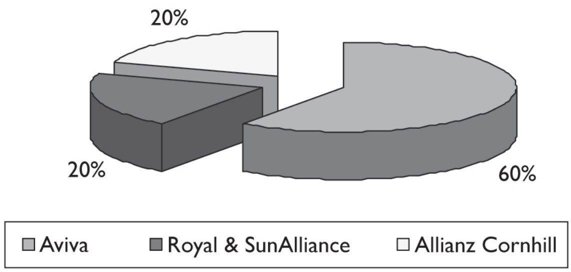
Allianz Cornhill partnered with Judicious Litigation Services (JLS), Tett Hamilton, Higos Insurance Services, Ten Insurance Services, England and Wales Cricket Board (ECB). It helps insurers in making sizable penetration in the corporate client's customer base. It also helps the insurers to complement the product or provide all insurance solution to the corporate client. For example, Allianz' partnership with ECB brought huge business to offer all accident and health insurance solution.

Aviva made corporate alliance with Daimler Chrysler, The Co-operative Bank, Leeds & Holbeck, ASDA[32] etc. Partnership with these companies made it sole provider of insurance products. Aviva can leverage client base of these corporate partners. Particularly, partnering with ASDA will give its products access to UK's favourite supermarket chain. Hence, partnering will help Aviva to offer ASDA customers with a range of general insurance products that offer great value for money and helpful service

More and more brokers will look for more corporate partnerships to stay-off the competition and safeguard their interest against rapid consolidation. Consolidation would lead to increase in the corporate partnership. Most of the existing partnership will remain in force. It will depend upon the specialized skills of the insurers. For eample, Daimler Chrysler, which used to operate a panel arrangement with four insurers, has given entire contract to Norwich Union. It also reflects that corporates are looking for one-stop solution, instead looking for multi-insurance tie-up to take advantages of best of breed service. Sole insurance solution provider will gain more momentum in the years to come.

30. TIE-UPS

FIGURE 23
TIE-UPS IN THE LAST 5 YEARS



Source: Compiled from various sources.

Distribution tie-up plays vital role in increasing insurance penetration. In the last 5 years, Aviva made distribution tie-up with Post-office, eBay, Co-operative insurance Society, and building society such as West Bromwich BS and Cumberland Building Society. It is quite evident that Aviva has adopted multi-pronged tie-up strategy, which covers myriad source of channel, to increase penetration in the UK market. Aviva is follwed by Allianz Cornhill and Royal& Sunalliance equally. Allianz Cornhill tied-up with aggregator website Confused.com and Amazon.co.uk. Royal & Sunalliance made partnership with two building societies- Derbyshire and Leek United Building Society.

It can be well construed that internet is having wider acceptance in the UK general insurance market. Companies are using online auction and shopping websites such as eBay and Amazon.co.uk to capitalize on their distribution strength. Moreover, commodity product, which requires low- involvement, are mainly sold thorough internet enabled channel. Aggregators are also being preferred as a channel of distribution for the personal line products. In addition, building societies are also increasing their foothold as a distribution channel.

31. DISTRIBUTION TREND IN THE LAST 5 YEARS: A VIEW POINT

Corporate partnership works as an insulator against consolidation for brokers. More partnership will take place in the years to come. Brokers will consolidate by acquiring small brokers to defend their position. Companies will also make more tie-ups with brokers to increase their penetration. Internet based channel such as aggregator and online auction and shopping websites are expected to gain more acceptance for buying personal insurance products. Affinity and building society will also be able to expand their network.

Aviva's multi- pronged distribution strategy seems to be consistent across all channels of distribution. Aviva is capitalizing all channel of distribution to catapult the growth. In stark contrast, AXA seems to be more aggressive in terms of distribution, especially brokers' acquisition. RBS, which seems to be dormant across the distribution channel, has competitive advantages of owning companies such as Direct Line, Churchill and NIG. It has advantages of owning companies, which are having lean operative model. Lean operative model includes internet and telephone. Hence, it reduces COR (Combined Operating Ratio), which leads to huge profit.

32. REGULATIONS

Since January 2005, insurance industry selling and administration has been regulated by the Financial Services Authority (FSA), as a result of the so-called Tiner reforms[33]. The new regulatory regime will place a cost burden on the industry over the next two to five years and these costs will fall disproportionately on smaller companies, traditionally the channel chosen both by the individual customer and the SME. It is also expected that many smaller companies would disappear over the next few years, usually by acquisition. According to Economist Intelligence Unit survey, majority (around 75%) of respondents expect compliance and regulation requirements to have a significant impact on their businesses. It is also expected that the impact of regulation could result in thinning down to a hard core of direct players, bancassure models and a periphery of other players[34].

UK is also going to implement Solvency II, a European Union-wide insurance directive. The directive is aimed at making Europe able to compete more effectively with emerging economies, such as

China[35]. The new rules will enable insurance companies to sharpen up, and limit, the amount of capital that they have to hold to cover their risks, should make it easier for insurers to get involved in cross-border merger and acquisitions. However, it is believed that it could trigger a wave of consolidation among big industry players.

33. CONCLUSION

Structural changes will take place. The changes can be attributed to regulatory changes and changing dynamics in the distribution, more specifically internet. Due to regulatory changes, especially Tiner reform, it is also expected that many smaller companies would disappear over the next few years, usually by acquisition.

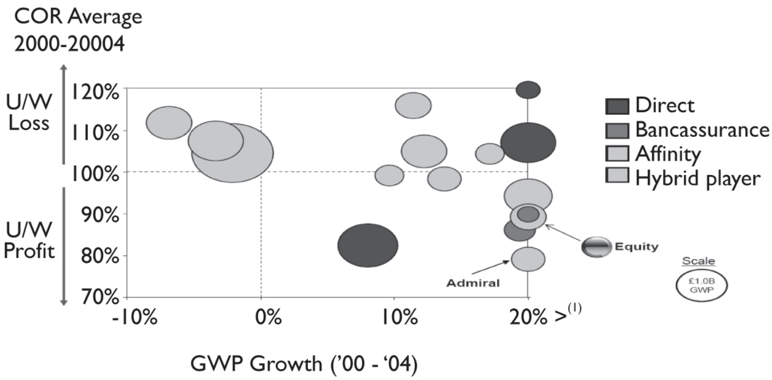
There will be limited merger & acquisitions among the larger companies. However, Broker's landscape is changing rapidly. They have undergone a substantial rationalization, with a number of important mergers and acquisitions among the leading companies. And, the trend seems to be increasing to support growth plans. It could even lead to unfair competition. To thwart the move of leading insurers, brokers are consolidating to safeguard their interest.

As far as growth of internet is concerned, it will grow modestly specially within personal line business. It is capitalizing on the opportunity provided by brokers, which are losing market share. In addition, their investment on advertising is further fuelling its growth. Despite the competitive state of the UK personal lines market, opportunities do exist for niche market players such as Admiral, Direct Line and Equity Insurance.

However, the extent to which the Internet will come to dominate depends on the extent to which one believes consumers will continue to want advice about the products they are purchasing. As consumers have become more sophisticated, they do not need advice, which can work as a catalyst for the growth of on-line sales.

The percentage of market quoted by aggregators should continue to grow rapidly. Price is key driver for the growth of aggregator website. However, the conversion rate of aggregators would remain be challenge. Despite these challenges, conversion rate is expected to grow modestly, about 10%, in the years to come. It is also gaining popularity with affinities, which will further fuel the growth.

FIGURE 24
UK PERSONAL MARKET INSURERS



Source: ABI statistics, Datamonitor, Historic syndicate 218 financial statements
(1) Companies on axis have growth greater than 20%.

The competitive challenges facing the industry are transforming attitudes to outsourcing. Insurance industry has to embrace new operating models to be more efficient. Economist survey also revealed that half of the respondents (36/72) to the survey believe they will need to adopt outsourcing over the next five years[36].

References

Mike Hawker, George Venardos, "Acquisition of equity insurance: A Specialist UK motor underwriter and distributor," http://www.iag.com.au/news/news_story/docs/20061204a.pdf, December 04, 2006.

Julian Lowe, "Current issues in personal lines, http://www.actuaries.org.uk/files/pdf/proceedings/cigi2007/Lowe.pdf.

"Structural change in the general insurance industry," Capita Insurance Services, http://www.capitainsuranceservices.co.uk/assets/documents/1651structuralchangeinthegeneralinsuranceindustry.pdf.

Arjan van Veen, Alex Chau, Ben Lin, "Insurance Australia Group - Broadening UK motor footprint – net 5%–7% EPS accretion," Credit Suisse, December 05, 2006.

Arjan van Veen, Jumana Nahhas, "Insurance Australia Group- UK motor: turnaround or false dawn?," Credit Suisse, August 01, 2007.

"United Kingdom- Non-Life (P&C)," AXCO, August, 2007.

"Channel Metrics: UK Motor Insurance," Finaccord, November 2005.

"The Future of UK Insurance," Business Insights, (p.2), http://www.globalbusinessinsights.com/content/rbfs0040m.pdf 2005.

"2007 World Insurance Report," London Roadshow," Capgemini, http://www.efma.com/wir07/pdf/WIR_Roadshow_London.pdf, Feb 07.

Andrew Power, "Channel surfing," Channel strategy (p.58), November 01, 2000.
Mathilde Jakobsen, "IAG: making a positive Equity move," http://www.insurance-business-review.com/article_feature.asp?guid=CF9B876A-151F-4A24-BB61-A40C10C52C26, December 08, 2006.

Notes

1. UK is the largest in Europe and the third largest in the world, accounting for 8.6% of total worldwide premium income. Source: "UK Insurance – Key Facts," Association of British Insurer, January, 2007.

2. Axa owns healthcare insurer Axa PPP healthcare. Zurich comprises a range of companies including Navigators and General, Zurich Professional and Zurich Municipal. Source: "UK Insurance – Key Facts," Association of British Insurer, January, 2007.

3. Royal Bank of Scotland group includes non-life companies Direct Line, Churchill, UKI Partnerships and NIG.

4. Halifax Bank of Scotland (HBOS) has Esure and First Alternative.

5. Figure is based on net written premium.

6. The percentage distribution of gross premium income between the major non-life classes in 2005. Source: "UK Insurance – Key Facts," Association of British Insurer, January, 2007.

7. Direct sales consists of internet and tele-sales.

8. It was established in the year 2006.

9. imarket is a trading platform enabling brokers and a panel of important insurers to trade more efficiently and cost-effectively; 12 types of commercial insurance are available.

10. AXCO.

11. Bancassurance includes banks and building societies (mortgage banks).

12. Royal Bank of Scotland Insurance is the second largest insurance provider in the UK. It covers over 5.1 million households and 8.1 million motorists. Source: AXCO.

13. A group of individuals defined mainly by their membership of some formal body.

14. Tesco is reported to have 1.4 million policies.

15. "Structural change in the general insurance industry," Capita Insurance Services, http://www.capitainsuranceservices.co.uk/assets/documents/1651structuralchangeinthegeneralinsuranceindustry.pdf.

16. In US and Australia, major insurance brands have not given in to quoting on aggregator.

17. Distinct from renewal sales.

18. Country like Australia doesn't provide an opportunity to capitalize on aggregator, as a distribution channel.

19. Admiral's confused.com controls around 60% of aggregator market.

20. Julian Lowe, "Current Issues in Personal lines," (p.8) http://www.actuaries.org.uk/files/pdf/proceedings/cigi2007/Lowe.pdf.

21. A leading managing general underwriter for international private medical insurance that offers expatriate benefits to individuals, small and medium enterprises, and large multinational clients around the world.

22. "Structural change in the general insurance industry," Capita Insurance Services, http://www.capitainsuranceservices.co.uk/assets/documents/1651structuralch

angeinthegeneralinsuranceindustry.pdf.

23. "Over 20% of brokers may be sold in next three years," Insurance Times, August 29, 2007.

24. Mathilde Jakobsen, "IAG: making a positive Equity move," http://www.insurance-business-review.com/article_feature.asp?guid=CF9B876A-151F-4A24-BB61-A40C10C52C26, December 08, 2006.

25. "AXA ties up two more broker acquisitions," Insurance Times, September 06, 2007.

26. "Groupama acquires majority stake in Lark Group," Insurance Times, August 30, 2007.

27. "Besieged buyout firms make £2bn by linking AA and Saga," Times, June 26, 2007.

28. "PHP acquires medical insurance business," Insurance Times, September 06, 2007.

29. Chase Templeton acquires Preferred Medical, http://www.preferredmedical.co.uk/news.php?id=18199097, July 03, 2007.

30. Distribution trend of the last 5 years (Till Sep., 2007) have been analyzed from the press release of various companies specific to General Insurance. Analysis doesn't include the AXA UK's 2003 press release because of unavailability.

31. RBS acquired Direct line insurance in the year 2002.

32. ASDA is a chain of supermarkets in the United Kingdom offering food, clothing and general merchandise products. Source: http://en.wikipedia.org/wiki/ASDA.

33. After the chief executive of the FSA, John Tiner.

34. Mike Hawker, George Venardos, "Acquisition of equity insurance: A Specialist UK motor underwriter and distributor," http://www.iag.com.au/news/news_story/docs/20061204a.pdf, December 04, 2006.

35. Miles Costello, "FSA to acquire new powers under European insurance directive," http://business.timesonline.co.uk/tol/business/industry_sectors/banking_and_finance/article2051168.ece.

36. Mike Hawker, George Venardos, "Acquisition of equity insurance: A Specialist UK motor underwriter and distributor," http://www.iag.com.au/news/news_story/docs/20061204a.pdf, December 04, 2006.