Staying ahead of the game
Mastering the Red Queen’s race in the Dutch insurance sector
September 2016
Executive summary

The Red Queen’s race, based on Alice in Wonderland, refers to the concept that keeping pace is not fast enough to win the race. It proposes that one must constantly adapt, fundamentally change and move twice as fast to gain advantage, but also to simply survive while pitted against an ever-evolving opposition in an ever-changing environment.

This metaphor nicely applies to the current state of the Dutch insurance industry. The industry is currently in the midst of a transition with an uncertain outcome. In previous years, overall GWP has been able to grow due to fiscal incentives, regulatory protective barriers and a favourable economic climate. As a result, there was little necessity for a focus on achieving operational efficiencies or innovation. Yet, from 2008, the value of new business has been declining. Changes in legislation, a changing distribution structure, changing consumer behaviour, a low interest rate, increased life expectancy and a combined ratio in Property and Casualty (P&C) of over 100, have resulted in a ‘perfect storm’ for the Dutch insurance industry in the last 2 years, requiring a fundamental transition. Dutch industry players must reinvent themselves and assess their desired contribution in the insurance ecosystem.

Learning from other industries which have travelled a similar path before, and translating these insights to the dynamics of the Dutch insurance industry, provides for a healthy wake-up call. So far, the insurance industry has been hesitant to make drastic strategic changes. Most insurers have followed roughly the same path—one that combines running a closed individual life book with incremental cost-cutting initiatives to counter the decreasing life books and the low profit margins in the P&C insurance market.

Deloitte believes that new emerging trends offer opportunities for insurers to transform the industry. Some of these trends are industry specific, where others are crossing over from other industries. This report identifies some drivers and trends with game-changing potential.
The sharing economy creates a new (insurance) market.
New platforms simplify the renting or sharing of products or services, reducing the need for ownership and consequently changing insurance needs. Customers’ desire to receive flexible insurance products for specific risks at particular times is driving the growing popularity of such flexible products. Insurance offerings could move from annual (automatic) insurance subscriptions to on-demand insurance. The rise of the sharing economy is exemplified by platforms such as Peerby.nl, Airbnb, Greenwheels and BlaBlaCar, and is mirrored in the insurance sector by a platform such as Trov.

Artificial intelligence, robotisation and blockchain allow for radical cost reduction and participation in value networks.
Emerging new technologies, including artificial intelligence, robotisation and blockchain—currently being tested by insurers and related industries—are expected to pivot in the near future. Software will be able to complete multiple tasks which at present can only be performed by humans, allowing insurance organisations to reduce the cost per policy, without heavy investments in IT architecture. Artificial intelligence — in combination with big data analyses — will allow for detailed individual financial planning and wealth management. This robotised advice could become of a higher added value than current advice provided by brokers or wealth management advisors. Blockchain provides the opportunity to establish new ecosystems, potentially connecting social media data, manufacturers and insurers in a seamless manner.

Cyber and climate risks offer opportunities for high-margin niche products.
New risks are emerging and existing risks, such as rapid climate change and digitalisation, are increasing. Customers will increasingly be confronted with these emerging risks. Insurers who learn to provide their customers with ease of mind by balancing efficient expert advice on avoiding risks, and limiting the impact (prevention) with solid after-care will likely make the difference. These new opportunities come with good margins but require investment into the development of complex products with high uncertainty.

Sensoring and analytics will help to better understand and service clients.
As the cost of sensors decreases, more and more sensors are being installed and there’s a huge increase in available data. This data allows insurers to offer more relevant packages based on actual use and behaviour, rather than on averaged statistics. In addition to better-fitting insurance packages, customers can benefit from the system by earning (in)visible rewards. For example, by sharing living data with an insurer and meeting weekly fitness benchmarks, users can earn discounts on products.

Blurring industry boundaries expand the insurer’s playing field.
Regulatory changes have been blurring the traditional boundaries in the life insurance sector between pension funds, banks, asset managers and insurers. The insurance industry is transforming from a spread-based to a fee-based industry. Boundaries are also blurring in the P&C sector, as access to data is not restricted to insurers anymore. The developments offer opportunities for insurers to expand their activities beyond their traditional industry boundaries. To disrupt or be disrupted seems to be the challenge facing insurers.
Now is the time to change. Insurers have the opportunity to ignite radical cost reductions or build new growth engines. The much needed earnings—while still available—of the closed books can be leveraged to fund the required exploration of new pockets of growth. A courageous, albeit careful, transformation is needed to ensure a sustainable future for Dutch insurance industry players.

If insurers dare to make these courageous choices and execute them well, we believe that the aforementioned trends will help insurers to reinvent themselves and grow towards a new future-proof business model. Insurers will have to focus and grow in areas where they can contribute value, be the best and/or have sufficient scale. By letting go of full control of the total value chain, radical cost reductions can be achieved while services will be improved.

Although it might look appealing to continue to optimise profits for the short term, only far-reaching and even disruptive innovation can secure a sustainable business model for the long term. And because technology does not obey national boundaries, it may be within reach for the Dutch industry to reclaim its role on the international stage, provided it can execute its focused strategy with vision.

This report identifies a number of strategic areas in the Life and P&C space where we think shareholder value can be created. This will happen where organisations work together and create new value networks and new propositions relevant to the consumer, instead of competing over the same pieces of the pie.

The report focuses on the Dutch situation. Although the fundamental risks are universal, insurance has been an industry that is typically defined by local characteristics, e.g. legislation and fiscal regulation, historical background and cultural differences. Many of the trends and developments described here are of a global nature, but their impact can be different from one country to another. The conclusions and opinions in this report must be read from a specific Dutch perspective.

We welcome your feedback and look forward to discussing our views on the future of the Dutch insurance industry with you.
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Introduction

The world is changing at a faster pace than ever before. Household retail brands present in downtown shopping centres have been replaced by online retailers operating omni-channel concepts. Renewable energy technologies are challenging the energy sector and the sharing economy is shaking up sectors ranging from taxis to hotels, forcing entire cities to rethink their infrastructure.

The pace of ‘creative destruction’—a term introduced by economist Joseph Schumpeter to describe how creation of the new destroys the old—seems not only to be accelerating, but also getting stronger.

At first sight, both the Dutch life insurance sector and the P&C insurance sector seem to be weathering the storm. While these two sectors are also changing intrinsically, most of the recent changes are a result of changing regulations. Regulatory changes have left their mark on the Dutch life insurance sector such as the introduction of bank savings products (Banksparen), the premium pension institutions (Premiepensioeninstelling, PPI), for example, or the ban on commissions on complex insurance products. Combined with the low interest rate environment the earning potential of the Dutch life insurance industry has significantly deteriorated over the last 2 years.

We believe that the insurance landscape will see further drastic disruption in the near future, from already existing sources of change—ranging from technological developments to changing consumer behaviour. These trends will amplify each other and have the potential to fundamentally change the P&C and Dutch life insurance sectors in the near future.

Six large players have dominated the insurance sector for the last decade, providing similar products and all operating across (and sometimes owning) the entire insurance value chain. We believe the next decade will gradually show a different picture. The long list of transitions threatens the continuity and growth of established insurers. At the same time, these changes offer opportunities and rewards for those companies that are able to differentiate and adapt. The game – and therefore the playing field – however is likely to change significantly.

Deloitte’s insurance practice helps both life and P&C insurers deal with challenges along the way. Our experience and insights – complemented by a series of interviews with thought leaders in the insurance industry – are presented in this booklet; our vision on the future of the Dutch insurance sector.

“We hope you find this booklet thought-provoking and helpful in riding the waves of change”.

Marco Vet, Partner,
Insurance Leader Deloitte Netherlands
“Although change is part of life, insurers are now facing a perfect storm”

Thijs van Woerden, Division Director Insurance Supervision, DNB
A perfect storm

Although change is of all times, the pace of change is higher than ever before. Both the life and P&C sector have seen transitions brought on by regulatory, economic and technological changes in recent years.

Until 2006, the life insurance sector was at an artificial high. Sales were driven by the fiscally attractive treatment of products, high asset returns and a sales push from intermediaries. The six largest players that dominate the life sector focused on growth rather than on efficiency or innovation. Then, from 2006, a number of developments started to change the life insurance industry.

Aforementioned developments have led to an annual decrease of premium income of 7% between 2008 and 2014. While group life premiums remained relatively stable, new individual life business decreased by 18% annually – from EUR 1.7 billion in 2006 to EUR 0.3 billion in 2015.
Leading towards a perfect storm for Dutch life insurers

2006: Start of media attention around the miss-selling of unit-linked policies;
2007: Introduction of the Dutch Financial Supervision Act (WFT) put additional pressure on financial institutions to take their customers’ interests into account (‘zorgplicht’);
2008: Introduction of bank savings products provided an alternative for the fiscally attractive pillar three savings using insurance products. Coupled with a drop in reputation, bank savings took over a large part of the insurance business. Term insurance was relatively unaffected, as banks are not able to offer this. Furthermore, insurers massively started their own insurance business. Term insurance was relatively unaffected, as banks are not able to offer this.
2010: Start of low interest rate environment. This has resulted in i) lower profitability of life insurers and ii) a further decrease in sales of saving products as lower returns on savings had to be offered to consumers;
2011: Introduction of the premium pension institution (PPI). This offered an alternative for defined contribution (DC) insured group life products, increasing competition on DC products. All large insurers participated in this new opportunity to retain volumes;
2013: Ban on interest-only mortgages. As all new mortgages require full redemption within 30 years, the demand for savings products on mortgages has vanished;
2013: The ban on commission to intermediaries for complex insurance products led to a decrease in the push of insurance products;
2014/
2015: A decrease in the accrual rate for pillar two group life products immediately impacted the group life insurance business;
2016: The introduction of Solvency II has impacted the regulatory burden for insurers over the last years and will continue to do so. Furthermore, the introduction of risk-based capital has resulted in further pressure on insurance products with guarantees;
2016: The introduction of the General Pension Fund (APF) offered an alternative for defined benefit (DB) insured group life products.

New individual life business has been decreasing by 18% per year

Annual premium equivalent (APE) new business individual life (€ bln1).

Individual life has been on an artificial high
With little new business coming in, most insurers separated their life books and now run these as ‘closed books’. In the current situation of ongoing decline of interest results, cost efficiency has become a must. As individual life business dries up, Dutch insurers have increased their focus on the P&C business. This sector has been less affected by regulatory forces but all the more by increased digitalisation, resulting in a strong increase in internet sales and the use of aggregators. Strong price competition has resulted in an average GWP decrease—2% CAGR as of 2008—and an increase of the combined ratio. Although cyclical behaviour of combined ratios is not new to the P&C business, this time, insurers face the additional challenge of operating in a low interest rate environment, making it difficult to compensate the high combined ratios in new business.

Now that markets have changed, insurers face a critical point where they have to decide how they can use their capabilities to win the race.

“The rise of internet sales, aggregators, peer-to-peer insurance and authorised agents have changed the P&C market”

Ton de Bruin, Advisor innovation, Verbond van Verzekeraars

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**P&C premium income is declining...**

GWP P&C excluding disability end note 2.

![Graph showing declining P&C premium income](image)

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**... and profit margins are eroding**

Gross combined ratio P&C, excluding disability and profit margin, including one year risk free rate 2/3.

![Graph showing eroding profit margins](image)

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“All insurers are currently doing is stealing pieces of the same pie.”

Ingrid de Graaf, Board member, Delta Lloyd
Staying ahead of the game | To disrupt or to be disrupted

New trends are always emerging and often have an impact on business. Some trends start in one industry and cross over to others, while other trends are industry specific. We highlight five key trends that we feel will have a large impact on the Dutch insurance industry: the sharing economy; robotisation and blockchain; climate change and cyber risk; sensoring and analytics and the blurring lines between industries.

The sharing economy creates a new (insurance) market
The sharing economy, also referred to as Peer2Peer (P2P) economy is projected to grow from $15 billion in 2013 to $335 billion in 2025. As P2P transactions entail risks (e.g. damage, theft or malfunction), one or both sides in the potential transaction could require insurance. On-demand insurance products do not have a pre-defined contract period or cancellation term. Turning insurance on and off, irrespective of time and place, is at the core of this concept. These insurance products have a limited duration and make use of mobile platforms. Customers' desire to receive flexible insurance products for specific risks at particular times is driving their growing popularity. At the same time, insurers looking to increase penetration in existing markets and access new, underserved, or niche markets, also see the possibilities that on-demand has to offer.

Newcom research published interesting awareness and usage figures about some P2P initiatives in the Netherlands, which illustrate that the P2P economy is already serious business in the Netherlands.
Several Dutch insurers have entered this market including Centraal Beheer Achmea, which is developing an optional insurance guarantee for Peerby transactions, and Allianz, which is providing insurance coverage for Snappcar transactions. As the market for P2P transactions is expected to grow twenty-fold in the next few years, we expect the P2P insurance-related market to do the same. It’s a market representing enormous potential for those insurers that can master the different dynamics of this new market.

“There will be a completely new playing field”

Marco Keim, CEO, Aegon NL
Artificial intelligence, robotisation and blockchain allow for radical cost reduction and participation in value networks

Emerging new technologies, including robotisation and blockchain, currently being tested by insurers and related industries, are expected to pivot in the near future.

The first focus for insurers when considering the application of robotics tends to be radical cost reduction. Process robotics, for example, deliver a compelling business case for the administration of the life insurance closed book. These closed book administrations tend to be coded in outdated software systems. Software robotics avoid the need for expensive IT integration, instead conducting multiple manual interactions using easy to programme software. This will replace human labour and reduce the cost per policy.

Blockchain technology has moved beyond the experimental phase and is likely to drive radical cost reductions but also improve customer experience and lead to breakthrough innovations for the insurance industry. The three important applications of blockchain (smart contracts, asset registry and cryptocurrency) allow for several relevant use cases for the insurance industry such as:

- **Automated assurance and accounting** allowing for example for transparency of accounting or automation of regulatory reporting
- **Document digitisation** allowing for a reduction in administrative and system costs e.g. when managing (part of) a policy administration in blockchain
- **Digital identity** schemes that aggregate user information across a variety of sources built using a blockchain protocol (e.g., social media, birth/death registries, State ID, biometric data, health records etc.). This can reduce identity and claim fraud or improve the customer experience by simplifying the required Know-Your-Customer process.
- **Improved claim administration.** Assuming systematic inputs from sources such as death registries, smart contracts could be used to administer automatic pay-outs from certain insurance products.
Examples of blockchain use cases in insurance

- Mutual (P2P) insurance based on consensus (or: crowd insurance)
- Improve KYC process by introducing ID-token, certificate or KYC approval
- Automate & simplify life insurance by using smart contracts
- Store and analyse personal life health info on blockchain
- Car insurance: register car and usage data to personalise premium and predict behaviour
- ‘Smart-claiming’: Optimise and automate claiming process (e.g. when missing a flight)
- Using prediction market (Augur) to collect actuarial data
- Real-time remote auditing of companies to ensure solvency
- Tracking valuables (diamonds, art) on blockchain to secure ownership and counterfeiting

“The blockchain protocol threatens to disintermediate almost every process in financial services.”

World Economic Forum

In the not so distant future, artificial intelligence – in combination with big data analyses – will allow for detailed individual financial planning and wealth management. This is potentially better than that currently conducted by brokers or wealth management advisors. Consumers will gain access to investment portfolios and analyses previously only available to large pension funds at little to no costs. Proactive recommendations and alerts on the full financial portfolio will allow consumers to optimise their insurance and retirement savings throughout their different stages of life.

We believe that insurers who succeed in introducing these innovations will be able to lower their cost position significantly. Moreover, they might reach new markets or consumer segments. Combining a wealth of data in the form of a digital ledger, blockchain and artificial intelligence also facilitate new partnerships in ecosystems where insurance is a derived demand, after an initial pull from another product. The insurance industry will therefore likely move from a value chain to a value network. As such, blockchain allows for the insurance of product usage, rather than product ownership. E.g. why not pass on the car insurance to a new owner when the car is sold via eBay, with a blockchain clearly indicating the related insurance coverage to the new owner?
Cyber and climate risks offer opportunities for high-margin niche products
We see two major trends that lead to increasing risk. One trend is climate change. The other is the development of connected technologies, or cyberspace. These trends provide opportunities for developing new and existing products at higher margins, but seizing these opportunities to their full potential requires a new and different approach.

Climate change leads to an increased likelihood and intensity of extreme events, such as hailstorms, flooding and drought, which will impact statistics on a wide range of products, while simultaneously increasing the demand for added protection. Scientists have warned of spill-over effects from climate change into other areas, ranging from ecological to economic changes. It is not a new trend and is predicted to persist for decades to come.

The insurance opportunities relating to climate change include the development of innovative niche products, the greater impact of prevention, increased demand for existing protection products as well as better pricing and selection of risks that are indirectly related to climate change. Severe losses in the Dutch insurance industry, due to recent rain- and hailstorms are examples of the relevance and magnitude of climate change in the Netherlands.

Examples of innovative products include insurance for green buildings to maintain their climate neutrality status or guaranteed returns for solar panels. The demand for existing insurance products, that compensate losses from natural catastrophes, is expected to rise, despite rising premiums. This means that there is more potential for impact from prevention, by making use of the insight into risk that insurers require anyway. And, prevention has a double impact: it makes clients more risk aware, further increasing demand, while at the same time reducing the impact of the catastrophe. Finally, understanding the impact of climate change on, for example, mortality rates (likely to increase for elderly people, due to more frequent heatwaves) or accident rates will enable better risk pricing and selection.

“Climate change creates both risks and opportunities for the insurance industry”

Thijs van Woerden, Division Director Insurance Supervision, DNB

Natural catastrophes have been increasing rapidly over the last 35 years
Number of catastrophic incidents per year\(^6\).
For cyber risk, we see a similar pattern. The increasingly rapid entry into cyberspace has already led to a significant increase in operational risk and the risk of cyberattacks. Further technological innovations, such as the internet of things and artificial intelligence, will likely strengthen this trend, possibly further emphasised by the emergence of new and unforeseen risks.

The opportunities which cyber risk brings for the insurance industry again fall into four categories: new products, higher impact from prevention as well as increased demand and better pricing and risk selection for existing products. Cyber insurance as a product has been around for 17 years, and over the last years it has seen strong growth, with healthy margins in the US. This is likely to continue on the European continent, given the persistent threats and incidents.

Traditional insurance products will increasingly involve a cyber component. Most obvious are the insurance against payments fraud or corporate liability insurance, while for some other products like car insurance or health insurance this effect is looming, yet less obvious (think of car-jacking by wire, for example, or the required mass-replacement of cyber-vulnerable implants). Understanding these effects can be vital, because historic risk trends can be completely disrupted if unforeseen cyber vulnerabilities lead to mass claims.

Customers will increasingly be confronted with these emerging risks. So, insurers who learn to provide their customers with ease of mind by balancing efficient expert advice on avoiding risks, and limiting the impact (prevention) with solid after-care will likely make the difference. These new opportunities come with high value but require investment into the development of complex products with high uncertainty. In the long term, insurers that seize this opportunity will gain a significant advantage, also on traditional products, as these will increasingly contain exposure to the new types of risk.

**Expected growth of cyber insurance market until 2020**

Forecast cyber insurance (€ billion).
“Although we are currently behind, cyber insurance has the potential to become the new Dutch export product”

Leo de Boer, Managing director Verbond van Verzekeraars
Sensoring and analytics will help to better understand and service clients
New technologies can help insurance companies microsegment their customer base, personalise insurance policies and even influence customer behaviour. Wearable and mobile technologies could play a major role in personalised insurance. Wearables offer a data-driven way to understand customer lifestyle and health habits. This data allows insurers to offer more relevant packages based on actual use and behaviour, rather than on averaged statistics.

In addition to better fitting insurance packages, customers can benefit from the system by earning (in)tangible rewards. For example, by sharing living data with an insurer and meeting weekly fitness benchmarks, users can earn discounts on products. The marriage of data with insurance in the context of wearables is thus creating a beneficial situation for both the provider and customer. Another application example is in the automotive industry, measuring driving behaviour.

Traditional risk-pool based products and pricing are based on actuarial risk assessment analysis and algorithms which are driven by statistics (e.g. life expectancy tables, claims history) underpinned by a limited number of variables leading to average risks. With more data points and real-time analysis, the probabilities of risk can be made more accurate, especially using advanced analytics and AI-like machine learning. This leads to the transition from classic ‘top-down’ statistical analysis using static models to predictive ‘bottom-up’ analytics using dynamic and non-linear models, supporting house-by-house, car-by-car and person-by-person models.

Besides improving risk models, the continuous stream of data enables insurers to create new value-adding experiences for customers. For example in some countries, insurers have teamed up with the national police to inform consumers about increased burglary risk in their neighborhood, moving from compensation to prevention.

The abundance of data enables insurers to apply (big) data analytics. The value created is beyond improvement in revenues (via better pricing), new revenue streams (new propositions) or improved combined ratios (due to lower claim rates). The ultimate benefit will be for the consumer and the society at large. The consumer will receive a tailored offering, less hassle and will experience fewer personal disasters due to e.g. better prevention. The society at large will become safer and better prepared for hazardous events or - as some insurer policies currently state - “acts of God.”
“The APF market will be competitive and low margin; scale in asset management and administration is key.”

Jan Willem Knoll, former Equity Analyst ABN AMRO.

**Blurring industry boundaries expand the insurer’s playing field**

Regulatory changes have been blurring the traditional boundaries between pension funds, banks, asset managers and insurers in the life insurance sector. This blurring is transforming the insurance industry from a spread-based to a fee-based industry. Besides this, technologically-driven companies are increasingly able to interfere with traditional intermediaries in the advice and sale of insurance policies. Insurers face the risk of being outrun or outdated by players that used to play in another game now cherry picking in the insurance industry.

Boundaries are also blurring in the P&C sector, as access to data is not restricted to insurers anymore. Car manufacturers, mobile phone operators and insurers all potentially know where and how consumers are driving. Usage Based Car Insurance (UBI) is the logical result. Platforms are created offering added benefits to consumers in the form of reduced insurance rates or discounts on relevant restaurants on their route to work.

On the other hand, the developments offer opportunities for insurers to expand their activities beyond their traditional industry boundaries. To disrupt or to be disrupted seems to be the challenge facing insurers.

**Regulatory changes blurring industry boundaries (life insurance example)**
The most recent development is the introduction of the General Pension Fund (algemeen pensioenfonds, APF). An APF is allowed to manage multiple pension schemes, as long as these are separated (i.e. ring-fenced).

The APF brings additional competition to pension schemes that would traditionally be in the domain of the insurer. On the other hand, the APF is an opportunity to expand the market reach of insurers. Because pension schemes do not offer the guaranteed benefit an insurer can offer, pension funds with low solvency ratios that are not able to transfer to an insurer are able to transfer to an APF. Most large insurers have already established an APF or are in the process of setting up one. Note that an APF is an independent non-profit organisation, in which insurers can only make profit by offering service with a margin to the APF.

We expect mainly large schemes, company or industry-wide pension funds to transfer to an APF. Smaller schemes would first need to combine with other schemes with comparable characteristics to create a large enough pool to share risks. This barrier makes the APF less attractive for smaller pension schemes, leaving these smaller schemes the main providers of group life insurance in the more traditional way.

We have already seen that the introduction of bank savings and the PPI, combined with the shift from DB to DC, are changing the insurance business model from a traditional spread model, where insurers take over risks and make money by locking in spread between their assets and liabilities, to a fee model for new business. A fee-based business model, however, requires a different skill set in managing the insurance operation and profit & loss account, as well as a different valuation of the earnings potential of insurers.

We expect that the introduction of the APF will take another big chunk out of the traditional spread business, leaving only a small proportion of the portfolio (e.g. term insurance, some annuities and a small piece of DB pension for small companies) as traditional insurance products.
Although the insurance market is changing, we believe that consumers and companies will fundamentally continue to need to transfer risk they are not willing to bear individually. Consumers will continue to save money and protect wealth to secure their financial future. We therefore expect that there will always be a market for providing insurance services to cover this demand. Also, the (data) basis which insurers have built up over the years provides an excellent starting position for launching new business models. The trends mentioned above will impact the insurance sector on multiple levels.
Individual life limited to term insurance
As long as there is a low interest environment, new individual life business will remain limited to term insurance and to a lesser extent annuities (as they are impacted by competition).

Group life becoming fee-managed business
We see insured group life becoming a predominantly fee-managed business, migrating towards digital platforms. Combined with new technology – such as robotisation and blockchain that allows the offerings of new, more relevant and lower cost investment options for consumers – the traditional business models where insurers are making large profits on spreads on their life insurance products will disappear.

Expansion towards broader spectrum of products
Blurring boundaries will allow insurers a further expansion of their traditional insurance business towards a broader spectrum of products. Companies that choose this direction will have to offer something more than the established parties are offering in order to compete.

Improve combined ratio or exit
The changing world will also leave its mark in the P&C business. Insurers unable to adapt to the new reality will end up with rapidly declining market shares and/or low to negative profit margins as pricing strategies no longer apply to the new situation.

Customer data analytics as (new) core competency
The sharing economy will lead to different risk classifications and sensoring will provide information to customers that will allow them to better understand what they actually need to insure and to what costs. Insurers who can use these developments to their advantage will be able to create new business models for new markets, using data from sensoring to better understand their customers and the risks that they are exposed to. New complex risks such as cyber and climate risks also offer new markets, with potentially high margins.

Radical cost reduction for closed life books
If managed well, there is still potential for attractive profits on old, closed life books. Robotisation, blockchain, direct distribution and communication and reducing overheads will deliver the capability to migrate to a lower cost base.

Resizing to digital reality
When insurers make courageous decisions on the adoption of new technology the organisation itself also ought to be reassessed. In recent years many Dutch insurance organisations have shrunk and FTE reductions of 25% or more have allowed organisations to adapt to the new reality. However, often the recent reorganisations are merely an adjustment to a new financial reality, not the new digital reality. New technology, as described in this report, will require organisations to align their culture, talent management, processes and business models to achieve long term digital success.

8 out of 10 of the interviewed experts believe at least two of the big six Dutch insurers will disappear in the near future

9 out of 10 of the interviewed experts do not believe that Dutch insurers are well prepared for the future
For new traditional business, high profits appear to be something of the past. However, with products requiring low capital, there is still the potential for high returns on equity. A redefinition of the insurance industry by insurers is required to ensure a sustainable industry in the near future and prevent other industries from cherry picking business away from the insurance industry.

Hesitant response in the market
In our perception, the insurance industry has been hesitant to make drastic strategic changes. Most insurers have followed roughly the same path, combining running a closed life book, incremental cost-cutting initiatives to counter the decreasing life books and low profit margins in the P&C market. Some insurers have introduced dynamic pricing to strengthen the combined ratio for P&C propositions. And, life insurers are trying to replace lost insurance business by competing in bank savings, and aim to retain balance sheet volumes by running a PPI and APF.

Clear strategic changes are needed to transform the highly competitive P&C market to a high margin market that offers new innovative products, responding to the needs of the customer of tomorrow. By building on old business models, insurers are investing in an industry of the past. Now insurers must take lead and adapt to the new, often digital, reality.

Although insurers do not have the best track record in showing agility, most of the industry experts we interviewed believe that established insurers will continue to dominate the insurance industry. The general perception is that insurers are slow in their digital transformation (slower than the banking industry, for example). Yet, due to high entry barriers and the security offered to consumers by established brands, new entrants will initially only achieve a niche position in the insurance market.

Opportunities for future-proof business models
We believe the trends mentioned above will offer opportunities for insurers if they make the right choices and execute them well. Insurers need to choose where they want to play and how they want to win. We see four different strategies that, if executed well, will create shareholder value. They focus on areas where different companies work together and create new ecosystems, rather than competing over the same pieces of the pie.

Where strategies based on optimising the business could secure annual profits in the short term, we believe that only a (disruptive) innovative approach can secure a sustainable business model in the long run.

The four strategies are defined to inspire, but are not intended as exclusive choices. At the end of the day, each insurance organisation will need to tailor the strategy to its ambition. Considering the size of many Dutch insurance organisation a portfolio approach, where different businesses opt for a different strategy, is also imaginable.

“To survive in the future, insurers will have to invest in new business models”
Marco Keim, CEO Aegon NL

“The main challenge for insurance companies is execution of strategy in a difficult environment”.
Duncan Russel, Head of Strategy NN
### Strategic focus areas

**Front end versus back end**

Focusing on the front end of the insurance value chain means enhancing customer relevance and improving the customer experience. Flexibility in product offerings is created by partnering with, or outsourcing to, companies that focus on the back end components.

On the back end of the value chain, insurers can use technology such as robotisation and blockchain to create competitive efficiency advantages.

**Sustainable versus disruptive innovation**

In any case, innovation will be essential for keeping up with market developments. As a minimum requirement, insurers should invest in sustainable, flexible digital platforms that allow cost-efficient service offerings. In order to remain competitive in the long run, insurers should make innovation part of their business model such that they will be able to disrupt existing business models. By constantly looking for new solutions for existing problems, insurers will be able to create a high-margin business model. Innovation and managing the innovation portfolio therefore becomes a (new) competency on the basis of which insurers transform their business.

Truly disruptive innovation focuses on reinventing the insurance business and reaching out to new markets or new segments that are currently underserved. Disruptive innovation includes taking risks and possibly cannibalising existing business or distribution partnerships.

“The benefit of having all of the parts of the value chain together is decreasing”

Danny van der Eijk, Former Board Member Achmea

“Insurers have to make a choice. They try to do everything, but do not have enough scale”

Jan Nooitgedagt, President Supervisory Board VIVAT

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**Strategic focus areas**

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Strategy 1. Blurred industry boundaries enable insurers to apply a ‘platform proposition’ strategy

Key characteristics of a platform proposition strategy:

- Strong brand
- Frequent customer contact and good service as a priority
- Resource orchestration (instead of resource control)
- Focus on network value
- Facilitate interactions and focus on customer product density
- Potentially outsourcing parts of the back end value chain and/or transferring undesired risks
- Platform access and governance

Trends such as the blurring of industry boundaries enable companies to sell products beyond the limitations seen when operating in a single ‘pipeline’ industry. This allows insurers to offer the full suite of products within a certain consumer domain (such as living, income or transportation) and provide added value by inviting other relevant participants on the platform. This potentially results in sub-optimal diversification in the insurance book. The insurer will have to mitigate this inefficiency by transferring risks to third parties, rather than putting a hold on sales of certain products.

Being recognised in certain consumer domains will enable insurers to bind clients to their business and use client information to increase the relevance and value to platform participants. Knowing the customer and targeted marketing, for example by using data analytics, will be key to maximising customer engagement, customer product density and ultimately revenues and profitability.

Strategy 2. Consolidators can provide services to other insurers

Key characteristics of a consolidator strategy:

- Flexible IT structure
- Lean and efficient administration and claims handling office
- Optimised capital structure
- Scale primarily as result of consolidation rather than own sale of new business
- Efficient system can potentially be used to provide administration and claims handling services to other insurers
- Focus on low cost per policy

The decreasing core life insurance market means that costs per policy will increase if insurers are not able to keep cost-cutting measures in line with the run off of the insurance book.

The operating systems of Dutch insurers are based on a large and growing market. But with new business in the individual life market close to zero, insurers have been setting up cost-reduction programmes and created closed books for their (individual) life books. With the ongoing transition from DB to DC pensions, partly operated by PPIs, lower pension accrual rates and the introduction of the APF, insured pension books will likely follow the same pattern.

So far, insurers have been hesitant to buy or sell closed life books for a multitude of reasons, including reputational risk. The new developments in the pension market, however, and a further run-off of the individual life books, are increasing the pressure to find a long-term solution on closed books.
This may therefore be a good moment to divest and focus on new business, or to further invest in efficiently-running closed books. Setting up a flexible IT landscape, lean and efficient administration and claims handling office is a first investment in the consolidator strategy. Optimising the balance sheet and capital structure in line with the new Solvency II regulations will, if executed well, result in significant increases in the return on capital. Furthermore, an efficient closed book machine can create a sustainable fee business in the long run by providing administration and claims handling for PPIs, APFs and insurers that choose to outsource this.

“Culture in the insurance sector is focused on not making mistakes rather than on innovating”

Danny van der Eijk, Former Board Member Achmea

Without regulatory push, disruptive innovation is the only way to return to high-margin business

Strategy 3. Innovation-driven expansion
Key characteristics of a strategy focused on expansion through innovation:

- Innovation as part of company culture
- Venture capital approach, risk appetite
- Long-term vision, ability to start small and accelerate growth (potentially international) when successful
- Focus on how capabilities can be used to come up with new products, rather than building on existing ideas
- Withdrawal from red ocean markets with standardised products
- Use technological advances to create new market space
- Outsource non-core competencies

Trends such as blockchain, sensoring and analytics, sharing economies, increasing cyber and climate risks offer opportunities to companies that are able to take a leap and truly innovate. Daring to let go of traditional products that compete in existing highly competitive markets (so-called ‘red oceans’) with low margins and uncovering new terrain with little competition (so-called ‘blue oceans’).

Cyber insurance could be one of these blue ocean products. The first Dutch insurer to develop a well-priced cyber insurance product would be able to conquer a large share of the market and reap significant profits. And, this opportunity is not limited to Dutch borders, because technology doesn’t obey national frontiers but rather facilitates expansion into new markets.
Strategy 4. Innovation-driven efficiency

Key characteristics of a strategy focused on efficiency though innovation:

• Focus on closed book management
• Use technology, such as robotisation, blockchain and artificial intelligence to automate business processes
• Highly flexible and scalable IT systems
• Minimal FTEs per product

A fourth strategy is to redesign the closed book to minimise the need for human input. Using robotisation to execute business processes will enable radical cost reductions in personnel. Artificial intelligence and blockchain will take on a large part of the consumer interaction, only leaving special cases, IT supervision and maintenance to humans.

This IT expertise combined with innovative, efficient and most important of all, scalable solutions can be used to provide services to other companies that are not able to service policies at such low costs. Customers could be companies in the insurance sector and possibly outside the Netherlands, creating economies of scale that will more than make up for initial investments.

“The time-to-market for developing new products is much too long”

Jan Nooitgedagt, President Supervisory Board VIVAT
The insurance landscape has changed and is expected to continue to change. Dutch insurers should explore their options, reinvent themselves and undergo a digital transformation in order to secure long-term sustainable profitability.

Insurers will need to stop competing over the same pie. A pie which is only getting smaller if you do not redefine the boundaries. Insurers should consider new opportunities offered by blurring industry boundaries or by the new disruptive propositions which can expand territory. Good first steps are to look beyond the traditional insurance pipeline and identify where in the broader value network the insurer wants to play, after which the requirements to win in the chosen market can be defined.

Ongoing investment into smarter IT and digital systems, and a continuous focus on innovation will have to be part of any strategy. By outsourcing elements of the traditional value chain, insurers can increase agility and limit high investments in old and rigid pipelines that were designed for the old world.

However, as the insurance industry enters new territories, the transformation needs to be done carefully, leveraging the much needed benefits – while still available – of the closed books to ensure a sustainable future for Dutch insurance industry players. Learning from other industries who have travelled a similar path before and translating these insights to the dynamics of the Dutch insurance industry provides for a healthy wake up call.

The future is definitely not just a gloomy one. There is and will be a need for protection against risks, and savings for old age. But, just as in evolution, the relevant market players of tomorrow are the ones that find the best ways to adapt to the changes around them.
Contacts

Marco Vet
Partner
Insurance Leader Deloitte Netherlands
mvet@deloitte.nl

Robert Collignon
Director
Digital Strategy and Insurance Industry
rcollignon@deloitte.nl

Zeno Deurvorst
Senior Manager
Financial Risk Management and Capital
Optimisation Insurance
zdeurvorst@deloitte.nl
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Endnotes


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