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# The Untouchables

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**The views expressed in this article are solely those of the author and do not reflect the views of either his employer or the Society of Actuaries.**

*“Uber, the world’s largest taxi company, owns no vehicles. Facebook, the world’s most popular media owner, creates no content. Alibaba, the most valuable retailer, has no inventory. And Airbnb, the world’s largest accommodation provider, owns no real estate. Something interesting is happening.”* — Tom Goodwin, senior vice president of strategy and innovation for Havas Media North America.

Front cover from the Economist lauded the four consumer Internet giants that are engaged in combat which is worthy of a Game of Thrones end of season episode. They were named as Facebook, Google, Apple and Amazon. It was quite amazing to think that House Microsoft did not even make the cut. The innovation war does not allow anyone to rest on one’s laurels.

Speaking of innovation, In February 1688, Edward Lloyd’s Coffee House in Tower Street was referred to for the very first time in the London Gazette. Was this really the last time that reinsurers had an innovative idea? If it was, then Edward still lost points for not leveraging the idea and starting a Starbucks-like coffee chain across the British empire.

I believe we can divide the new Internet-driven technologies and businesses that are challenging existing businesses into two categories: those that sit comfortably next to existing companies, such as Amazon and Wal-Mart; and those that have largely wiped out their competitors, such as online music streaming services. (I was made to feel very antediluvian when I recently learnt that major produce CDs, opting for digital-only music sales.)

Why have traditional reinsurers not been materially changed or challenged by the new risk transfer techniques that are backed by venture capital or private equity funds? Is there really an impregnable moat that protects our industry from change? Or, could it be due to any of the following items:

- Risk transfer is complicated and can’t be challenged easily by new companies/concepts.
- The risk transfer value change is already efficient enough.
- Regulation, tax law and capital arbitrage protect reinsurance product offerings.

- Reinsurance is sufficiently essential to insurance markets as to make it irreplaceable.
- Insurers are satisfied with the current markets, which they see as stable.
- The business of reinsurance is antifragile (as defined by Nassim Nicholas Taleb, who defines antifragility as a state greater than resilience—a state where entities experiencing shocks actually benefit from them).
- Reinsurers are led by executives who have a follow-the-herd mentality and/or embrace the present too tightly.
- Reinsurance company shareholders are not pushing reinsurers to innovate.
- If and when driverless cars become a reality (since cars sit idle 97 percent of the time), self-owned cars may become a thing of the past, which will kill the car insurance market as we know it.
- Some clients are already looking to the capital markets for risk transfer solutions for catastrophe and longevity. The world’s top reinsurers, however, have not investigated this avenue.

Even if no new players are entering the risk transfer market, the four trends cited above should convince us that the reinsurance market is not untouchable, and should have us concerned about how we can reinvent our present business model and product offerings.

I would respond to all these items with a resounding “I don’t think so!”

Let’s now consider a few trends related to our clients:

- A lot of merger and acquisition activity is currently taking place. Insurance companies are getting bigger and retentions are increasing, which is shrinking reinsurance premiums.
- The average age of the career life insurance sales agent is rising fast, which means that as a cohort, agents are falling out of sync with those who comprise their primary target market: young individuals.

What really confirms the reinsurance industry’s lack of risk transfer innovation is how leading reinsurers are prospecting and selling in their newest markets. None have used the opportunity of entering a new reinsurance market to introduce or leverage a new offering or business model. If reinsurers had developed some innovations, emerging markets might have provided perfect opportunities to leapfrog the old and showcase the new. But sadly it’s business as usual—same old, same old.

Reinsurers today might very well be working on innovative ways to transfer risk, but limiting investment in research and development in this area will not enable a major breakthrough. I would like to suggest that the main culprit for this



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lack of investment in innovation might be the industry's fixation on "quarterly capitalism," or a focus on short-term results. The reinsurance industry might be too wary to shell out the big bucks necessary to fund alternative risk transfer models that may, at best, only pay off in the long run.

Nonetheless, I believe the reinsurance market will eventually be impacted dramatically by a new and innovative way of doing business. The question is: will the innovation be a complement, as Airbnb is to traditional hotels, or a disruptor such as Netflix, which killed Blockbuster but sits happily next to cinemas? Right now that's hard to say.

Change will definitely come, whether the traditional reinsurance market embraces it or not. It has to: the reinsurance market is huge, representing US\$570 billion in capital, and it is profitable, representing a tempting opportunity. Indeed, for many years, Warren Buffet extolled this industry, trumpeting his reinsurance investments (although *The Wall Street Journal* recently reported that even Berkshire Hathaway is reassessing its exposure to the sector). Nonetheless, at some point, a new player is going to take notice of the industry and innovate, and traditional reinsurers, unfortunately, may have little influence over events and no control of the consequences.

So, it's not if, but when. The only question is which of the seven kingdoms will be the first to be materially impacted. Here I refer to the seven realms of Life, P&C, Reinsurers, Retrocessionaires, Brokers, On-Shore and Off Shore. Who will be left standing at the end?

Winter is coming. ■

This editorial's inspiration came from a presentation by IE Business School (Madrid, Spain) Professor Eloy B. Garcia on Geopolitical Challenges in a Multipolar World. A fascinating Q&A session with Professor Garcia is included within this newsletter.