

# WHAT BRITISH INSURANCE BROKERS THINK

**AUGUST 2006**

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## CONTEXT

The **BIBA** conference is one of the key events on the UK's insurance calendar, serving as a valuable discussion and networking forum for all those involved in the broking sector.

The theme of the 2006 conference was '**making the difference**' - reflecting the unique perspective and influence the broker channel has on the insurance market.

Brokers are making a difference to their customers' businesses daily: anticipating trends, understanding the risks, offering choice, extending the cover, solving problems and reducing cost for the vast majority of UK businesses who trust their broker for expert advice and unbiased opinion.

Recognising the importance of this sector, Lloyd's was not only one of the sponsors of the 2006 conference, but took the opportunity to survey brokers' opinions regarding opportunities and threats within the UK industry. Here, we share the results, which we hope will help UK brokers to benchmark themselves against their peers, and to assist their planning as they prepare for the future.

## METHODOLOGY

Acritas interviewers attended the BIBA 2006 conference and were given the opportunity to conduct impromptu interviews with conference attendees.

In total, 117 conference attendees were interviewed. All those interviewed were brokers and were spoken to by random selection. The interviews lasted approximately 10 minutes and addressed a range of issues.

Cross break analysis was conducted by size of organisation and regional location, any interesting differences are noted in the commentary

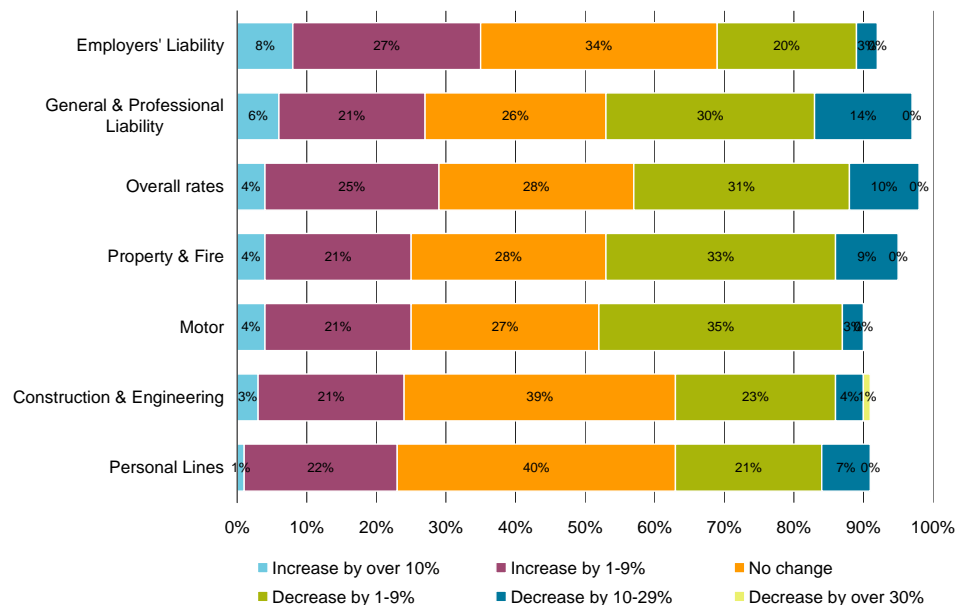
- Organisations with 50 or fewer employees have been categorised as 'smaller' and those with 51 or more employees are categorised as 'larger' for these research purposes (smaller and larger organisations were represented in equal proportions)
- Regional classifications have been grouped as follows: South East (including London) compared to all other areas
- All figures for BIBA 2006 Conference research results have a base of 117 unless otherwise noted

## FINDINGS

### 1. A PERIOD OF STABLE PRICING PROVIDES WELCOME RELIEF

In contrast with many recent years, brokers expect little change in pricing conditions as the UK market continues to experience a period of relative stability. As a result, brokers should benefit from the need to spend less time explaining and communicating market instability to clients, and focus more on adding value to their role.

Q. Over the next twelve months, what do you think will happen to UK insurance rates?



Brokers are agreed that there should be no major price increases over the next 12 months. Indeed, overall, any pressure on rates is expected to be downward (41%) rather than upward (29%).

However, views do vary.

Larger brokers are more likely to expect a decrease in rates (53%) than their smaller counterparts (28%).

Views also vary by class of business. Employers' Liability is regarded most likely to see rate increases (35%) while General and Professional Liability is most likely to see rate decreases (41%).

Peter Franklin, National Technical Director of JLT, said:

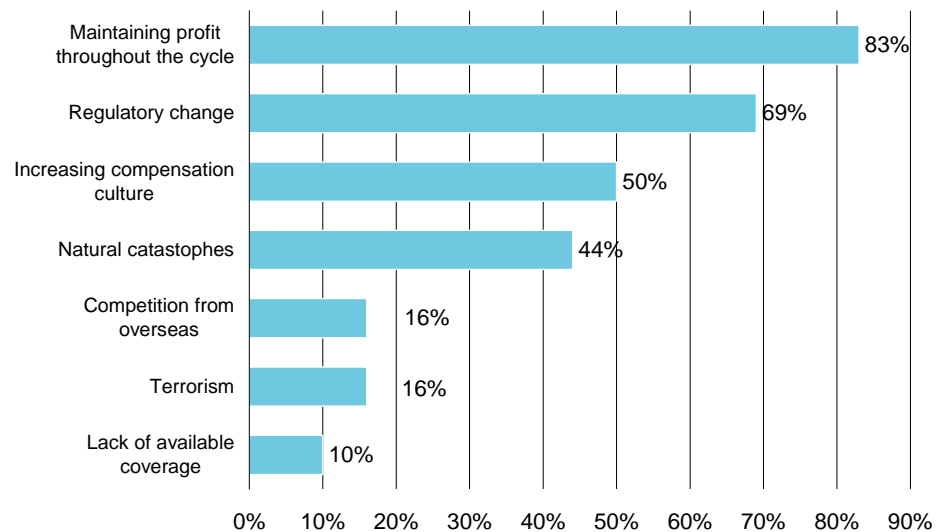
*"Recent changes in legislation have led to firms being liable to pay for employees' NHS treatment following an accident at work. Also, a recent asbestos legal case which was decided in favour of employers and, therefore, their insurers looks likely to be reversed by legislation. All of this has put pressure on employers' liability rates, and this pressure is sure to continue."*

*"As for the professional indemnity market, this has had a few profitable years recently, and with increased market capacity we can expect further reductions in rates. This is also the case with public and products liability."*

## 2. BUT MARKET CYCLES ARE STILL THE GREATEST INDUSTRY CHALLENGE

**Over 80% of brokers believe the greatest challenge for the UK insurance industry in the next year is to manage the insurance cycle better than in the past, while over two-thirds are also concerned about the pace of regulatory change**

Q. Which of the following do you think are the top three challenges facing the UK insurance industry in the next 12 months?



Regardless of size or regional location of the broker organisation, maintaining profit through the cycle is considered to be the most significant challenge for the next 12 months. While the expected stability of pricing should help greatly, brokers know that the industry is often slow to learn from past experience, and memories of the last cycle are still at the forefront of many minds.

David Meur, Managing Director of Genavco Insurance Ltd and Chair of BIBA's property committee articulates the view of many when he says:

*"The insurance cycle has been endemic in our industry for decades now. It affects everyone in the business - insurers, reinsurers, intermediaries and, not least, insurance buyers.*

*Our customers fail to understand why the premium they need to pay for an insurance risk can be so volatile over relatively few years, when the risk itself doesn't change materially. It is therefore difficult to engender confidence in our industry on the part of our customers, and develop the reputation of integrity and professionalism which we espouse.*

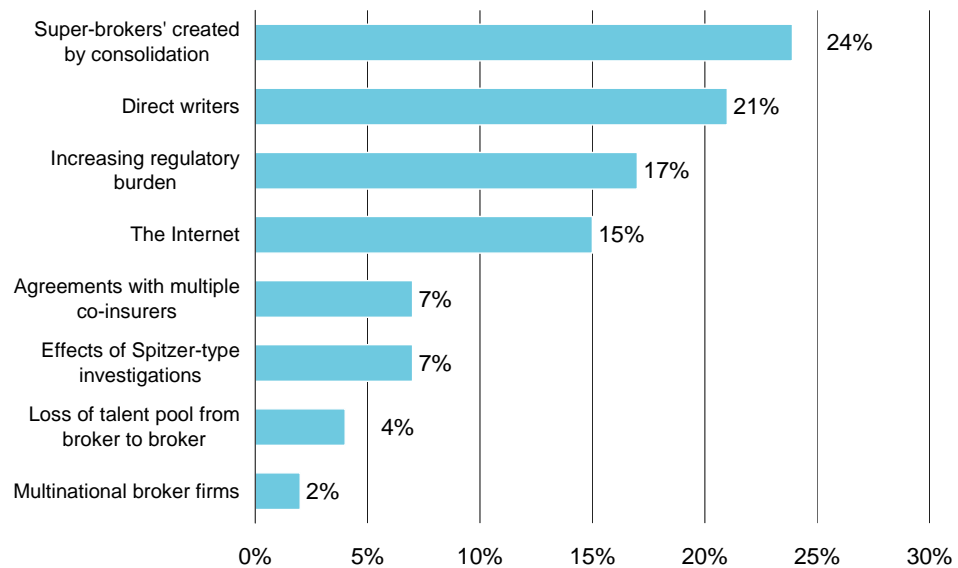
*We have consistently said over the years that we need to learn the lessons of the last cycle, and introduce greater stability in the future. Once again, we need to ask ourselves exactly what started the last hard market, and what ended it, leading to the latest downturn that we are now experiencing. Are market cycles inevitable? or is there not a better way of managing our business over the longer term?"*

This finding is consistent with what we have found elsewhere. Managing the cycle was also identified by Lloyd's Underwriters as the most important challenge for the industry to address in Lloyd's 2006 Underwriter Opinion Survey, in February this year. But some 69% of underwriters stated at that time that the industry had not made enough progress on this issue yet- it seems that almost everyone in the UK insurance market agrees that more needs to be done.

### 3. DISTRIBUTION TRENDS ARE THE BROKER'S BIGGEST THREAT

Changing distribution trends are seen by both large and small brokers as their most significant threat. The creation of 'Super-brokers', the influence of direct writers, and the rise of the internet all appear in the top four challenges. In addition, smaller brokers are concerned by the increasing regulatory burden they experience.

Q. Which of the following presents the most significant threat to UK brokers over the next three years?



Smaller broker organisations actually perceive the increasing regulatory burden to be the single most significant threat. The cost implications (not least through the considerable management time required for compliance) can be substantial to a small business to the point of being prohibitive, while larger brokers are naturally less concerned by the regulatory burden having greater resources available to address the requirements. The clear message which brokers would send to regulators is that one size does not always fit all, for as diverse a sector as the UK broking industry.

However, distribution trends remain the greatest concern for brokers of all types, overall. The larger broker organisations more commonly cite the threats presented by the formation of so-called 'Super-brokers', as companies grow by embarking on a series of acquisitions of competitive firms. Through a high degree of power over insurers, such 'Super-brokers' are seen by many to control capacity and distort the open market.

Colin Lees, Managing Director of Lymm Insurance Brokers Ltd based in Cheshire, said:

*"Super-brokers are without a doubt the biggest challenge we face. As these companies get bigger and swallow up larger percentages of business, they get more control over distribution channels and prices and*

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*can exert more pressure on underwriters, skewing profitability but with no risk. I can't see this being good news for the customer or the underwriter."*

One thing is clear, UK brokers currently feel they have enough on the horizon to challenge them at home, without worrying about the wider international issues of multinational competition, and the impact of industry investigations such as those in the US.

#### 4. BUT BROKERS ARE TAKING ACTION

**Our research shows that UK brokers are generally taking an active role in responding to these threats. Overall, organisations are most actively addressing the issue of challenges of increasing regulation (89%) and the Internet (77%)**



UK brokers are currently spending more time getting up to speed with regulatory requirements and becoming Internet-savvy, than responding to any other threats. Nevertheless, the majority are very active in responding to most of the challenges.

Interestingly, although identified as the number one threat, a relatively small proportion of organisations (only a third) are actively addressing the issue of 'Super-brokers'. Maybe UK brokers aren't sure what they can do in response, or maybe they feel they cannot stop the trend.

Colin Lees, Managing Director of Lymm Insurance Brokers Ltd in Cheshire, said:

*"For smaller brokers, it is a question of money. They don't trigger the higher commissions and volume overrides to generate the kind of budgets super-brokers have for marketing, making it more difficult to compete.*

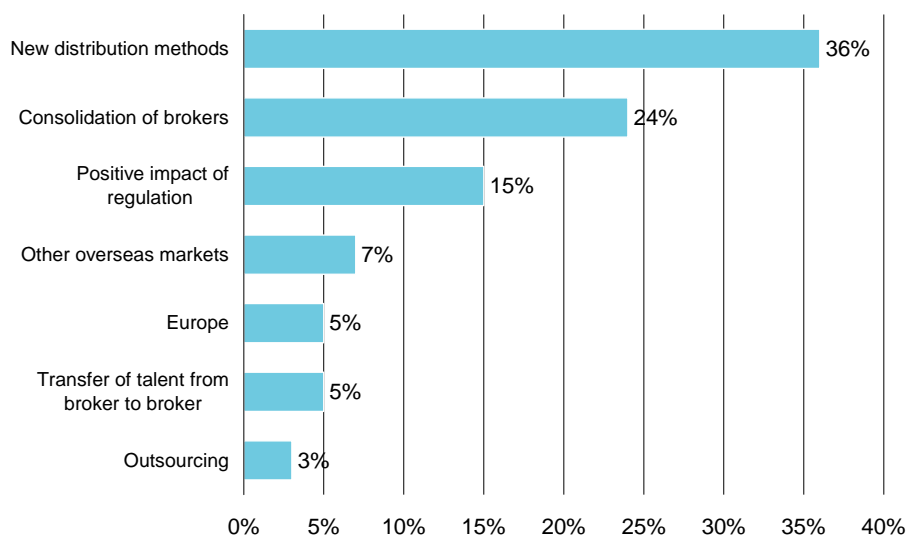
*"But non-super-brokers can compete by offering a unique brand. They can offer specialist knowledge and skill delivered by highly competent and experienced professional people who really know what they're talking about. It is an intimate relationship, on a one-to-one level, that focuses on a niche technical area of our industry that's too complicated to be handled by a standardised process.*

*"Getting a return from this kind of brand is not as fast as a more process-driven, vertical market, but equally it is not vulnerable to a well-resourced marketing attack by a superbroker."*

## 5. EVERY CLOUD HAS A SILVER LINING: FROM THREAT TO OPPORTUNITY

**If changes to distribution methods are the biggest concern, this research also proves that they provide the biggest opportunity for UK brokers too. Just over a third see this as the greatest opportunity for brokers in the UK, over the next three years. This is followed by nearly a quarter (and smaller brokers in particular) expecting broker consolidation to provide positive opportunity for their own firms.**

Q. Which of the following presents the greatest opportunities for UK brokers over the next three years?



In second place after new distribution methods, nearly a quarter of respondents (and smaller brokers in particular) expect broker consolidation to provide positive opportunity for their own firms.

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Even the more onerous regulatory environment is perceived by a fair proportion (15%) to be advantageous for brokers in the end, probably by helping to raise industry standards and reputation.

Again, UK brokers are largely occupied with capitalising on opportunities at home, with only a small proportion seeing opportunity in European (5%) or wider global markets (7%), and even fewer (3%) thinking of outsourcing. It does mean, however, that those brokers who spot international opportunities and are able to respond to them now, may have a competitive advantage over their peers.

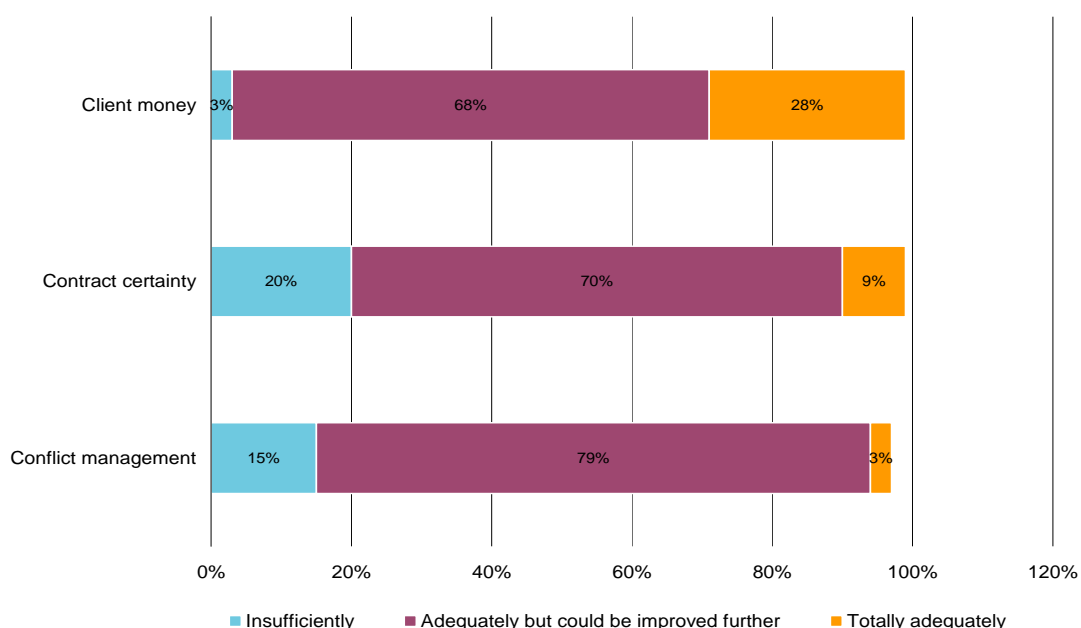
Mark Hewett, Deputy Chairman of Guy Carpenter & Company Ltd, says:

*“Global economic growth will continue to be driven by the emerging markets - the UK, and London in particular, has always been a major player on the world stage with a concentration of intellectual capital and a proven ability to innovate. Changes to the distribution system should be seen as an opportunity offering real scope for growth with improved accessibility, process efficiencies and the ability to deliver new products.”*

## 6. IS PROGRESS ON REGULATORY ISSUES FAST ENOUGH?

**Generally speaking, UK brokers feel their sector has done an adequate job in addressing the key issues of client money, contract certainty and conflict management. However, a number of brokers still feel there is room for improvement in each area.**

Q. How would you rate how well the UK broker industry at large has addressed the following issues so far?



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Brokers believe that client money has been most adequately addressed to date (97%) while contract certainty is the area where most work remains to be done: 20% believe progress to be insufficient and only 9% regard it as totally adequate.

While recognizing the importance of this issue, David Hough, Executive Director of the London Market Insurance Brokers' Committee, feels that good progress is now being made:

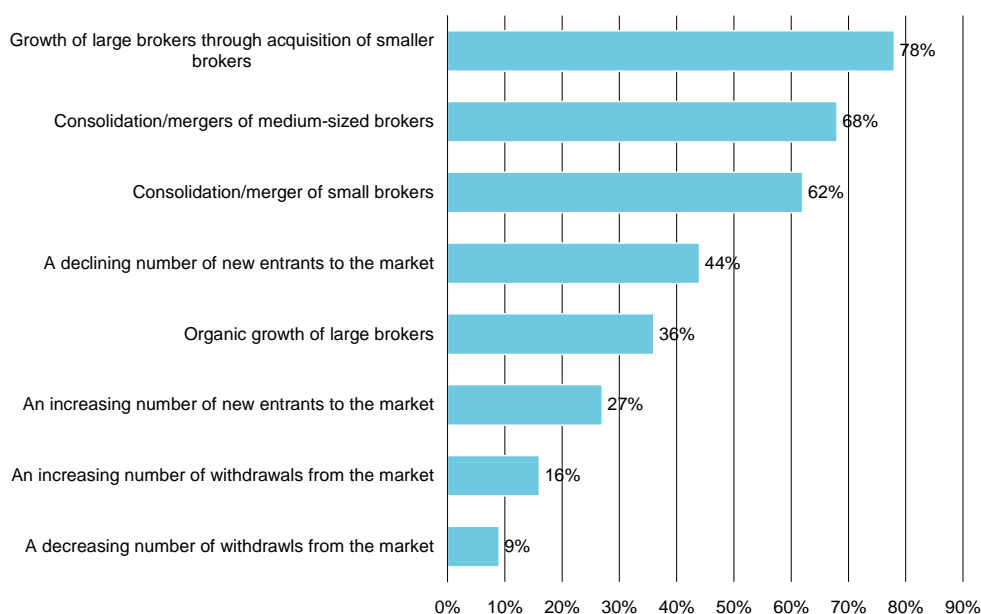
*"Much of the solution to contract certainty in the UK retail market rests with the insurers who produce the policies. A non-London group of reform champions is driving this forward and it appears to be making good progress.*

*"But in the London market, the drive for contract certainty is led by the Market Reform Group - leading figures in the market responsible for its modernisation. A tremendous amount of work has been done, resulting in regular measurement and detailed guidance on the issue to help brokers and underwriters. So far, the market has responded positively. We are confident that we will meet the end of year target of 85% of contracts going through the London market being certain."*

## 7. FURTHER CHANGE AHEAD IN THE UK BROKING SECTOR

**The majority of UK brokers are in no doubt - the industry landscape will change as consolidation takes place over the next 18 months, particularly through acquisition by larger firms, but also via mergers of medium and small brokers**

Q. Which, if any, of the following changes do you expect to see affect the shape of the UK broker market in the next 12 – 18 months?



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In the currently competitive UK market, not many see an increasing number of new entrants to the broking sector (27%) and only slightly more are hopeful of opportunities for organic growth (36%). But without much in the way of withdrawals expected either, mergers and acquisitions are the single biggest force for change on the horizon in the next few years.

## CONCLUSIONS

“The impact of the market cycle on intermediaries and their customers, consolidation and other changes in distribution, regulation and technology all provide continuous challenges and opportunities.” – Eric Galbraith, Chief Executive, BIBA.

UK brokers believe that 2006 and 2007 will be a time of both stability and change.

Whilst rates are currently relatively stable, brokers do not believe that the UK insurance industry is doing enough to manage the cycle over the longer-term. Given that Lloyd's underwriters see it as a top concern too, it seems we have consensus across the UK industry that the issue has not simply gone away. Moreover, there seems to be agreement that steps can and should be taken to lessen its impact if we are prepared to learn from past experience. For brokers and their clients, anything which creates a more stable market can only be good news.

One of the clearest themes emerging from the research is that distribution structures and channels are changing. As you might expect, these present both opportunities and threats for intermediaries. The formation of ‘Super-brokers’ is certainly seen as a threat by many for example. On the other hand, relatively few see the internet as a threat but most brokers are actively addressing how best they can make use of it

Another trend emerging from the research findings relates to consolidation. Both larger and smaller brokers expect to see consolidation take place across the sector at all levels, with acquisitions of smaller brokers, and mergers of smaller and medium-sized brokers most likely. In general, brokers see opportunities emerging for their own businesses as a result of these changes.

On regulatory issues, the majority of brokers surveyed believe that the industry has done an adequate job of addressing the key issues of client money, contract certainty and conflict management. The focus should now be on successfully completing the course for contract certainty by year end. But there is no doubting the impact of the increasing regulatory burden on UK brokers, with smaller brokers in particular asking whether there is enough understanding and flexibility in respect of their situation.

Overall, there is little doubt that British insurance brokers are ready and willing to embrace change.

Eric Galbraith, BIBA Chief Executive, concludes:

“This survey confirms that the broking and intermediary channel is responsive to change, recognises the challenges and opportunities that exist, and continues to be innovative”.

## APPENDIX

### 1.1 Demographics – Region

London	32%
SE (exc. London)	21%
SW	10%
W Midlands	7%
Nationwide	6%
Northern Ireland	5%
NW England	4%
NE England	3%
Scotland	3%
Wales	2%
E Midlands	2%
Global	1%

### 1.2 Demographics – Classes of business frequently placed

General & Professional Liability	73%
Employer's Liability	67%
Property & Fire	67%
Construction & Engineering	58%
Motor	53%
Personal lines	47%
Marine	44%
Catastrophe	14%
Aviation	5%

### 1.3 Demographics – Number of employees within an organisation

Less than 10	11%
10-50	39%
51 to 100	15%
101 to 250	9%
Over 250	24%

### 1.4 Demographics – Percentage of portfolio placed at Lloyd's

Less than 10%	44%
10 to 25%	27%
26 to 50%	12%
50 to 100%	16%