

Future proofing the UK
mutual insurance sector
The need to think
strategically



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Future proofing the sector

The sector is at a crossroads where it needs to examine its structure and purpose in order to identify the critical success factors to secure its future.

There have been seismic changes in the economic and regulatory environment over the last three years. This has had an impact on all parts of the financial services industry, and the mutual insurance sector has not escaped.

The sector is at a crossroads where it needs to examine its structure and purpose in order to identify the critical success factors to secure its future. There is no doubt that difficult decisions lie ahead. Recent history has not been encouraging and the traditional mutual model is under threat. We predict significant shrinkage in the number of organisations in the sector over the next ten years.

The economic environment has brought issues for the industry in areas such as investment volatility, reduced sales of protection policies and challenges around the IFA distribution model. Solvency II, the Retail Distribution Review and tougher regulation generally all raise challenges, and the sector needs to change in order to meet them. The key to a successful future is identifying and adopting the right strategy. A key part of this will be maintaining and enhancing relationships with members and demonstrating the value of the mutual model. The sector needs to achieve closer ties with customers, perhaps using schemes such as the 'mutual dividend' models used by some including NFU Mutual and Royal London.

Although challenges to the sector clearly exist, there are many positive factors to consider:

- A key part of the mutual message has been stronger customer service levels as a local and/or niche market focus allows mutuals to better understand their customers.
- Decisions are taken to benefit the members rather than having to satisfy both customers and a separate group of shareholders.
- Government and EU support exists in principle for the mutual model, albeit significant practical support has not yet been forthcoming.

The sector should look to learn from some of the lessons of the Building Society sector as it has faced similar challenges. Our paper draws out some key points for boards to consider.

- Consolidation is a likely option for many in the sector. How should organisations position themselves for this change?
- Partnering with other mutuals should be considered, widening the propositions available to customers. Too many mutuals work in isolation.
- Talent will be key and investment needs to be made in this area – high quality management is needed in this time of change.
- Business models need to adapt to differentiate from proprietaries. Such models include genuine specialism or an affinity group model but there may be other models that emerge.
- Innovative ways of injecting new capital need to be found.
- The sector needs to consider whether it can play a part in helping the government's wider social policy.

Bold action is necessary across the sector for it to succeed.

The changed shape of the sector

“Mutual organisations were formed out of the common needs of working-class communities during the industrial revolution for protection against the insecurities of life. They were usually funded by many small contributions, since only by aggregating the small savings of many people could a capital fund be created. Membership was a mechanism to ensure that the organisation continued to serve the needs of all its contributors. People did not create mutuals to derive a profit, or to seek a capital gain, but in order to benefit from a service.”¹

The last 15 years has seen significant changes in the structure and financial strength of the insurance mutual sector. The late 1990s to early 2000s saw a trend towards demutualisation with Norwich Union, Friends Provident and Standard Life all choosing to swap their mutual status for ownership by shareholders via London Stock Exchange listings. Furthermore, the acquisition of Scottish Widows by Lloyds TSB, Scottish Provident by Abbey National and the closure of Equitable Life to new business during this period meant that many of the biggest names of 15 years ago had, by 2006, largely been lost to the mutual sector.

Financial strength surveys of ten years ago were dominated by mutuals. Although mutuals still appear to rank favourably in free asset terms against their non mutual competitors, a lot of the sectors’ capital strength has been eroded in the last ten years. This has been a challenge across the whole of the industry and it could be argued that the capital reductions have not always been as a result of delivering superior returns.

In March 1998 the Financial Times published a four page spread on the future of mutuality. The lead article in this publication was written at a time when demutualisation was becoming an increasingly popular option, not just in the UK but around the world with the largest mutual insurer in the US, Prudential Insurance, having just announced its intention to demutualise via a stock exchange listing. This trend led to the author commenting that “mutuals could all but disappear in the 21st century”.²

While clearly in recent years the trend towards demutualisation has slowed, significant threats to the future of the sector remain. There is now only one mutual in the UK top 10 life insurance organisations by premium size³.

In 2011 there are around 200 mutual insurers and friendly societies in existence, with around £86bn of funds under management³. Based on the most recent market analysis, mutual insurers now make up about 5% of the total UK insurance market³. As a comparison, the building society sector still makes up approximately 20% of the UK savings market despite the building society sector’s demutualisations and mergers having been more widely publicised.

The mutual sector position in the UK contrasts with that in many European states where mutuals are far more prevalent and in some cases comprise over half of the insurance market. The International Cooperative and Mutual Insurance Federation (ICMIF) calculated that mutual and cooperative insurers represented 24% of the total insurance market in Europe in 2008 – 22% of the life market and 30% of the non-life.⁵ The equivalent statistics for the UK were 4% for life insurance and 10% for non-life. Some of the UK success in the non-life sector has been in P&I clubs, for example around shipping insurance.

1 A Guide to Societies based on the principle of Mutuality - Malcolm Hornsby and Mervyn Wilson, New Sector Magazine, Issue No 28, June/July 1997

2 Financial Times – March 1998 “Survival Depends on Differentiation” by Christopher Brown-Humes

3 Association of British Insurers data (taken from website)

4 2010 financial statements for relevant entities

5 ICMIF 2008 data as presented in the European Parliament 2011 paper “The role of Mutual Societies in the 21st century”

The UK insurance mutual sector has historically been dominated by a number of large players with a long and fragmented tail of smaller scale players. The top 5 insurance mutuals have around 80% of the sector's total funds under management⁴, and over 90% of mutuals have assets of less than £1billion⁴.

By far the largest organisation currently is Royal London which had total assets in excess of £34bn at 31 December 2010⁴. Its subsequent takeover of Royal Liver from 1 July 2011 and discussions with Co-operative Financial Services to acquire its life and asset management businesses would take this to in excess of £55bn, more than four times the size of the second largest insurance mutual, NFU Mutual.

However, growth by acquisition only changes the number of mutuals in existence. Continued organic growth of funds under management is needed to increase the size of the sector. This requires a focus on the development of new and existing products and a need to connect with customers.

Top ten list of mutual insurers by asset size in 2000 vs 2010

	2000 ⁶	2010 ⁴
1	Standard Life	Royal London
2	Scottish Widows	NFU Mutual
3	Equitable Life	Equitable Life
4	Friends Provident	Liverpool Victoria
5	NFU Mutual	Wesleyan Assurance
6	Royal London	Royal Liver
7	Liverpool Victoria	MGM Advantage
8	Wesleyan Assurance	Reliance Mutual
9	Royal Liver	Family Investments
10	MGM Advantage	Police Mutual

NB Excludes Co-operative Insurance Services, part of CFS group.

The top five insurance mutuals have around 80% of the sector's total funds under management, and over 90% of mutuals have assets of less than £1billion.

⁶ 2000 FSA returns data for relevant entities

Drivers for change

Capital and Solvency II

Raising capital has always been a challenge for the sector, yet without sufficient capital the sector will struggle to have sufficient funds to develop new products, retain high calibre staff and reward members for their loyalty. Currently capital is recycled from generation to generation and any acceleration of that cycle would be beneficial to the sector.

Subordinated debt remains an option but tends to be expensive relative to the actual return on capital that the sector generates. Similar options include permanent interest bearing debt such as that used by the building society sector, although the concept has not as yet been transferred successfully to insurance.

Monetisation of the value of in-force business is a realistic possibility but leads to a significant diminution in the future profits that can be realised. Levels of reinsurance used in the mutual sector may increase as arrangements are put in place in order to support the additional capital requirements under Solvency II.

The sector needs to find innovative ways of obtaining new capital. There are examples of non-UK mutuals achieving this, and also within the UK building society sector.

Solvency II regulatory changes are an ongoing source of debate within the industry, with concerns raised by many associated with the mutual sector that the original proportionality principle of Solvency II (i.e. that "it should not be too burdensome for insurance undertakings that specialise in providing specific types of insurance or services to specific customer segments")⁷ has already been lost.

A recent survey conducted by the Association of Financial Mutuals⁸ (published in September 2011) indicated that the majority of directors are confident over the ability of their organisations to comply with the requirements of Solvency II by the intended 2013 deadline, which has since moved back. However, concerns were raised in respect of regulatory clarity and guidance and the ongoing costs of complying with the new regulations.

The decision to delay the implementation of the regulation by a further 12 months to 1 January 2014 has some benefits, but potentially increases the cost of implementation and extends uncertainty over the final outcome.

The costs associated with the development of an internal model for Solvency Capital Requirement purposes are largely considered to be disproportionately high for many of the smaller mutuals; however, they are equally unable to claim the rewards offered by the standard formula for underwriting diversification by line of business and geographical region. This is expected to result in many of the smaller mutuals with a local and/or niche product base having higher capital requirements under the new risk based regime - resulting in reductions in existing surplus. In addition, for many, existing subordinated loans often have considerable sums outstanding and eligibility under tier 1 capital is expected to be an issue.

Other concerns include governance and reporting requirements being onerous together with deep misgivings about Pillar I with regard to the calibration of long and/or specialised lines of business. Many mutuals in continental Europe could suffer heavily under the current calibration, and we wait to see whether their lobbying efforts bear fruit. The ICMIF and other European mutual bodies are engaging closely with the European Insurance and Occupational Pensions Authority "EIOPA" and the European Commission to ensure the mutual voice is heard.

Areas of focus on the agendas of mutuals for the next six months per the AFM study include the system of risk governance. Under Solvency II the quality of risk management systems becomes even more important and getting resource with the necessary knowledge and expertise can be challenging and costly for smaller organisations.

The additional disclosure requirements will give mutual organisations further opportunity to communicate their financial and operational strengths to members. However, we would not underestimate the effort that will be required to meet these requirements. Many mutuals will have to provide information they do not currently disclose, with corresponding extra cost and pressure on resources.

High expense ratios

Many smaller mutuals have higher expense ratios than their competitors due to the historic structure of the organisations, lack of outsourcing and, in certain cases, entrenched ways of doing business that have not always been the most efficient. In recent years those with the highest costs have either already been acquired by larger players or have had to introduce significant cost cutting programmes.

7 Solvency II Directive, Section 14b

8 Association of Financial Mutuals Solvency II survey published in September 2011

Cost reduction tends to be cyclical, however. There is a period of change, which many went through during cost reduction programmes three years ago, but equilibrium often returns. How hard has the sector pushed itself on costs – have bad behaviours crept back in?

Businesses need to identify where cost reductions can be made, with an eye to investment in the right places in order to retain the ability to respond to market challenges. Any organisation that has not felt pain in this area is likely to have significant work to do.

Outsourcing has, to date, been limited in the mutual sector. In addressing cost issues this may become a more prevalent practice and options around alliances with other mutuals are likely to be increasingly considered. The building society sector has been investigating such avenues for several years, although little progress has been made, due to the ability to increase efficiency while still retaining independent, strong branding as a mutual. Joint ventures between mutuals in Europe are fairly common, using centralised facilities. In our view with the challenges the UK mutual sector currently faces, a little more of this collaborative approach could go a long way.

Impact of Consultation Paper CP11/05 “Treating with-profit policyholders fairly”

The FSA has recommended that mutuals which are no longer writing significant volumes of with-profits business should close these funds and distribute their value to with-profits policyholders. While the publicised FSA view is that this will not have a significant impact on the industry, the majority of those in the sector disagree.

In May 2011 the Association of Financial Mutuals (AFM) compiled a response to the policy paper. The response aims to set out proposals for a sustainable with-profits mutual sector, backed up by legal opinion.

In the 2010 financial statements for the largest 12 mutual insurers, for nine of firms gross written premium (GWP) relating to with-profits policies was 5% or less of total GWP. Exceptions to this trend were Royal Liver (now part of Royal London), Scottish Friendly and Police Mutual. Attempts to reinvigorate with-profits sales have met with mixed success. Some mutuals, such as MGM Advantage, have taken a different path and emerged as effective niche players including new with-profits offerings, but many have experienced poor with-profit sales. For the majority of businesses it is hard to see how with-profits can be effectively revived without significant investment.

Some societies have successfully used with-profit funds to build profitable subsidiary businesses, however this is subject to regulatory challenge under CP11/05.

The impact of CP11/05 will vary tremendously depending on each mutual’s constitution. The AFM believes that the FSA’s approach will lead directly to the closure of several mutuals and that, without a change in regulation, the sector will rapidly decline and result in further closures over the next five to ten years.

Separating capital from membership is the key; however, achieving this is not easy. Ringfencing is a messy process and does not by any means guarantee a sustainable model as a result. Consideration of “members funds” which would require the vote of members within the organisation is one option that could be considered – the view of the regulator of such solutions is, however, not clear. The FSA needs to continue to be engaged by the sector in looking at potential proposals.

Case study: LV=

LV= is a much commented case study of an organisation that has effected massive change in image and brand. The shift in direction started with the appointment of Mike Rogers as CEO in June 2006. Its acquisition of the ABC insurance team later in 2006 allowed the mutual to make a distinct strategy move that is not without its challenges in view of CP11/05, but has nevertheless given the insurer a new direction and a distinct place in the UK insurance landscape.

Subsequent rebranding in 2007 coupled with some clever, and high profile, marketing (until that point LV had not used TV advertising, and there were few in the mutual insurance sector that had) since that point has catapulted the brand into the public consciousness and created a step-change in the success of the organisation. 2007 also saw the acquisition of Tomorrow from Swiss Re and Britannia Rescue from The Civil Service Motoring Association

The Highway broker acquisition in 2008 has served to complement and strengthen the general insurance part of the organisation through expanding the distribution network.

The distribution challenge

While the Retail Distribution Review (“RDR”) is expected to have wide ranging impacts on the financial services sector, the general expectation is that the impact may be less for mutuals than other life insurers.

Initial views on RDR were that the bancassurers would emerge as winners. This is no longer as clear. Mutuals may well own a large part of the market not covered by the IFA community. Has the right customer data been analysed to examine this?

Mutuals’ roots were around looking after specific communities – part of the community going forward will be ‘unadvised’. Can mutuals step in to assist the unadvised community?

The business written by the majority of mutuals tends to be niche speciality business with small premiums. It will be difficult to make money on this type of business on an advised basis. Surveys indicate policyholders are willing to pay much less for advice than the actual cost, making it difficult to make money on an advised sales basis under likely adviser charging structures. Thus new models for serving customers will be required. The good news is that mutuals with strong affinity groups will typically already have strong direct relationships with customers and may find it easier to move to non-advised or streamlined advice approaches. However, this theory remains to be proven.

Those mutuals using traditional IFA channels will face the same pressures as other life insurers including a lower number of distribution points, the need to change business model to adviser charging and the likely resistance of consumers to paying fees. All insurers, whether mutual or proprietary, as a result of RDR are having to explore the channels they use, the charges they will levy and the implications for product and service delivery.

In the run up to RDR it will be important to protect the back book as advisers seek either to write commission business prior to RDR’s implementation or to shift assets onto platforms to allow them to earn greater assets under management fees. The expected increased use by IFAs of wraps and platforms mean that mutuals need to consider making products available through these channels. For those that choose not to use the wrap/platform model, it will be important to ensure that products are included in the product set for restricted advice firms as there is expected to be a growth in that model.

To achieve a broader proposition base, partnerships with other mutuals should be sought.

In all cases, a clear segmentation and management of legacy business will likely be required, and a review of offered products will be necessary.

Alongside this, there is the expectation that more consumers will go direct to supplier for their products. Mutuals will need to consider their ability to distribute direct and to develop introducer or affinity arrangements.

The political landscape

It is hard to call whether politics will help or hinder the cause of the majority of mutuals. For example, a number of insurance mutuals have historically been involved in the provision of Child Trust Funds (CTFs). The Government’s decision to stop supporting CTF’s from 1 January 2011 will have a significant impact on the business of these societies.

In July 2011 the All-Party Parliamentary Group released an inquiry paper entitled “Fostering diversity: promoting mutuals”. This paper aims to respond to the concerns raised and in particular notes that the Government appears to have concentrated its policy efforts on encouraging the development of new mutuals to provide public services rather than to support the existing financial mutual sector.

The paper made the following recommendations:

- that it is imperative that the Coalition urgently adopts a comprehensive policy strategy to implement its Coalition Agreement commitment to promote mutuals;
- that HM Treasury should act as a strong advocate for mutual businesses, in particular in its dealings with the FSA and subsequent new regulatory authorities; and
- that HM Treasury should pro-actively promote the interests of financial mutuals within Government, and ensure that balance is given to understanding and promoting mutuals across all Government departments.

On the other side of the coin, the Government is increasingly concerned about the ageing population in the UK and the lack of pensions/savings held by many. Worrying statistics include a third of all young people not currently saving towards their retirement⁹. Recent research by Confused.com suggest 31% of Brits believe life insurance is a waste of money and 34% say they cannot afford life insurance.

Engagement with the Government is required to examine this topic further and work towards a potential joint solution. It may be possible to secure government funding for the provision of particular services which would help to address some of these concerns.

The not-for-profit sector is very large and it may be possible for mutual insurers to form links with other organisations in that sector in order to pursue common aims. An ageing population and increasing pressure on government spending is likely to mean an increase in social protection required in the medium to longer term, and the sector needs to become more relevant to these areas of society, which was, after all, how it initially began. This has been, perhaps, a missed opportunity to date. This is too large a topic for this paper to attempt to address, but the point to draw out is that steps need to be taken by the sector to engage with the government to find a solution to these challenges and opportunities.

To keep social protection systems affordable, the government is likely to look to transfer increased numbers of services to voluntary social and health insurance schemes and private pension schemes. This will stimulate demand in these areas and likely lead to increased premiums. Given the challenges faced by the Government the question should be asked as to the role mutuals can play in providing a valuable and affordable solution for some of the social protection issues.

The current Government coalition agreement documented its commitment to promote mutuals, stating, *"We will bring forward detailed proposals to foster diversity in financial services, promote mutuals and create a more competitive banking industry."* While this statement related specifically to the banking industry following the economic crisis, the support for mutuality as a whole was received positively by members of the sector. However, concerns have since been raised by mutual insurers and friendly societies that they face serious threats to their future as a result of the FSA's stance on sector issues, and that HM Treasury appear to be unwilling to engage with them in the way that they have engaged with the building society sector.

Political and policy arguments may well offer the best chance of success. Insurance mutuals need to be proactive and work together here to lobby the relevant parties in order to promote the sector's best interests. We believe that this aim should be pursued with renewed energy, as there may be more political support than in the past.

Europe

The UK has a particularly low mutual share of the market at 5%, compared with up to three quarters of the market in some European countries.

Within some parts of Europe there is a closer link between the provision of welfare coverage through the mutual, which is integrated into the statutory social protection system – in some cases managing their own facilities such as hospitals.

A draft Council Regulation on the Statute for a European Mutual Society was withdrawn in 2006 but is due to be re-tabled – opening new possibilities for mutuals to operate across European borders, and to form a 'European mutual' or a European Mutual Group Society (EMGS). The aim of an EMGS would be to create financial links between two or more legal entities within two or more Member States, likely to be through mergers of existing mutuals. This could bring future opportunities for the sector in terms of consolidation and expansion.

Building societies – following in their footsteps?

We can look to the building society sector for examples of how similar challenges as those faced by the mutual insurance sector have been approached.

In 1988 there were 78 building societies in the UK. Some level of consolidation had already begun prior to the financial crisis, due to the pressure of margin squeeze, cost of retail funding and big bank competition. The number had shrunk to 59 by the start of 2008, and by 2011 has dropped to 48 in total¹⁰.

A number of societies had been struggling for some time in terms of strategic direction, and had been attempting to tackle the 'cost vs differentiation' challenge. A number of niche players emerged, such as those focussing on areas such as buy to let or commercial lending.

During the crisis, issues at some societies caused reputational issues for the sector, and brought the perception from the FSA that the sector was part of the market problem. This led to a number of decisive actions being taken by the FSA in 'encouraging' mergers within the sector. A familiar pattern started to emerge, firstly removing the management team, then looking at capital raising options such as PPDS (Profit Participating Deferred Shares) and then moving towards merger options. Some of these actions took place within a swift timescale.

Raising capital and maintaining liquidity became a challenge, hampered for the larger societies by rating actions. Some failures occurred within the sector, where attempts at rapid diversification to counter margin challenges, had led to poorer decisions on books of business - one example being Chelsea Building Society, which was forced to find a new home in the Yorkshire Building Society.

Similar to the mutual insurance sector, building societies still had a number of core strengths:

- strong local presence through the extensive branch networks in place and the continuing strong links and affinities with their local communities;
- strength in the core mortgage and savings markets through a significant market share;
- continuing price advantage through not having to pay dividends to shareholders; and
- an attractive brand that largely retains customer trust.

However, there remained longer term pressures on the building society business model, and it is important to remember that it was competition in societies core operations that led to parts of the sector looking to exploit new markets to improve their margins. Though parts of the sector have now moved back to concentrate on traditional markets, the pressures that caused the need for diversification are still present.

The sector faced a set of strategic and operational options that mark the way for where the mutual insurance sector will need to travel:

- Trade out in current position.
- Mergers within the sector.
- Improve cost management.
- Divest non-core subsidiaries.
- Identify niche markets and move way beyond just being 'nicer' to customers.
- Invest in branch network and become genuinely central to communities.

The JC Flowers transaction with Kent Reliance Building Society in 2010 was a landmark for the sector. The society members saw the savings and loans business moved into a subsidiary bank part owned by Flowers, with the stake being partially paid in convertible preference shares which, when exercised, will deliver Flowers majority control. The driver for the society in this transaction was capital constraints that would not allow them a future.

What does this tell us about the direction for the mutual insurance sector? Some similar, and some different, challenges but one overriding need – to examine the core business model, assess direction and make bold decisions.

Looking to the future

So, in the light of the above challenges, what are the ultimate outcomes for the sector? We see a slimmer sector that needs to considerably reshape in terms of direction and focus. Given the likelihood of this more sparse landscape, there are a number of options that can be taken by individual mutuals:

1) Wither on the vine

Some mutuals will arguably be able to continue to operate in their current form; however, these are likely to be in the minority given past experience and the regulatory challenges that lie ahead.

Options around monetisation of cash flows through reinsurance arrangements could help survival by providing capital now repaid through future premium flows.

Another option is around the ringfencing of with profits business. This is a challenging process, however, and even profitable new business that is bought in subsequent to such ringfencing may not result in a sustainable model due to a lack of early profits emerging.

It will be essential for mutuals to tackle high expense ratios, either through taking actions within their own society or potentially sharing activities across societies or outsourcing more activities to third parties. Member intervention may be required to force action in this area where management incentive to change is low. They must also protect their key distribution channels to maintain their access to customers in the post RDR world. In addition, processes need to be optimised, whether in response to regulations, such as risk and governance processes under Solvency II, or to improve operational efficiency. Peripheral non-core businesses must be looked at to ensure they are not a drain or an unwarranted distraction of organisation attention.

There is a strong possibility that many smaller mutuals will fold due to their inability to operate in the future economic and regulatory environment. They will either run-off slowly or be taken over.

2) Consolidate

The actual numbers of mergers and acquisitions across the sector to date have been relatively low given the challenges to business model and the number of organisations. Within the insurance mutual sector Royal London and Engage Mutual have been notably active in recent years, as have Reliance Mutual, Oddfellows and Scottish Friendly, albeit at the smaller end of the scale.

Consolidation will only help, however, if efficiencies are proactively sought through the process – efficiency needs to be part of the transaction objectives to have effect.

Royal London

- December 2008 – Scottish Provident (Protection business).
- July 2011 – Royal Liver.
- Currently in discussions with Co-operative Financial Services to take over its life and asset management businesses.

Engage Mutual

- November 2010 – Ecclesiastical Life Limited (£270m of the long term assets of the business).
- December 2010 – Provincial Hospital Services Association.
- August 2011 – National Friendly's One Fund.

Growing via acquisition is a valid long term growth strategy at an individual organisation level; however, while this may work as a strategic option in the short term, it will not lead to organic growth for the sector as a whole. There are also challenges around the strain on management teams that such consolidation activities make – in the building society sector the regulator acted as a 'brake' to some organisations doing too many acquisitions and becoming overstretched.

The larger players have an option in terms of demutualisation via a sale to another life business or possibly through private equity input (e.g. the JC Flowers acquisition of Kent Reliance in the building society sector); however, we believe this to be an unlikely option for most firms.

A second possibility could be around the entrance of an external consolidator, similar to the Resolution model. An extension of this would be a 'run-off consolidator' bringing together mutual insurers to operate a group run-off model which would potentially outsource aspects of the run off to an organisation such as Capita. A scenario could be envisaged whereby the regulator, in an environment of requiring 'recovery and resolution plans' to be in place, could potentially be a driver in this sort of process.

The question should be asked as to whether there is a JC Flowers or Resolution equivalent for the mutual insurance sector?

Options around Joint Ventures with other organisations should be explored to a far greater extent than has been considered to date. Together with this, the Co-operative Financial Services and Britannia transaction highlights the potential for a banking sector merger with mutual insurance.

3) Differentiate

The majority of mutuals do not have the scale to compete on the basis of cost with other insurers. Therefore, for those that are to survive as individual entities, there is a need to develop a focus on specific markets or products to differentiate themselves within the market. This could include protecting or obtaining a defensible niche, e.g. organisations such as NFU Mutual, MGM Advantage and Police Mutual show that a niche focus can work well.

Fundamental to this success will be the ability to understand customers through increased use of data analytics and possibly develop products to meet those customer needs. All organisations should be asking themselves whether they currently do this to their maximum potential or whether improvements could be made – could the mutual sector emerge as winners under RDR by taking the non-advised market. Partnering with other mutuals to offer a broader range of propositions could be beneficial here.

Issues around expense ratios and efficiency must be dealt with quickly and the distribution challenge will need to be tackled to ensure products are able to reach customers effectively in the post RDR world.

Talent will be key to innovation and forward thinking. How much movement in talent have organisations seen, and how open to new ideas is the current talent base? How can 'new blood' be brought in? Are there performance issues that should be tackled?

Case study: MGM Advantage

MGM Advantage is an example of a mutual that has transformed its approach in recent years by providing policyholders with added value through specialism, in retirement income. They aim to make their products innovative.

MGM has also recognised that technical excellence and good product design are only part of the story; they have made a big effort to make it easy for their customers. The following excerpts from their website provide a flavour of this:

"We'll make doing business with us as easy as possible.

We'll never forget that we're owned by our members, and we'll put their interests at the heart of everything we do.

We'll treat all our customers fairly and with respect at all times.

We'll let you know before we make any changes to your policy terms.

We'll always try to do the right thing and we'll put things right quickly when we don't.

We'll tell it how it is – we won't hide behind jargon".¹¹

It is helpful to remember that many ordinary people find life assurance products and jargon confusing. Many have a poor opinion of the industry based on past experience. Mutuals should have an advantage when it comes to establishing trust between company and policyholder; if this is backed up by making every interaction as straightforward and friendly as possible, surely there is scope to turn this into a competitive advantage.

11 Taken from MGM Advantage website

Conclusion

Mutual insurers must have a clear and defensible strategy if they are going to survive and thrive. Doing so requires developing clarity on their market participation approach, their relative competitive strengths, the propositions and appeal to customers and distributors, and their internal capabilities. Only through this can they decide whether they can identify a role they can move to that is sustainable and value accretive to members.

The sector needs to consider as a whole its relevance in the future insurance landscape. The key may be in the identification and pursuit of a clear social-political objective. Demographic change means that existing social protection systems are unlikely to be sustainable and service will have to be provided outside of the state. Mutuals need to embed themselves in society to give the best chance of survival, and, given that social responsibility is at the foundation of their existence they are well placed to form part of the solution to social protection issues.

A wide-thinking, non-defensive review of strategy is something every mutual should have undertaken or be seeking to undertake.

Honest appraisal of management performance and ability to drive change will be required, and investment in talent should be a priority.

Mutual insurers will need to collaborate, both within the sector and externally, to find a collective path through the challenges faced. Effective and proactive engagement and lobbying with Government and regulators will be vital. As a whole the sector needs to consider how it differentiates and become integral to how society operates in this changed environment

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