OPPORTUNITIES IN INSURANCE

BUSINESS AND TALENT PROFILE OF TORONTO'S INSURANCE INDUSTRY

Centre of Excellence in Financial Services Education

Brondesbury Group

Ontario

TFSA Toronto Financial Services Alliance

The Centre of Excellence in Financial Services Education

The Centre of Excellence in Financial Services Education (CoE) is focused on strengthening Toronto's talent pipeline, which is crucial to addressing the needs of employers, students, internationally educated professionals and educators – and to attracting new talent to the region. To this end, the Centre of Excellence works closely with a range of partners across sectors, performing important research and outreach.

The Centre of Excellence:

- *Aggregates research and information on Toronto's talent and educational strengths*
- *Works with employers and educators to improve the focus and quality of education programs*
- *Encourages cross-sector dialogue on talent and education-related issues*
- *Showcases the region's strengths and the career opportunities that await in the Toronto region*

The Centre of Excellence is part of the Toronto Financial Services Alliance (TFSA) which is a public-private partnership among government, academia and the financial sector, dedicated to building Toronto region's stature as an international financial centre.

The Centre of Excellence is supported by the Ministry of Training, Colleges and Universities, the City of Toronto and the financial services sector of the Toronto region.

For more information on the CoE, please refer to: www.workinfinancialservices.com

The Brondesbury Group

The Brondesbury Group is a research and consulting firm that bridges the gap between market research firms and high-level strategy consultancies. The firm is built on a base of experienced professionals with backgrounds in financial services, government, education and organizational psychology. It typically works on projects that present challenges for most organizations – too much data, not enough information, or a need for specialized knowledge and research methods. The firm's specialty is finding out what decision-makers really need even when they are unable to articulate those needs themselves.

For more information on the Brondesbury Group, please refer to: www.brondesbury.com

PLEASE DIRECT QUESTIONS OR COMMENTS PERTAINING TO THIS REPORT TO:

DR. CATHERINE CHANDLER-CRICHLOW
Executive Director
Centre of Excellence in Financial Services Education
E-Mail: ccrichlow@tfsa.ca

MS. KAMINI SAHADEO
Director – Strategy Implementation
Centre of Excellence in Financial Services Education
E-Mail: ksahadeo@tfsa.ca

In collaboration with the Centre of Excellence in Financial Services Education, The Brondesbury Group consultants facilitated the research described in this report. The research team includes:

DR. ED WEINSTEIN
The Brondesbury Group
E-Mail: edwin.weinstein@brondesbury.com

Date of Publication: June 2014

Table of Contents

01

EXECUTIVE SUMMARY

Executive Summary

This study is a follow-up to a Pilot Workforce Survey completed earlier in 2013. That study identified insurance as an area of growth and the likelihood of talent shortages within the insurance industry.

This study builds on the earlier work, providing insights into the nature of growth in the industry, as well as more precisely identifying the types of talent the industry needs and the likely reasons for talent shortages.

While the study aims to be an encompassing overview of the industry, it is focused on two key areas and their implications:

- Key business trends, both international and domestic; and
- Talent attraction and mobility.

The report focuses on selected information from a wide variety of industry sources, primarily:

- Face-to-face interviews with 25 selected industry executives;
- Analysis of statistical sources identified by these executives as reliable industry standards; and
- Review of other selected articles on industry growth, structure and dynamics from credible sources.

The contents of this report should be of interest to:

- The Ontario Ministry of Training, Colleges and Universities;
- The Toronto Financial Services Alliance (TFSA) business development team;
- The Ontario Ministry of Finance;
- The Ontario Ministry of Economic Development, Trade and Employment; and
- Department of Foreign Affairs and International Trade Canada.

International Markets

Four Canadian life insurers make the list of top 50 global insurers: Manulife, Great West, Sun Life, and Industrial Alliance. Canadian life insurers write more business (Gross Written Premium) outside of Canada than they do in the domestic market. Insurance also represents a substantial portion of Canada's direct foreign investment. (Source: Swiss Re, "Canadian Life & Health: A Stable Industry Navigates the Financial Storm, November 2010). In contrast to life insurance, several Canadian P&C companies tried to compete internationally and failed.

The keys to success in the international market are:

- A deep understanding of how the local market has grown over time;
- Local trust in your brand;
- A robust supply chain; and
- Enough capital to meet the needs of these markets.

Foreign insurers create substantial employment in Canada, but do not create as many of the high-skilled head office jobs (locally) as domestic insurers. Canadian insurers expanding overseas create skilled jobs in Canada, but most jobs are necessarily generated in the region where the company locates its international offices. Regardless of domestic or foreign ownership, however, insurers often transfer high performers (in Canada) to foreign markets where they can generate greater returns.

P&C companies see Canada as a healthy and competitive market, with firms seeing higher growth in commercial lines rather than in the personal lines. Life insurers, in contrast, see Canada as a mature market with less growth than in the emerging markets. They see pockets of domestic growth in investment and annuities.

Internationally, regulation is seen as the main impediment to growth, as regulators demand that insurers increase reserve requirements, reducing the amount of capital that can be invested. The same environment that led to more regulation is keeping interest rates low. Combined with low equity returns, this makes it difficult for all types of insurers to earn good returns on their own capital and makes it very difficult for life insurers to meet the demands of their guaranteed products.

The strategies adopted by different insurers to mitigate these problems will drive the market over the next five years. The main strategies are:

- Pull out of markets where these forces hinder growth;
- Focus on medium- or high growth opportunities (regions, business lines, segments) to get better returns on capital investment;
- Focus on sales of products with higher margins; and
- Build non-guaranteed assets under management (AUM).

The availability of talent has also emerged as another obstacle to international growth. While the nature and magnitude of the shortage differs by country, it is a global issue.

P&C Insurance in Canada

In personal lines, growth potential looks best for the High-Net-Worth (HNW) and affinity markets, which makes customer service skills critical for growth, particularly in the HNW market. The mass market, in contrast, is driven by the adoption of technologies that help contain costs while increasing customer access.

On the commercial side, opportunities for growth are best in the natural resources sectors and in cross-border coverage. Growth is more tightly tied to opportunities for profitability. Profitability is driven by good risk models, underwriting, and actuarial skills.

The drivers of success in the P&C industry are good underwriting and managing costs. Like their global counterparts, Canadian P&C firms cite regulation, macro-economic trends, impact from catastrophes, weak investment performance and talent as issues that may hinder growth.

In past years, the industry has dealt with talent gaps by relying on productivity growth and by cross-training people. This has not been sufficient. The result is a number of talent gaps across functions including: underwriting, actuarial, risk management, compliance, marketing and technology areas of the business. These gaps appear to be most pronounced in high-skill positions such as actuarial, risk management and compliance. In addition, there is an indeterminate talent gap in a number of nascent areas, where some roles (e.g., social media marketers, enterprise risk managers, data specialists) are just starting to play a major part in industry success. While firms are confident these gaps exist, there is uncertainty on how pronounced the gaps actually are because these roles are so new.

Life Insurance in Canada

The economy was the major driver of the life insurance market over the past five years (2008-2013). The financial crisis led to more stringent capital requirements for life insurers, which has exacerbated the earnings pressure stemming from the low interest rates (and sometimes low equity returns) due to broad-based monetary easing (implemented to lessen the impacts of the Great Recession). The economic environment reduced the life insurance industry's risk appetite, driving down returns. As a result, the industry, faced with slow growth prospects, has increased its focus on cost-efficiency and productivity, catalyzing additional investment in people and systems to make it more competitive.

Looking ahead, the domestic life insurance industry in Canada is expected to grow at less than one-fifth of that in international markets, which suggests that capable insurers will be expanding internationally. (Recent international pullbacks were driven by a need to meet capital requirements rather than a real desire to exit overseas markets.)

Within Canada, there is general agreement that investment-related business lines will experience growth. The baby boom bulge will keep the investment and annuity business buoyant for the next 5-10 years, while group business lines will see a move to 'designer benefits' tailored to each individual plan member. Group retirement services are also expected to grow, as will efforts to retain retirement assets as employees retire.

There is no simple formula for success in life insurance. It takes a broad range of capabilities. Product innovation, good underwriting, effective marketing and sales, solid investment management, efficient administration systems, good client service and great claims handling are all needed skills for success. In addition, leaders must be best-of-breed risk managers, demonstrate leadership, and prudently manage capital to compete. Life insurance is a business that requires knowledge and skill to navigate, which is often contingent on experience. As a result, there is a lengthy development period for skills that has led to shortage of talent at intermediate levels.

Focusing on talent demand, projections of 5-6% hiring per year seem to be consistent with expected growth rates. For many high-skill positions, the rate of exit from retirement is equal to or greater than the hiring rate because the cohort to fill these positions is still getting the experience they need.

There are a few general themes that cut across the talent shortages in all areas of life insurance:

- Technical skills alone are not enough. Soft skills including communications, interpersonal skills, collaborative leadership skills and business acumen are needed for advancement in any technical field;
- Financial services are viewed as desirable. Within financial services, insurance is viewed as ”boring”;
- The Gen Y desire for work variety is at odds with the industry desire to build specialized experience;
- Insurers have not fully adapted to the lifestyle desires of Gen Y including: flex hours, work from home, and job mobility; and
- Retention is more of an issue than hiring. “Churn” is a big factor with new hires for all four of the reasons just mentioned.

The three biggest talent gaps are: Actuarial, Sales, and Information & Communications Technology (ICT). To a lesser extent, there are shortages in Marketing, Risk management and Claims adjudication.

Next Steps

1. Adapt working environments to meet Gen Y criteria.
2. Provide incentives to attract skilled expatriate Canadians back to Canada.
3. Attract qualified foreign professionals with a combination of job guarantees and a transitional program that helps them quickly earn the Canadian equivalent of their credentials. (Note: The CA’s have programs like this that can serve as a model.)
4. Accept industry accreditation courses for post-secondary credit.
5. Develop bridging programs for career shifters.
6. Include business communications and basic business skills in the curriculum for technical jobs.
7. Foster more cross-disciplinary training, both courses and co-op.
8. Independently study why people move to a new company, especially in other industries, to develop retention strategies.

   A comparison of compensation across financial services sectors should be an explicit part of this study.

9. The insurance industry needs to do more marketing within preparatory programs.
10. Provide HR departments with better information about re-deploying people from other sectors into financial services.
11. Adapt the TFSA Workforce Survey to get more precise numerical information on shortages with periodic special surveys.
12. Take a closer look at remedies to issues outside the scope of this report: regulatory harmonization, catastrophe funds, providing better overseas support to Canadian insurers, etc.

02

INTRODUCTION

Introduction

The Toronto Financial Services Alliance (TFSA) is a unique public-private partnership dedicated to building Toronto as a global financial services centre. Operating within the TFSA, the Centre of Excellence in Financial Services Education (CoE) offers a range of information and services to help foster Toronto's talent pipeline.

One of the TFSA's major aims is to assess the size of the Financial Services (FS) sector, the demand for talent, and the supply of talent. This effort is well underway. A substantial amount of information has been gathered about the size of the FS workforce and its demand for talent. To date, this information is quite high level.

In a human capital framework, understanding the competencies and experience the market requires demands a more granular understanding of market growth and what is driving it. The TFSA is pursuing this information as part of its mandate to further develop the Toronto Region as a Financial Services centre. With funding from the Ontario Ministry of Finance, the TFSA is pursuing a detailed understanding of those parts of the Financial Services Sector that are currently growing or anticipating growth.

The insurance industry has been identified as one of the sub-sectors of financial services that are currently experiencing growth. For the purposes of this report, the insurance industry is divided into two parts: Life & Health; and Property & Casualty. There are two other significant parts of the insurance industry that align their activities to the fundamental split between insuring "people" (life & health) and "things" (property & casualty). These two groups, reinsurers and independent agents & brokers, formed part of the base of commentators for this study.

There are two primary questions that this study aims to address:

- What business reasons will drive changes in staffing in the regional insurance industry over the next 3-5 years?
- What can be done to enhance the competitiveness of the insurance industry in Ontario over the next decade, both in terms of revenue and employment?

To answer these primary questions we need to understand the structure and dynamics of the insurance industry, both domestically and internationally. We need to understand the opportunities for growth in the insurance industry including the specific business lines that are likely to grow and the kinds of talent those business lines require.

This report will address the issues in five brief chapters. In addition to this Introduction, the remaining four chapters are as follows:

- The International Market
- Property & Casualty;
- Life & Health;
- Enhancing Competitiveness.

Supporting evidence will be drawn primarily from personal interviews with industry experts. As a complement to the interviews, we will cite findings from relevant literature and statistical sources that address the two primary questions.

On behalf of the TFSA-CoE, we would like to thank the industry experts who gave us their time and their thoughtful views on the insurance industry. In alphabetical order, the people we interviewed are listed below, along with their position at the time of the interview:

Bialy, Leszek Vice President, Head of Customer & Distribution Management, Global Corporate Zurich Canada	**Hendrickson, Deborah** Senior Vice-President, Broker & Customer Care Claims & Customer Service Operations Aviva Canada
Cohen, Steve Senior Vice-President, Personal Lines Underwriting & Pricing Aviva Canada Inc	**Ingham, Darryl** Vice President, Toronto Office SSQ Financial Group
Comerford, Gary Executive Vice President & Chief Marketing Officer RGA International	**Lorentz, Paul** Executive Vice President & General Manager, Insurance & Investment Solutions, Retail Markets Manulife Financial
Coskery, John Vice President, Property XL Reinsurance America	**Ludlow, Sharon** President & Chief Executive Officer Swiss Reinsurance Company Ltd
Dixon, Rohan Executive Vice President, Chief Brokering Officer AON Reed Stenhouse Inc	**Marcotte, Louis** Senior Vice-President Strategic Distribution Intact Financial Corporation
Gibson, Edward Senior Vice President, Strategy & Chief Actuary Empire Life	**Mason, Karen** Senior Vice President, Group Equitable Life of Canada
Gove, Peter Senior Director, Disability Management & Life Insurance SSQ Financial Group	**McKay, Paul** Vice President & Deputy Global Compliance Chief Manulife Financial

Monteith, Stuart Senior Vice President, Group Benefits Sun Life Financial	**Toffick, Neil** Registrar Insurance Institute of Canada
Oxenham, Rose Senior Vice President, Risk Services Northbridge Insurance	**Watchorn, Lee** Board Member, Equitable Life of Canada Past President, Sun Life Financial (Canada)
Polson, Eileen Vice President, Business Partner, Individual Insurance Sun Life Financial	**Watson, Philip** Vice President, Appointed Actuary Equitable Life of Canada
Posthuma, Gerald Vice President and Head of Global Asset Liability Management Manulife Financial	**Zimmerman, Oscar** Senior Vice-President & Managing Director, Corporate Insurance Scotiabank
Reibel, Sue Senior Vice President & General Manager, Group Retirement Solutions Manulife Financial	
Reid, Thomas Senior Vice President, Group Retirement Services Sun Life Financial	
Ruiz, Francis President Insurance Career Network	

03

INTERNATIONAL INSURANCE MARKETS

International Insurance Markets

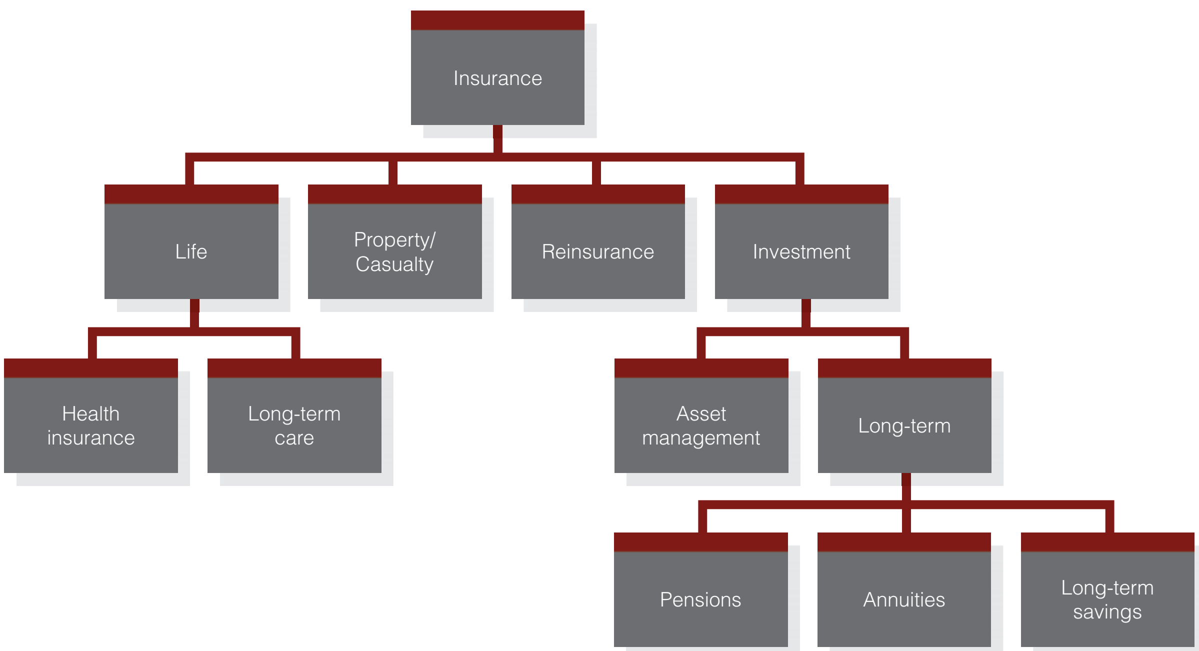
In the domestic insurance market, firms are distinctly divided into Life & Health ("Life insurers") or Property & Casualty ("P&C"). In the international insurance market, this neat distinction is not the norm. Thus the way we describe international markets will differ from later chapters on the domestic market, but we will structure the chapters to be as comparable as possible.

Market Structure

When we reviewed material on global insurance firms, their activities were described in four major categories: Life, Property & Casualty, Reinsurance, and Investment.

Life, P&C, and Reinsurance companies all invest their own money to improve their profitability, but several also invest client money as a source of revenue. There are several businesses focused on asset management including: mutual funds, segregated funds, pooled funds, and other investment products. Insurers also have several products that hold invested assets on behalf of their beneficial owners including: pensions, annuities, and long-term savings (e.g., retirement savings plans, educational savings plans, etc.).

Exhibit 2.1 International Overview of the Insurance Business



Major Competitors

There are many ways to rank global insurers including: assets, market capitalization, gross written premium and more. A.M. Best, the leading firm for rating the creditworthiness of insurers, uses assets as the basis for ranking. It is more stable than other measures. Exhibit 2.2(next page) shows the Top 50 global insurers (excluding reinsurers) ranked in descending order according to their assets. Assets are measured using US dollars at the end of 2012.

The top 10 global insurers all have $500 billion or more in assets. Some 3 of the top 10 are from the US; the UK and Japan have 2 insurers each; and the remaining 3 insurers come from the rest of the EU.

Six of the top 10 insurers (highlighted in pink) are active in both the life and P&C markets. Aviva is active in P&C, while the other three are active in life insurance. Virtually all are active in investments.

Four Canadian insurers make the list of top 50 global insurers (highlighted in blue): Manulife (#12), Great West (#23), Sun Life (#24) and Industrial Alliance (#47).

Manulife with $488B in assets is considered to be a major player in the insurance market. Great West and Sun Life, with approximately half of Manulife's asset base, is classified as mid-tier. Industrial Alliance is at the lower end of the league tables with $42B in assets. It is the only one of the four companies with significant P&C operations.

In the judgment of our respondents with international experience, no Canadian P&C firm has substantial international activity. A few have tried to compete internationally and have failed. Canadian P&C firms don't have enough size for the US market (e.g., capital and organization) and have no experience in markets further afield. It is also hard for Canadian P&C companies to reinsure risk outside Canada.

Manulife (MFC) and Sun Life Financial (SLF) are the primary Canadian competitors in the international market. Great West Life (GWL) primarily competes in North America and the UK. Both of the leading international firms have over 100 years of offshore experience in Asia.

EXHIBIT 2.2 TOP GLOBAL INSURANCE COMPANIES 2013				
RANK	COMPANY	COUNTRY	TOTAL ASSETS, US$B, (31/12/2012)	MARKET CAP, US$B, (MAY 2013)
1	Japan Post Insurance	Japan	$ 1,083.0 *	-
2	AXA	France	$ 1,009.5	-
3	Allianz	Germany	$ 920.4	-
4	MetLife	USA	$ 836.8	$ 44.6
5	Prudential Financial	USA	$ 709.3	$ 30.7
6	Nippon Life Insurance Company	Japan	$ 622.5 *	-
7	Assicurazioni Generali	Italy	$ 585.3	$ 28.6
8	Legal & General Group	UK	$ 562.9	$ 16.5
9	American International Group	USA	$ 548.6	$ 67.0
10	Aviva	UK	$ 512.7	$ 14.5
11	Prudential plc	UK	$ 489.4	$ 45.9
12	Manulife Financial	Canada	$ 488.2	$ 28.4
13	AEGON N.V.	Netherlands	$ 485.1	$ 13.3
14	CNP Assurances	France	$ 467.7	-
15	ING Verzekeringen NV	Netherlands	$ 450.3	-
16	Dai-ichi Life Insurance Company	Japan	$ 403.9 *	$ 13.4
17	Meiji Yasuda Life Insurance Company	Japan	$ 360.9 *	-
18	China Life Insurance	China	$ 304.6	$ 79.9
19	Sumitomo Life Insurance Company	Japan	$ 291.5 *	-
20	Standard Life	UK	$ 283.0	$ 13.5
21	Predica [1]	France	$ 271.6	-
22	Life Insurance Corporation of India (LIC)	India	$ 267.5	-
23	Grest-West Lifeco [2]	Canada	$ 251.8	$ 26.5
24	Sun Life Financial	Canada	$226.8	$ 16.9
25	Lincoln National	US	$218.9	$ 8.9
26	Resolution Limited	Channel Islands	$ 207.5	$ 6.0
27	Northwestern Mutual Life Insurance	USA	$ 202.5	-
28	ERGO Insurance Group [3]	Germany	$ 195.1	-

EXHIBIT 2.2 TOP GLOBAL INSURANCE COMPANIES 2013 (CONTINUED)				
RANK	COMPANY	COUNTRY	TOTAL ASSETS, US$B, (31/12/2012)	MARKET CAP, US$B, (MAY 2013)
29	Swiss Life Holding	Switzerland	$ 178.7	$ 5.1
30	Massachusetts Mutual Life Insurance Company	USA	$ 167.5	-
31	Cathay Life Insurance	Taiwan	$ 165.3	$ 14.3
32	Principal Financial Group	US	$ 161.9	$ 10.9
33	T&D Holdings	Japan	$ 156.9	-
34	Samsung Life Insurance	South Korea	$ 142.2	$ 17.7
35	Phoenix Group Holdings	Channel Islands	$ 139.8	$ 2.2
36	AIA Group	Hong Kong	$ 134.4	$ 53.5
37	Aflac	USA	$ 131.1	$ 23.9
38	Ageas	Belgium/Netherl	$ 128.7	$ 9.2
39	China Pasific Insirance (CPIC)	China	$ 109.3	$ 28.6
40	New China Life Insurance	China	$ 79.2	$ 11.8
41	Shin Kong Financial	Taiwan	$ 70.0	$ 2.7
42	Unum Group	US	$ 62.2	$ 7.5
43	Hanwha Life Insurance [4]	South Korea	$ 61.0	$ 5.3
44	Protective Life	US	$ 57.4	$ 2.9
45	Sanlam	South Africa	$ 52.3	$ 10.7
46	Mediolanum	Italy	$ 43.7	$ 5.0
47	Industrial Alliance Insurance	Canada	$ 42.0	$ 3.5
48	MMI Holdings	South Africa	$ 36.8	$ 3.9
49	American Equity Investment Life Holding	US	$ 35.1	$ 1.0
50	CNO Financial Group	US	$ 34.1	$ 2.6
51	Symetra Financial	US	$ 29.5	$ 1.6
52	Torchmark Corp	US	$ 18.8	$ 5.9

*Figures are for fiscal year ended March 31, 2012

[1] Predica is a life insurance subsidiary of Crédit Agricole Assurances.

[2] Great-west Lifeco is a subsidiary of Power Corporation of Canada.

[3] ERGO is a subsidiary of Munich Re, one of the leading reinsures and risk carriers worldwide.

[4] Hanwha Life was formerly known as Korea Life Insurance and changed its name in October 2012.

Source: http://www.bestlifeinsurers.com/top-life-insurance-companies/world-assets

We treat reinsurers as a separate part of the market, and for completeness, we have listed the top 10 global reinsurers, none of whom are Canadian. (Note that reinsurer rankings are based on gross written premium rather than assets.)

EXHIBIT 2.3 TOP 10 GLOBAL REINSURERS		
RANK	COMPANY	GROSS WRITTEN PREMIUM (2011, USD $B)
1	Munich Reinsurance Company	$ 33.7
2	Swiss Reinsurance Company Limited	$ 28.7
3	Hannover Rueckversicherung AG	$ 15.7
4	Berkshire Hathaway Inc	$ 15.0
5	Lloyd's	$ 13.6
6	SCOR SE	$ 9.8
7	Reinsurance Group of America Inc	$ 7.7
8	China Reinsurance Group	$ 6.2
9	PartnerRe Ltd	$ 4.6
10	Korean Reinsurance Company	$ 4.6

Source: A. M. Best

The aggressive competitors in the global market include Prudential plc (UK), AIG (AIA), Allianz, and Manulife. Sun is a question mark. Generali is in retreat.

- Prudential (UK) went from being a UK-based insurer to an Asian-based life insurer in 10 years. They have a diversified life products strategy that includes asset management.
- AIA (AIG) is back and very active. Despite problems in the US, they never lost international reputation.
- Allianz, like most EU life insurers is repositioning to meet the capital requirements of Solvency II. This is leading to both market exits and entries to balance growth and capital. Allianz like most EU insurers is not agile.
- Manulife is strong in Asia with a presence that dates back to the 1880's. Third-party research reports reinforce this view of MLF's position in Asia. Its position in North America is more challenging overall, especially in Canada.

Canadian Competitors in the International Market

Canadian life insurers write more business outside of Canada than they do in the domestic market. Although two-thirds of this business is in the US, Canadian life insurers are making substantial inroads in Asia and Latin America. Manulife, Sun Life and Great West Life account for most of this. Insurance represented 14% of Canada's direct foreign investment in 2008. (Source: Swiss Re, "Canadian Life & Health: A Stable Industry Navigates the Financial Storm, November 2010). Recent statistics are consistent with the Swiss Re estimate of 14%, since they show that the Finance, Insurance & Management sector account for 53% of Canada's direct investment abroad (Source: Statistics Canada, "The Daily", May 9, 2013).

As an indicator of performance, let us look at the strongest international competitors as viewed by leading equity research analysts.

A February 2013 TD Securities Equity Research report says of Manulife Financial (MFC): (Note: verbatim quotes from the report)

- Sales growth in Asia was impressive…Wealth management sales were more than doubled [sic].
- US wealth management sales were strong. Sales increased 44% y/y.
- Core EPS was lighter than expected.
- There remains a big gap between core earnings of $2.2B in 2012 and management's target of $4.0B in 2016.

A BMO Capital Markets report on MFC (February 2013) gives some details on Manulife's performance by region.

- Growth in wealth management sales between 2011 and 2012 were 38% for Asia, 4% in the US and (7%) in Canada.
- Growth in insurance sales between 2011 and 2012 were 17% for Asia, (6%) for Canada and (3%) for the US.

The other international competitor from Canada, Sun Life Financial (SLF) has more uncertain positioning.

- Sun has largely exited the UK and Europe. It has no more individual life in the US.
- In Asia, Sun owns 25% of a domestic company in China. By necessity, such a small share means the PRC partner dominates.
- The value of Sun's company in Hong Kong has eroded since its purchase.
- Philippines is a great operation and profitable with good growth.
- According to the 2012 Sun Life Annual Report, SLF owns 26% of the voting shares in Birla Sun Life (India). As we understand it, Birla Sun Life is now largely run by the Birla family.
- Sun has some brand image issues in Malaysia and Vietnam emanating from their purchase of local companies.

Looking at a recent research report on SLF from BMO Capital Markets (dated February 2013), we note the following comments.(Note: verbatim quotes)

- Asia earnings growth continues to be challenged.
- Sales were mixed…Canada insurance and wealth management sales were down 6% and 10%, respectively, Asia insurance down 20% and US group up 35%...Canada group sales were strong, up 36%
- Capital continues to be good.

The TD Equity Research report on SLF from February 2013 is more positive. The differing views help explain why commentators view SLF as a question mark. From the TD report, we add the following observations. (Note: verbatim quotes)

- MFS (its majority owned US asset management operation) had another stellar quarter.
- Premium and deposits grew 49% y/y and this should help ease concerns about growth outlook.
- US employee benefit group (EBG) sales increased by 25%...The US EBG division made no money. This was due to building out the platform.

Great West Life (GWO) substantively operates in Canada, the US and the UK/Ireland. With the recent acquisition of Irish Life, their business in the region will be more substantial. GWO is an integral part of Power Financial Corporation (PFC), which is active in banking in Europe. GWO's fortunes are more tied to the North American economy than those of MFC and SLF. A BMO Capital Markets report on GWO (February 2013) gives some details on its performance.

- In Canada, sales on most product lines are up, but profitability is down except in Group insurance.
- Sales in the US are down, but net income is up largely due to some tax benefits.
- The UK/Isle of Man operations saw a 57% increase in sales and a 50% increase in Premiums & Deposits YoY, but net income was down.

As an indicator of the current prospects for these three companies, we note that a recent TD Action Report (June 2013) gives a "Buy" recommendation for Manulife and Sun, while suggesting a "Hold" for GWO (and Industrial Alliance).

International Success Factors

While the US continues to get most Canadian direct investment abroad, when we think of "International Success" in the current global environment, we are mainly talking about growth prospects in the emerging markets, especially in Asia and Latin America.

Commentators suggest that to succeed in Asia, you need to have 'international' as part of your organizational DNA. SLF and MFC have been in Asia for more than 100 years and have people who understand the local market. The key issue in the international market is the trust in your brand. You need people on the ground feeling part of an international culture and not an isolated outpost. There is an incubation period for building international culture. It can't be bought or built, but has to grow over time.

People also underestimate the extent of the local supply chain that is needed to support international operations. This includes: regional underwriters and actuaries; HR; regional marketing; and more to support country efforts. The international market takes excellence. The actuaries need to be the top 1%.

Several small life insurers tried to succeed in Asia in the 80's and 90's, including a few Canadian firms (e.g., Laurentian, Mutual). None of them succeeded. A few of these efforts bankrupted or severely impaired their parent company in the process, leading to the sale of the parent to a stronger life insurer. Those who have succeeded, SLF and MFC, have a long history in Asia.

Several Canadian P&C companies tried to compete internationally and did not succeed. Kingsway and Queensway both failed in their attempts to enter the US market. Canadian P&C firms don't have the market experience and knowledge they needed to underwrite successfully, **nor did they have the capital needed** to deal with large-scale catastrophes. Under these circumstances, reinsurers were reluctant to provide cover.

With the exception of TD in the US, only Scotiabank has substantively ventured into the insurance market internationally. Insurers believe that banks don't have the culture to compete successfully and focus on simple commoditized product. Banks are seen as reluctant to pay commissions, thereby making the local brokerage networks inaccessible to them.

Nonetheless, Scotiabank is operating successfully in the international insurance market in a modest way. This bank insurer operates in many countries, typically wherever the bank has retail operations. Their offerings differ by country, but creditor insurance is most common with P&C following. In Canada, they are in both the creditor life and the P&C market. In most markets, Scotiabank prices products, distributes and pays claims. They usually hire a third-party to provide the actual product. The driving factor in their choice of products in each market is the Return on Equity (ROE).

Besides fiscal discipline, Scotiabank's success in international insurance markets does follow the maxim early in this section. As the most international of the Big Five Canadian banks, Scotia has the greatest depth of international experience. In addition, Scotia typically enters foreign markets by buying a significant stake in an existing bank. Through these partnerships, they gain the local knowledge and local brand strength that are needed for success.

For some international firms, especially German and Swiss, their home country regulations give them an advantage in international markets that Canadian companies don't have. On the P&C side (including reinsurance), one of the main reasons that German and Swiss insurers have been so successful is a difference in taxation on reserves held to pay for catastrophes. German and Swiss insurers can build these reserves without paying tax on either the reserve or the investment income on the reserve. The policy has allowed German & Swiss companies to cover catastrophic losses without creating insolvencies. With the exception of a very recent policy allowing tax breaks for earthquake insurance reserves in Canada (especially BC), there is no comparable policy here.

Employment Creation

International operations have an upside and downside for jobs.

In P&C and reinsurance, Canadian firms aren't active internationally, but foreign companies are active in Canada. In the views of our respondents, this creates three impacts:

- Foreign operations create substantial employment in Canada;
- The P&C business is increasingly automated, and as such, there is no push to outsource local labour to other countries. The jobs created here will stay (if they are not automated); and
- Successful mid-career talent has been transferred to markets where their skills can earn more for the company, especially the US and UK. We understand that some of this talent is now getting repatriated to fill senior positions in Canada.

Life insurance companies like MFC and SLF have hundreds of employees in Ontario to meet the needs of US and international operations. These are often skilled head office jobs. But by necessity, the bulk of employment created by international operations must be located in the regional market. And as we saw for the foreign P&C companies in Canada, this is exactly what happens.

Opportunities in Canada

Chapters 3 & 4 will deal at greater length with opportunities in Canada, but for now we provide a brief overview of Canada in an international context.

P&C companies generally deem Canada a healthy but competitive market. Opportunities are generally viewed as more positive in the commercial lines than in personal lines (see chapter 3). Growth in the Small-Medium Enterprise (SME) segment looks particularly good in Canada, as do selected segments for personal property.

Several other circumstances make Canada attractive for P&C:

- It has favorable loss ratios compared to most global markets including the US;
- Commercial lines have been especially profitable in Canada.
- Higher home prices have raised the cost of home insurance premiums;
- There have been no major catastrophes in relative terms; and
- With increasing reliance on technology and need for capital, there are opportunities for consolidation and acquisition. Smaller companies are at a disadvantage.

A recent TD Securities report on Lifecos in Canada is bullish on the Canadian market, saying "Following a few rounds of life insurance price increases, risk mitigation actions, a renewed focus on expenses, and expansion of wealth management operations in what we call a rational market, the Canadian Lifeco divisions are poised to show above-normal bottom-line growth, in our view…Although the report focuses on Canada, we could not ignore the recent changes in macro conditions, specifically interest rates and the improved mood around the Lifeco sector." (Source: TD Securities Action Notes, June 7, 2013). This report cites several clear growth opportunities:

- The ability to offer guaranteed retirement payout products which banks can't offer;
- The expansion of defined contribution pension plans, a market largely dominated by Lifecos;
- A shift back to participating whole life products and away from universal life products; and
- Improved profitability of individual insurance segments.

For life insurers, Canada is a mature market with growth likely in the 0-6% range, but this growth can vary significantly between different product lines. Where growth is limited, it is often due to the low interest rate environment. Domestic carriers write more than 90% of all life and health premium (Source: Swiss Re, Canadian Life & Health, November 2010). The Big Four life insurers write more than 50% of all business.

Growth in Canada is expected to be less than one-fifth of growth in international markets, but there are areas of opportunity (Source: TD Securities Action Notes, June 7, 2013).

- Many believe that younger Canadians are massively under-insured for income replacement protection and life coverage.
- Tied to the under-coverage is a need for more products to serve the self-employed market cost effectively.
- SME need to "catch-up" with the benefits they offer.
- Annuities have lots of room for growth.

The real growth opportunities on the individual side are insuring longevity risks rather than mortality risks. Products that insure morbidity (risk of disease or infirmity) are growing in popularity but building acceptance takes time.

Market Dynamics

Three problems plagued life insurers over the past 5-10 years: over-guaranteed products, low interest rates, and the global liquidity crisis. The global liquidity crisis was exacerbated by regulatory demands for more capital, which insurers attribute to regulators confounding the respective capital needs of banks and life insurers.

Some of the key affects of these three core problems were:

- Whole life, annuities and several investment products guaranteed minimum returns. The promise of a 3% guaranteed return seems safe in a 6% interest rate environment, but these guarantees are costly to meet in the current (low interest) environment;
- Life policies have assumed inflation as part of how they meet their obligations to grow. The expected levels of inflation, as reflected in low interest rates, have not materialized;
- The bank liquidity crisis in 2008 quickly migrated to the life insurance sector. With a lack of funds available to provide emergency reserves and a shortage of reinsurance, many life insurers were forced to sell off assets to meet their guarantee obligations; and
- The reinsurance sector came back fast and has helped life insurers capitalize to meet the ever more stringent capital requirements imposed by regulators, but to do this Lifecos often sold a chunk of their profitable business to the reinsurers.

Smaller companies often suffered more, especially new entrants, because regulators were less comfortable with their business. Regulators prefer 'experienced business'.

Life Insurers needed "financial heft" to survive the perfect storm of 2008. Three Canadian Lifecos had the heft needed, but two suffered consequences. GWO survived well. MFC and SLF suffered as a result of the guarantees in their US product portfolios. SLF continues to "de-risk" its global product portfolio.

Regulation & Capital

Regulation is an issue for insurers around the world. The concerns about regulation include: the volume of regulation being enacted, the cost of compliance, the uncertainty for business, and more. In a global survey of some 500 practitioners, it was seen as the #1 challenge for the industry, up from the #5 position two years before (source: Centre for the Study of Financial Innovation, Insurance Banana Skins 2011, p.5).

Regulators from around the world are meeting (recently in Toronto) and increasingly harmonizing the rules. The ability to "arbitrage regulations" is vanishing.

Much of the regulation troubling insurers is that regulatory authorities are treating them like banks with regards to capital requirements. Solvency II imposes new capital requirements. As it stands now, it will not be fully implemented until 2018, but local authorities institute comparable requirements before that. The unpredictability of regulation is part of insurer concern. As an example, we note that the timelines for Solvency II have changed several times. The rules remain unknown and the timelines suspect.

With three potential levels of regulation (global, national, provincial), insurers increasingly worry that clarity on regulation is often not available until near the expected implementation date. The result is that firms are unable to comply with the regulations on time. The date for implementation then gets extended, and in the interim, regulators make more changes, creating additional uncertainty.

In terms of opportunity created by regulation, Toronto is recognized globally as a world centre for good governance and regulation. People from around the globe come here to Toronto to study regulation, a position that the region should take advantage of. There is the Institute on Governance (Ottawa, Toronto) and the International Actuarial Association is located in Ottawa but active here. Two other organizations are active too.

Other Issues Affecting Growth

The first four concerns noted in 'Insurance Banana Skins' are all tied together. Regulatory compliance increasingly requires that insurers hold more capital, which dampens the availability of capital for growth. The same environment that led to more regulation is keeping interest rates low ("quantitative easing"). This has made it difficult for insurers (of all types) to earn a sufficient return on capital, and, for life insurers in particular, makes it very difficult to meet the demands of their guaranteed products.

The remedies to these issues different insurers choose will drive the market over the next five years. Superficially, the strategies we see are:

- Pull out of markets where these forces are a 'big drag' on growth;
- Go to medium-high growth markets (regions, products, segments) to look for better returns on capital investment;
- Focus on sales of products with higher margins; and
- Build non-guaranteed assets under management (AUM).

Continuing with the concerns raised in 'Insurance Banana Skins', we note that natural catastrophes are #5 on the list. While we recognize there is little that can be done about these events, but the consequence of the increase in weather-related catastrophes is a major concern (this is discussed in the next chapter). Now, let us turn to the #6 issue, which is talent.

Talent Gaps

The most important thing to note about 'Talent' is that it was not on the list of Top 25 concerns in 2009. **Over the last few years, talent has emerged as a global issue.** CSFI talks about the difficulty the industry has in attracting and retaining top quality talent. In some emerging markets, the industry is relatively new and lacks widespread recognition, while in developed markets the industry is often seen as 'boring and conservative'.

The CSFI report indicates that attracting and retaining high quality talent is far more serious in Asia and the Middle East (ranked #2), and to a lesser extent the Far East (ranked #3). In Europe, talent is ranked #10 and not a big issue overall, but in the highly competitive London market it is ranked #4. In North America (including Bermuda) it is ranked close to the global average (rank #7).

As we understand it, there is a shortage of underwriters for specialty areas. These underwriters require substantial experience and a training placement in order to build their skills. Interviews suggest that compliance and risk management may be siphoning off some of the best talent, since both are high demand areas where competition for talent is substantial.

We note that talent is far less of an issue for reinsurers than for insurers. Several commentators shared this concern, noting that reinsurers (and brokers) need top talent and pay more for it than insurers. We speculate that compensation may be more of an issue for the industry, especially at mid-career levels, than an intra-industry report is likely to identify. Too, we suspect that top talent may be drawn to better paying markets in the current environment.

Insurance Banana Skins 2011

(2009 ranking in parenthesis)

1. Regulation (5)
2. Capital (3)
3. Macroeconomic trends (4)
4. Investment performance (1)
5. Natural catastrophes (22)
6. Talent (-)
7. Long-tail abilities (10)
8. Corporate governance (17)
9. Distribution channels (16)
10. Interest rates (11)
11. Political risk (18)
12. Actuarial assumptions (9)

04

DOMESTIC PROPERTY & CASUALTY

Domestic Property & Casualty

This chapter summarizes the structure, dynamics, growth opportunities and talent needs of the Ontario Property & Casualty insurance market.

Market Structure

The Top 20 Property & Casualty (P&C) insurers in Ontario are shown in Exhibit 3.1. They are listed in descending order based on the amount of direct written premium[1] (DWP) they generated in 2012 in Ontario. The final column of the exhibit shows their share of the entire Canadian market.

As one can see, the Top 20 P&C insurers generated some $18.3 billion in DWP in Ontario. The first six companies on the list all generated more than $1 billion in DWP last year (source: Canadian Underwriter Statistical Issue, June 2013).

The Top 20 In Ontario are also major players in the Canadian market, accounting for 81% of Net Written Premium (NWP) in Canada (Note: NWP is DWP less commissions and reinsurance). Seven of these carriers generate half of Canada's NWP in the P&C market. Intact and Aviva generate almost one-quarter of the NWP on their own. Along with TD general insurance, they are the 'big three' players on the personal side. On the commercial side, Canadian underwriter refers to the 'big four' companies as Lloyds, Northbridge, Zurich and AIG.

EXHIBIT 3.1 TOP 20 P&C INSURERS IN ONTARIO

COMPANY	DIRECT WRITTEN PREMIUMS (TOTAL BUSINESS - ONTARIO 2012)	GROSS WRITTEN PREMIUM (2011, USD $B)
Intact Financial Corporation	$ 2,743,765,000	15.06
Aviva Canada Inc	$ 1,922,923,00	8.23
TD Insurance, General Insurance	$ 1,666,789,000	6.33
State Farm Insurance Company	$ 1,633,960,000	4.41
RSA Canada Group	$ 1,295,369,000	6.00
Economical Insurance	$ 1,023,994,000	4.13
Co-operators General Insurance Co	$ 981,177,000	4.84
The Dominion of Canada	$ 951,240,000	2.89
Allstate Insurance of Canada	$ 772,802,000	2.49
Desjardins General Insurance Group	$ 750,150,000	4.65
RBC General Insurance / RBC Insurance	$ 418,706,000	2.25
Wawanesa Mutual Insurance	$ 667,517,000	4.99
Ontario Mutual Insurance	$ 663,091,000	1.29
Northbridge Financial Corporation	$ 560,556,000	2.27
Lloyd's Underwriters	$ 724,265,000	5.01
Zurich Insurance Company Ltd	$ 351,308,000	1.54
Chubb Insurance Co of Canada	$ 349,579,000	1.45
Chartis Insurance Co of Canada	$ 332,154,000	1.49
Gore Mutual Insurance Company	$ 279,740,000	0.76
Jevco Insurance Company	$ 241,684,000	0.89

Source: Canadian Underwritier Statistical Issue. June 2013. Web.
<http://www.canadianunderwriter.ca/issues/de.aspx?sp=1>

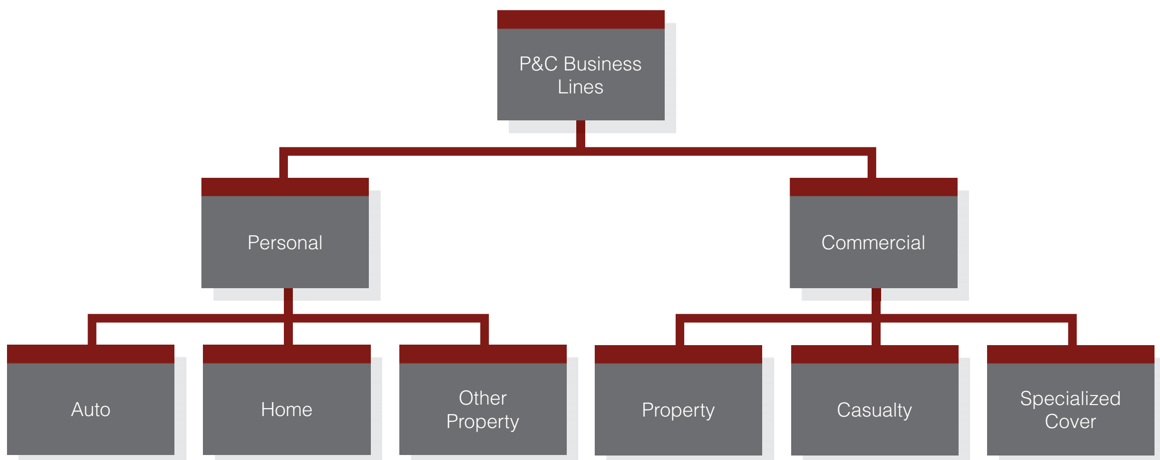
[1] Direct written premium is the total amount of an insurer's written premiums without any allowance for premiums ceded to reinsurers. (Source: International Risk Management Institute, 2013)

Organizing Models for the Business

There are three types of Property & Casualty (P&C) insurance carriers: Domestic (e.g., Intact); Global/NA (e.g., Zurich, AIG); and Specialists (e.g., QBE). The major division amongst P&C insurers is Personal versus Commercial lines.

Personal lines consist mainly of largely: auto, home, and other property. The commercial market lines divide into: property; casualty (e.g., general liability, Directors & Officers, Errors & Omissions, etc.); and specialized cover (e.g., Environmental, Marine, etc.).

Exhibit 3.2: P&C Business Lines



Segment Overview

In addition to organizing by business lines, P&C insurers often organize business around customer segments. The segments in the personal lines market are: mass market, affinity groups, and High-Net-Worth (HNW). Commercial market segments are more varied by company and typically based on size (small business, commercial, institutional), geographic spread (domestic, cross-border, global), or specialized industries (e.g., mining, energy, etc.).

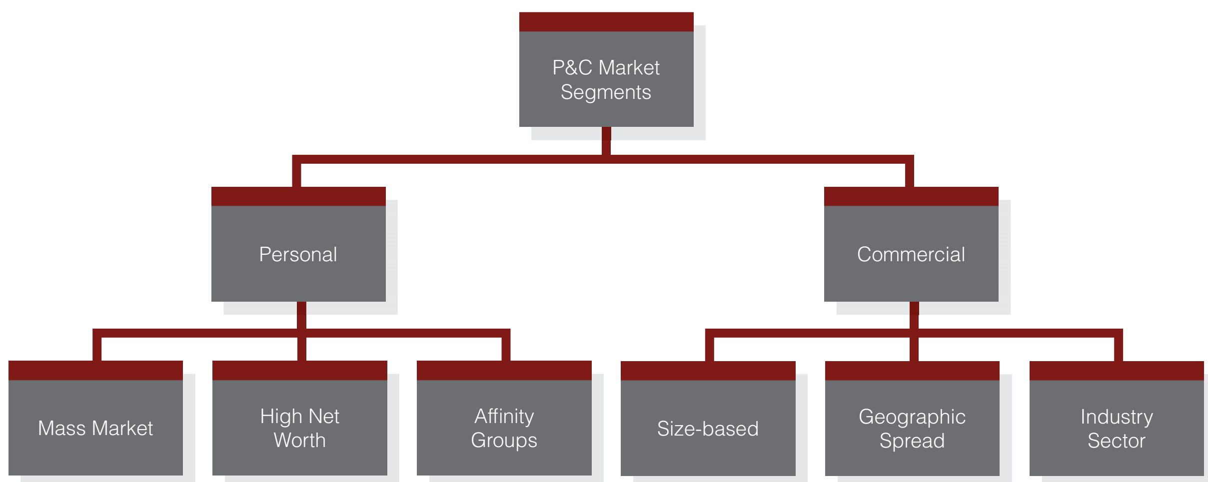
Personal lines carriers improved their performance in 2012, but this was uneven across firms. The bottom quartile of personal line insurers paid out more in claims than they earned in premium (Source: Canadian Underwriter Statistical Issue, June 2013). Smaller companies were at a disadvantage because they lack the scale necessary to compete for "mass market" business. P**ersonal lines are increasingly sold direct or on the web to both the mass market and the affinity market** (e.g., alumni associations, professional associations, etc.). In addition, a focus on technology has led to consolidation of brokers on the personal side and limited access to mass markets. **Future growth for brokers is likely to focus on the high-net-worth market.**

Despite limitations on growth in the personal lines market, we are seeing aggressive growth at Intact, Aviva and Royal Sun Alliance (RSA). They have grown both organically, and, in some cases through acquisition. Banks are also actively going after the personal lines business, both mass market and affinity groups (TD). The need for technology to sell and deliver personal lines has led to consolidation as companies seek the scale needed support the technologies that competitiveness. Banks have a technology platform they can build on.

While personal lines are a 'consolidation story', commercial lines, in contrast, are seeing new entrants drive competition. Insurers focusing on commercial lines have been more profitable than those focusing on personal lines, leading to greater price competition in commercial markets. While some have entered this market through acquisitions, the majority of firms choose to build their businesses organically. **In order to build, new entrants typically raid experienced actuaries and underwriters from existing firms.**

In the commercial lines market, aggressive growth is being pursued by AIG, Zurich (in the mid-market), RSA, QBE and ACE. To a lesser extent, growth is also pursued by: Allianz, ARCH, Axis, FM Global, and XL Group (esp. for Environmental liability). Multi-line companies like Aviva and Intact also showed good growth.

Exhibit 3.3: P&C Market Segments



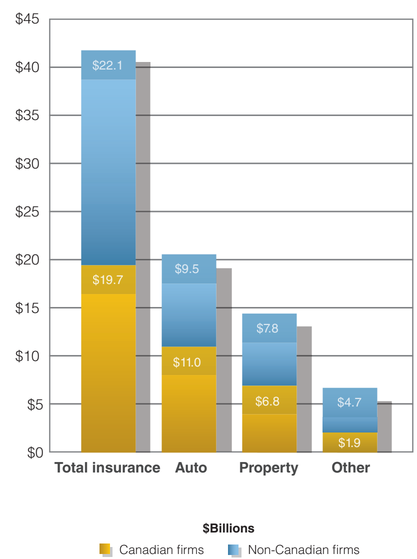
Business Line Overview

Ontario auto premiums represent roughly one-quarter of all P&C premium in Canada (Source: Canadian Underwriter Statistical Issue, June 2013). In 2012, direct written auto was $12.4 billion for Ontario versus $20.7 billion for Canada as a whole. Premiums in Ontario are higher than in other regions of Canada due to exceedingly high levels of fraud, especially disability. Limitations on bodily injury claims, instituted in 2010, have helped many carriers recover from major losses in earlier years, however, recently proposed limitations on premium, combined with a number of adverse court decisions threaten to end this brief period of recovery. Some personal lines writers are considering exiting the auto insurance market in Ontario, which would certainly result in a significant loss of employment in the industry within Ontario. The main offset to auto premiums are healthy rates on homeowner's policies. Rising real estate values have made the home insurance line reasonably attractive.

Overall, the measure of fiscal health that Canadian Underwriter uses most often is 'Direct Loss Ratios'. A direct loss ratio (DLR) is the proportion of total premium that is paid out for losses (source: IRMI, 2013). It does not include commissions, company operating expenses or other costs, but rather reflects the quality of underwriting. A direct loss ratio of 60% means that for every $100 of premium gathered, $60 is paid out for claims. Thus loss ratios are like golf scores, the lower they are the better the performance.

Using DLR as our guide, we find that the health of the personal auto business improved a small amount between 2011 and 2012 (76% to 74%), while personal property showed the greatest improvement in DLR (69% to 58%). On the commercial side, we saw 6-7% improvements in DLR for commercial property and commercial liability (source: Insurance Bureau of Canada and MSA as reported in the Canadian Underwriter Statistical Issue, June 2013).

Exhibit 3.4 Net Premium Written by Business Line (Canada)



Overall, Canadian firms wrote 47% of Net Premium (see Exhibit 3.4) for P&C. The proportion was 53% in the relatively low margin auto insurance business and much lower in the specialized 'Other property' lines. Across business lines, Canadian firms had loss ratios that were about 2½ % lower than industry average.

Banks in the P&C Market

Banks focus on personal lines including some specialty businesses. They typically offer simplified products that are direct-to-consumer. For specialized products like travel insurance that can be sold on the web, banks are particularly effective. Banks have also been very effective in affinity markets, having the advantage of familiar brand name to earn the trust of alumni and professionals.

Bank-based insurers are much more focused on Return on Equity (ROE) than other insurers because the bank often uses ROE to decide where to allocate capital. Banking regulations require higher ROE than insurance regulations, leading bank insurers to focus on managing expenses through direct distribution.

Laws prohibiting the sharing of information between banks and their insurers are a major limit on bank growth in the market. This means they cannot use their marketing infrastructure to boost sales. If this limitation were removed, we would expect to see considerable growth in the bank insurance market, perhaps at the expense of non-bank P&C insurers. Having said that, growth for banks is typically in the under-served market, focusing on people that do not have their own P&C broker.

Market Dynamics

The simple story is that good underwriting and cost management are the drivers of success in this industry. Both are easier said than done, especially in the current environment.

Echoing their global compatriots, Canadian non-life firms cite regulation, macro-economic trends, catastrophes, investment performance and talent as concerns. It is our sense from the interviews that talent is a bigger concern in Ontario than it is in global rankings (#8) of concerns for non-life insurers (source: CSFI, Insurance Banana Skins 2011, p.8).

Concerns don't lessen the increasing importance of technology for driving growth, taking cost out of the system, and getting consumers what they need. Technology needs are pervasive across the organizations (from marketing to compliance). Demographics may not be part of the insurer concerns, but they certainly play a role in market dynamics.

Regulation

Looking forward, **regulation is focusing increasingly on capital and solvency**, in response to the last banking crisis. Just as Basel III is affecting bank capital requirements, Solvency II is affecting insurers. While Solvency II is an EU directive, it has an impact here in two ways: first, many major P&C carriers are European and EU directives affect their business globally; second, OSFI has traditionally been at the forefront of strong solvency standards. There is some uncertainty about how Solvency II will be translated into requirements for non-life insurers, but what is certain is that compliance will take resources that divert from the management of the underlying business.

Solvency regulations have a direct impact on bank insurers too. Manufacture of insurance generally delivers an ROE of 10% according to one of our respondents, but banks have to achieve an ROE of 17% under their regulations. Also, as more insurance products are sold, additional reserves and regulatory capital is required. This effectively 'traps" the capital in the insurance company (in the bank) because it does not count as regulatory capital for the bank. With Basel III already increasing capital requirements for banks, it is becoming more difficult for banks to do more than distribute insurance.

Other solvency requirements that affect insurers include the need for reserves against specific risks. Earthquake risks are a major focus at the moment, while at the same time the industry is puzzled that there is no government-led programs (as in other G8 countries) for the bigger risks associated with floods or water damage.

Regulation also affects products, especially auto insurance. The biggest issues are fraud and pricing intervention. The level of fraud in Ontario has been massive, especially in bodily injury claims and, to a lesser extent, in the cost of repairs. Evidence suggests the fraud has been systemic and that organized crime is sometimes involved. Limits on P&C bodily injury claims introduced by the government in 2010, gave the industry its first year of positive growth (in 2011) since 2007. Yet despite these limitations, fraud continues to be an issue (ranging from accident benefits through to inflated repair costs). To combat fraud, the industry is investing heavily in IT to try and identify and reduce the fraud-related costs.

While the new legislation has reduced losses due to fraud, the mandated underwriting of substandard risks ("bad drivers" as most people would call them) and government intervention in auto rates threatens to erode those gains. There is a strong expectation that cuts in auto insurance rates may lead foreign auto insurers to exit the market, reducing employment. A small contingent of the industry expects that the industry will respond to rate cuts with innovative auto insurance products like 'pay as you drive', however, this is far from being certain. Other areas where regulation plays a role are investment and distribution. On the distribution side, the main impact of regulation is the limits on bank distribution and their inability to build on the bank's infrastructure or client base. There is little expectation that this will change.

Turning to investment regulation, we note several areas of regulation including: trading practices; allowable investments; use, reporting and accounting of derivatives; and corporate governance. The constant stream of new regulations creates uncertainty and drains management focus. At the same time, it has created a **significant demand for compliance officers** (of many types), where there are known gaps in the supply of talent.

Macro-Economic Trends, Investment, Catastrophes

In the current low interest environment, **generating a sufficient return on investment is quite difficult.** The resulting lack of investment income puts more focus on rates and losses. Economic conditions have not encouraged growth, and for many carriers the real growth has been in Alberta, especially in the Oil & Gas industry. But while growth has been tepid, Canada has not suffered as much in the recent recession as other countries and by G8 standards the economy is anything but stagnant. In fact, exports continue to be a strong point in the Canadian economy, leading to an increased focus on trade insurance and performance bonds.

Catastrophes are, by their nature unpredictable, but long-term risks can be assessed. There is a strong sense that weather-related catastrophes are on the rise, possibly due an increase in weather volatility associated with global warming. To quote Canadian Underwriter, "In 2012, Canada experienced an unprecedented fourth consecutive year of weather-related catastrophes at or exceeding the $1 billion mark" (source: Canadian Underwriter Statistical Issue, June 2013). Losses over the past four years have been more than double the average over the last ten. As we understand it, water-related damage is higher than at any time in history. Companies are responding by tightening their standards for underwriting water damage and raising rates.

While the industry is concerned with water losses, we understand that the government is more concerned with earthquake coverage in light of a number of earthquake-related disasters (including tsunamis triggered by undersea earthquakes) around the Pacific Rim in recent years. This impacts reserves.

Based on underwriting statistics, it is also impossible to ignore the impact of a major catastrophe. In addition to the $1 billion in weather-related catastrophes paid out in 2011, the industry paid out $1.7 billion for damage related to the Slave Lake wildfires (source: Canadian Underwriter Statistical Issue, June 2013).

In light of the many types of risks companies face (e.g., regulatory, economic, investment, catastrophe, compliance, technology, currency, reputation, market, etc.), **enterprise risk management (ERM) is a growing challenge in both insurance companies and in the corporate world.** The Chief Risk Officer (CRO) has emerged as a new corporate power role, as companies struggle to manage all of the risks their enterprises face.

Demographics

Older clients are creating product needs that have yet to be met. There are also a wider variety of "post-retirement" work arrangements than ever before. Downsizing, moving to retirement homes, and the snowbird lifestyle also need to be addressed.

Conversely, younger consumers create different demands. The younger consumer wants to interact more with technology. They need to be able to interact with technology and communicate with the company on a 24/7 basis. To get their attention and their business, companies need to invest in technology.

Technology

Technology is at the heart of success in the personal lines side of the business. For marketing, we see social media and web presence as increasingly important for bringing in new business on a cost-effective basis. Insurers are also increasingly building their own front-end systems to handle all direct customer interaction. Clients are expected to do more online themselves including using web tools to research the type and amount of coverage they need. They will also want to go online to look at the status of their claims.

On the claims side, technology is also being developed to detect fraud related to applicants, claims, injury clinics, auto repair shops and more. Linking up claims across companies and people is important, but privacy requirements add to the challenge. Predictive analytics is playing a big role, as are 'telematics' to analyze behaviour patterns. The days when automobiles contain processors that report on driver behaviour for underwriting purposes are not far off in practical terms.

Besides marketing and claims, internal administration/accounting, underwriting and service delivery all have a range of specialized technology needs. Meeting these needs is not always easy, because most firms are operating with legacy systems. The needs on the commercial side are less obvious, but we understand that enterprise risk management is at their core.

Growth Opportunities

Growth in the P&C market is largely tied to the economy, and as such, Alberta offers the best prospects for growth in the short-term. In personal lines, growth potential looks best for the High-Net-Worth (HNW) and affinity markets. Customer service skills will be particularly important for the HNW market. The mass market is a slow build and technology is the key to its growth.

For personal lines, growth will increasingly be tied to branding, as insurers forge direct links to consumers. Customer service will drive success beginning with buying and continuing through any claims process. The customer will require flexibility. Technology will play a strong role.

On the commercial side, opportunities for growth are best in the natural resources sectors, as well as cross-border coverage. Growth is more tightly tied to opportunities for profitability. Profitability is driven by good risk models, underwriting, and actuarial skills. Brokerage will continue to play a big role and that requires more people with good knowledge of competitor products, as well as interpersonal skills. P&C insurers will need people with service skills who are capable of credibly selling their value proposition to both brokers and clients.

When asked what it would take to foster growth, respondents point to the need for a stabilized regulatory environment with reduced political intervention. Having said that, the industry believes that government can help growth and reduce costs to people and businesses by taking away some of the "structural risk" in the business. Limits on payments for bodily injury effectively did this in the auto insurance business.

As P&C insurers see it, government could effectively provide guarantees of payment over-and-above capped industry payouts for "extreme catastrophes". This is already done in many countries in the G8. This approach would limit industry payout for catastrophes like earthquakes, tornados, floods and wildfires. Many believe the lower cost of this cover would then make it accessible to small and medium sized businesses. The reduction in reserves that insurers need to hold to cover these risks would also be freed up and available to foster growth.

Talent Gaps

In past years, the industry has dealt with talent gaps by "doing more with less" and by cross-training people. Those methods are not enough to overcome a shortage in actuaries, and as many note, it is hard for Ontario to compete with the salaries paid in Alberta.

Talent gaps include: underwriting, actuarial, risk management, compliance, marketing and technology areas of the business. The exact scope of these talent gaps cannot be ascertained through these interviews, but we can get a sense of relative need. Overall, it is likely that the highest skill jobs are hardest to fill, especially actuarial, risk management and compliance. Shortages are hard to estimate, in part, because some roles (e.g., social media marketers, enterprise risk managers) are just starting to play a major part in industry success.

Before we look at specific roles with talent shortages, we provide an overview of strategic trends and their implication for talent.

Strategic Trends and Talent

Personal lines are increasingly developing strategies by segment. Talent gaps are an issue. The mass market, for auto and home, is increasingly online and aiming to reduce labour costs, so talent needs focus on online/social media marketing and IT.

Affinity groups (e.g., alumni, professional associations, service organizations, etc.) are a growth area that has not been significantly penetrated. Affinity groups are desirable because they are characterized by higher retention rates and, due to the similarities among group members, are less costly to underwrite. Talent gaps are an obstacle to growth in affinity marketing, especially people who know how to build brands online and through direct marketing, as well as capable social media marketers. These individuals need to be experienced.

High-Net-Worth (HNW) is an under-served market for P&C in Canada. With over 300,000 millionaires, one respondent with considerable international experience estimates that 80% are under-insured compared to other markets like the US or EU. There is a push into this market by AIG, Chubb, GC&A and ACE. To meet the needs of this market, companies need people that understand personal products, because product is the main differentiation. For HNW, service and claims handling are an important part of the product. Talent gaps are an obstacle to growth in the HNW segment, because this segment needs experienced and high quality people for product development and marketing. Underwriting (UW) is a real issue in this specialized space. The UWs must know the markets and their price points. This is a market that takes real skill to capture.

For commercial lines, the main areas of growth are cross-border coverage, new product introductions, and coverage adapted to specific industry sectors (e.g., energy, natural resources, trade). Commercial lines demand technical knowledge to develop and price new products (e.g., cyber-liability, fiduciary liability, etc.), as well as marketing skills to foster uptake of these new products. Since underwriters are also active in sales in commercial lines, the technical underwriting skills must be supplemented with interpersonal and sales skills too. With much of the sales in the commercial market handled by brokers, some respondents suggest there is also a shortage of people with the customer relationship skills and product knowledge (of different carriers) to handle business growth.

Underwriting

Good underwriting and managing costs are the main drivers of success. Good underwriting takes a lot of experience and understanding of risks.

The general sentiment is that there are not enough new entrants into the business in general and that the industry has done little to convey the interesting roles that are available. Compensation is thought to be less attractive than other parts of financial services, compounding the problem. Having said that, most indicate that they can find people to fill junior roles in underwriting. Training for a junior underwriter can be done in-house in a matter of 3-6 months. Entry-level underwriting courses are available from the Insurance Institute of Canada (IIC), either directly or through some community colleges. Based on IIC course enrolments they provided, we estimate they provide training for roughly 100 new trainees and 28 junior underwriters each year (source: e-mail from Registrar and follow-up phone discussion, IIC, 1 May 2013).

The average age in the industry is also quite high, with many senior underwriters in the 55+ age group. If they are willing, it is quite common for companies to retain these underwriters past retirement age by offering incentives. New entrants often poach these senior underwriters to build their business, using large salary increases to attract these employees.

The general sentiment is that the next generation of senior underwriters (now age 35-54) is where there is a shortage of underwriting talent. Talent is being developed. IIC provides 'university level' training in underwriting, which is usually paid by employers. Training/mentoring is also done in-house. Nonetheless, based on IIC course enrolments, we estimate that IIC provides courses that help create five or fewer senior underwriters per year. (This may even be an overestimate, since the knowledge gained from IIC courses must be bolstered by relevant experience to be of value to the insurer.)

Against this background, several reasons are posited for the shortage of experienced people who can move into senior ranks. Those most commonly proposed are:

- Failure of P&C insurers to adequately invest in training because better-trained people are so often recruited away;
- Poor compensation compared to comparable jobs in other financial services sectors, especially with regards to increased compensation with greater experience;
- Transfer of top performers to bigger markets where their skills can generate more revenue, especially the US and UK; and
- Inadequate recruiting/retention in the 1980's and 1990's, especially during economic downturns.

The consensus is that so far the shortage of people hasn't hindered growth, but at the same time, the shortage of highly experienced underwriters in some areas (e.g., engineering underwriting) has negatively affected earnings through inadequate underwriting.

Actuaries

P&C actuarial training is very specific because it measures risk over much shorter time horizons than life insurance. Most P&C actuaries have written exams offered through the Casualty Actuarial Society, which specializes in topics related to P&C. About 10% of the members of the Canadian Institute of Actuaries are employed in the P&C practice area (source: http://www.actuaries.ca/about-us/actuaries/what/pc).

The Canadian Institute of Actuaries reports that they have 1008 members in Ontario and 630 in the GTA (source: e-mail from Public Affairs, Canadian Institute of Actuaries, 2 May 2013). By extrapolation, we conclude there are about 100 P&C industry actuaries (fellows) in Ontario and 63 in the GTA. Based on responses in our interviews, we would estimate there are about 250 actuaries at more junior levels in the P&C industry. There is no independent confirmation of these numbers at this point, although the TFSA-CoE Workforce Survey should provide useful point of comparison.

Respondents indicate that there has been a large increase in the demand for actuaries over the past ten years, without a corresponding increase in supply. Actuaries are typically hired while studying and they complete their program while working. Entry is said to be fairly steady. The past ten years have seen the emergence of stronger actuarial support systems for training, mentoring and ongoing coaching. Compensation is mainly viewed as a challenge in the under-35 age group. Responses suggest that retirements may pose a problem for senior level talent over the next 5-10 years.

Risk Management

As we stated earlier, enterprise risk management (ERM) and the Chief Risk Officer (CRO) role are recent developments. The workforce demand for these roles is expected to grow, especially within commercial lines. The CRO and enterprise risk managers are expected to identify risks early and mitigate them. They need to have considerable internal expertise, as well as knowledge of risk management. There will also be competition for CROs coming from outside the insurance industry, as large enterprises around the world seek to grapple with the complexities of risk in global commerce.

With an expectation of rising demand, we note that the Federal Department of Finance, Government of Ontario and financial sector leaders launched the Global Risk Institute in Financial Services in 2010 to "help build on Canada's growing reputation in financial risk management" (source: http://www.fin.gc.ca/n10/10-081-eng.asp). This should help fill some of the need.

Risk managers and CRO's will likely be drawn from the ranks of the Fellow Chartered Insurance Professional (FCIP) graduates. About half of FCIP graduates report going into risk management roles, and (training is typically paid for or reimbursed by their employer). Based on this rough statistic, we estimate that IIC prepares about 90 risk managers per year. We have no information on the preparation of risk managers for P&C from other sources, but we suspect that the IIC dominates this part of the financial service sector.

Compliance

Compliance is a growing issue and typically handled at the head office level. It often reports in to the CRO. With OSFI requiring more information in recent years, the amount of time and number of staff devoted to compliance has increased. Industry expectations for (future) regulation indicate that this trend will continue.

In our experience, compliance roles typically require a fairly sophisticated background in accounting or law, as well as industry knowledge. Actuarial training is also required for some areas of compliance in P&C companies. Given the highly skilled nature of these jobs, there cannot be a 'quick fix' for talent shortages in this area. We suspect that wage competition from other areas of financial services will prove to be a major hindrance to filling positions in the P&C industry, especially because compliance is a known area for talent shortages across the financial services sector.

Marketing

Traditional marketing with its focus on advertising and brand is not suited to the P&C industry. What the industry is looking for is real experience in direct-to-consumer marketing, as well as experience using social media for marketing. There is not a lot of experienced talent available. The extent of this demand is difficult to gauge.

Information and Communications Technology (ICT)

The extent of shortages in ICT is unknown. Nonetheless, there is a shortage of experienced people to apply social media and associated metrics to guide marketing, business capture, and client retention. Tied to online buying (in general) is the need for expertise in Customer Relationship Management (CRM) systems. Typically this requires expertise with relational databases.

In order to reduce costs, insurers aim to get their customers doing more of the work online. Good customer interface systems are needed to make this possible, and in the event of a claim, there must be systems that give the customer access to their claims information while protecting their privacy from others. Most insurers build their own front-end systems. There is a shortage of talent to do this, especially in light of the legacy systems so prevalent in the industry.

Finally, as we mentioned earlier, there is a tremendous need for fraud detection and reporting systems. These require both programming expertise and expertise in predictive analytics.

The industry has three major barriers to attracting ICT talent: legacy systems, industry image and compensation.

First, the P&C industry is mainly operating with legacy systems. This leads to significant system constraints that limit flexibility and make it difficult for developers to build creative solutions. New graduates want to work on the newer systems they have learned about in their training. When they do get involved in developing new systems, they are then faced with the frustrating challenge of getting their system to work in concert with the legacy system.

Second, the insurance industry must compete with companies like Google as an exciting place to be for talent. Innovative companies tend to attract the best of the new talent, and, despite some leading edge initiatives in the industry, the insurance does not project an attractive image to an ICT graduates.

Finally, there is little doubt that other areas of financial services can and do pay more for ICT talent (than insurance companies). This compounds the difficulty of finding people, especially experienced staff who can lead projects.

Analytics

In addition to predictive analytics for fraud detection, there is emerging growth in telematics. Telematics extracts information from information systems within an automobile to learn how well someone drives and then uses this information to set premiums for their auto insurance. This is one possible 'product design' response to limits on auto insurance premiums.

The speed of growth for both predictive analytics and telematics will depend upon analytical capabilities and the ability to attract ICT talent. Such analytical capabilities are in short supply and usually require training in statistics at the Master's or Doctoral level. Additionally, some knowledge of the industry is typically needed to ensure that recommendations based on analytics are both logical and legally defensible.

05

DOMESTIC LIFE & HEALTH MARKET

Domestic Life & Health Market

This chapter summarizes the structure, dynamics, growth opportunities and talent needs of the Ontario Life & Health insurance market, including the important related businesses of annuities and investment management.

Market Structure

The top 20 life and health companies in Canada are shown in Exhibit 4.1.[2] These 20 companies generate about $78.3B in total revenue – well over 90% of industry revenue. Some 14 of these 20 companies have Canadian head offices in Ontario, although we note that two of them (Canada Life and London Life) are subsidiaries of Great West Life, which also has a head office outside Ontario (shown in pink). Splitting the revenue on these two subsidiaries, the revenue generated by the top 20 companies with Ontario head offices is $48.5B – a bit more than 60% of all industry revenue.

A notable element of this list is the three reinsurers rank in the top 20 (Munich, RGA, Swiss). While these companies don't directly write insurance, they do reinsure risks written by other life & health insurers. Together these reinsurers account for about one-eighth of total revenue in the industry (with Munich Re accounting for the majority).

To quote TD Securities in its Action Notes (June 7, 2013 Equity Research, p.43), **"The Canadian life insurance industry is truly an oligopoly** with the Big 4 public companies (Manulife, Sun Life, Great-West, and Industrial Alliance) controlling over 50%, and in some cases over 85%, of the main life insurance market segments."

RANK	EXHIBIT 4.1 TOP 20 LIFE & HEALTH INSURERS, 2011	TOTAL REVENUE $,000
1	Sun Life Assur of Canada	13,616,723
2	Manufacturers Life	11,349,427
3	Munich Reinsurance Co	8,891,929
4	Canada Life	8,124,482
5	Great-West Life Assur	7,120,596
6	Desjardins Financial Sec	5,192,201
7	London Life Ins	4,940,034
8	Industrial Alliance Life	4,704,013
9	Standard Life Assurance	3,262,924
10	RBC Life Insurance	1,727,154
11	Empire Life Insurance	1,548,026
12	SSQ Life Insurance	1,287,667
13	RGA Life Reinsurance of Canada	1,157,679
14	Transamerica Life Canada	1,060,264
15	BMO Life Assurance	1,041,664
16	Swiss Reinsurance Company	861,408
17	Co-operators Life Ins	739,072
18	Indep Order of Foresters	723,545
19	Equitable Life of Canada	584,106
20	Capitale assureur	428,827

Source: Top Canadian Insurance Broker, Statistical Issue, May 2012, p.31

[2] This is based on the most recent publicly available information.

Delving further into the market structure, Top Canadian Insurance Broker provides additional comparisons of leading insurers, identifying top carriers for life premiums and top annuity writers. Within each of these two broad product lines, they distinguish individual lines and group lines of business. (Exhibit 4.2 shows the top companies for life insurance premium.)

Three carriers account for half of the life insurance premium generated for individual insurance: London Life, Manufacturers Life (MFC) and Sun Life (SLF). Given the reality that London, Canada and Great West Life (GWO) are all one company, it is reasonable to state that the top three carriers (substituting GWO for London Life) generate 63% of all individual life premiums.

EXHIBIT 4.2 LEADING LIFE PREMIUMS

RANK	TOP 10 INDIVIDUAL	NET LIFE PREMIUMS $,000	SHARE OF MARKET %
1	London Life	1,940,920	18.1
2	Manufacturers Life	1,882,981	17.6
3	Sun Life Assur of Canada	1,518,373	14.2
4	Canada Life	989,230	9.2
5	Industrial Alliance Life	848,392	7.9
6	Great-West Life Assur	460,633	4.3
7	RBC Life Insurance	457,596	4.3
8	Desjardins Financial Sec	385,612	3.6
9	Empire Life Insurance	321,074	3.0
10	Transamerica Life Canada	292,854	2.7
	TOP 10 GROUP		
1	Munich Reinsurance Co	1,284,334	35.9
2	Great-West Life Assur	492,394	13.8
3	Desjardins Financial Sec	487,894	13.6
4	Canada Life	234,169	6.5
5	Manufacturers Life	141,369	4.0
6	CUMIS Life Insurance	138,776	3.9
7	SSQ Life Insurance	115,406	3.2
8	Industrial Alliance Life	95,815	2.7
9	London Life Ins	91,079	2.5
10	Standard Life Assurance	71,292	2.0

Source: Top Canadian Insurance Broker, Statistical Issue, May 2012, p.30

Looking at Direct Life in Force (Exhibit 4.3) shows us the face value of policies written by each company, as well as the dividends those policies paid (in the case of individual lines). The total is a staggering $3 trillion of life insurance in force with $1.70 trillion on the individual side. This exhibit gives a better sense of market position, since reinsurers are excluded from the rankings since they don't have any Direct Life in Force.

As we can see, when Canada & London Life are grouped together, the top 3 carriers still write more than half of individual premium. The top 10 carriers account for 84% of the individual life market. In this exhibit, however, we see the top three carriers as more evenly matched for individual insurance in force.

On the group side, the three top carriers (combining Canada Life into GWO) account for three-quarters of the $1.46 trillion of group life in force. The top 10 carriers account for 93% of the group life insurance in force.

EXHIBIT 4.3 LEADING DIRECT IN FORCE

RANK	TOP 10 INDIVIDUAL	NET LIFE IN FORCE $,000	SHARE OF MARKET %
1	Manufacturers Life	376,467,367	18.61
2	Sun Life Assur of Canada	325,000,228	16.07
3	Canada Life	181,654,712	8.98
4	London Life Ins	176,173,546	8.71
5	Transamerica Life Canada	165,667,131	8.19
6	Industrial Alliance Life	151,275,563	7.48
7	RBC Life Insurance	93,709,558	4.63
8	Primerica Life of Canada	91,698,622	4.53
9	Empire Life Insurance	69,149,729	3.42
10	Desjardins Financial Sec	67,199,406	3.32
	TOP 10 GROUP		
1	Manufacturers Life	330,778,041	21.16
2	Sun Life Assur of Canada	313,587,596	20.06
3	Great-West Life Assur	273,699,614	17.51
4	Canada Life	259,441,851	16.6
5	Desjardins Financial Sec	142,200,062	9.1
6	Industrial Alliance Life	42,862,387	2.74
7	SSQ Life Insurance	42,001,787	2.69
8	Standard Life Assurance	30,085,125	1.92
9	CUMIS Life Insurance	24,661,523	1.58
10	Blue Cross Life of Canada	20,869,088	1.33

Source: Top Canadian Insurance Broker, Statistical Issue, May 2012, p.30

Annuity writers are another type of business in this segment. Exhibit 4.4 shows the leading annuity writers. Combining individual and group businesses, the top 10 carriers wrote $5.35B in net annuity premium in 2011.

On the individual side of the business, we see a very different market structure than for life insurance. GWO has no presence in the top 10, but even more striking is the presence of a bank-owned life insurer (BMO Life Insurance) in fourth place. It is quite clear that annuities are a very different business than life insurance.

The individual annuity business is less concentrated than the life insurance business in some ways, although MFC and SLF do account for one-third of the net annuity premium. BMO Life accounts for another 12%. The top 10 carriers account for 90% of the net individual annuity premium – about $2.27B.

In the group annuity business, the top 10 carriers account for 86% of the net annuity premiums – about $3.08B. More than one-third of this is reinsured. The three major publicly-traded insurance companies (including their subsidiaries) account for an additional 27% of net annuity premium.

Looking at both business lines, we can certainly see a few things about the top three carriers.

EXHIBIT 4.4 LEADING ANNUITY WRITERS

RANK	TOP 10 INDIVIDUAL	NET ANNUITY PREMIUMS $,000	SHARE OF MARKET %
1	Manufacturers Life	444,098	17.58
2	Sun Life Assur of Canada	376,596	14.91
3	BMO Life Assrance	320,959	12.71
4	Industrial Alliance Life	307,579	12.18
5	Canada Life	244,310	9.67
6	Capitale assureur	160,123	6.34
7	Empire Life Insurance	132,681	5.25
8	Desjardins Financial Sec	129,329	5.12
9	Standard Life Assurance	79,807	3.16
10	Equitable Life of Canada	70,332	2.78
	TOP 10 GROUP		
1	Munich Reinsurance Co	1,284,334	35.88
2	Great-West Life Assur	492,394	13.76
3	Desjardins Financial Sec	487,894	13.63
4	Canada Life	234,169	6.54
5	Manufacturers Life	141,369	3.95
6	CUMIS Life Insurance	138,776	3.88
7	SSQ Life Insurance	115,406	3.22
8	Industrial Alliance Life	95,815	2.68
9	London Life Ins	91,079	2.54
10	Standard Life Assurance	71,292	1.99

Source: Top Canadian Insurance Broker, Statistical Issue, May 2012, p.30

- SLF is strong in individual annuities but not a strong competitor for group annuities. In terms of direct life in force, it is quite balanced between individual and group lines;
- MFC is far stronger for individual lines than for group lines; and
- For GWO, London Life is strong in individual life, Great West Life is strong for group businesses, and Canada Life is quite evenly balanced.

Organizing Models for the Business

Life insurance companies offer such a wide range of services that it is difficult to cleanly group them, especially since they are often grouped differently at different companies. Based on business and analyst reports, however, Life **Insurance Business Lines can be organized as shown in Exhibit 4.5.**

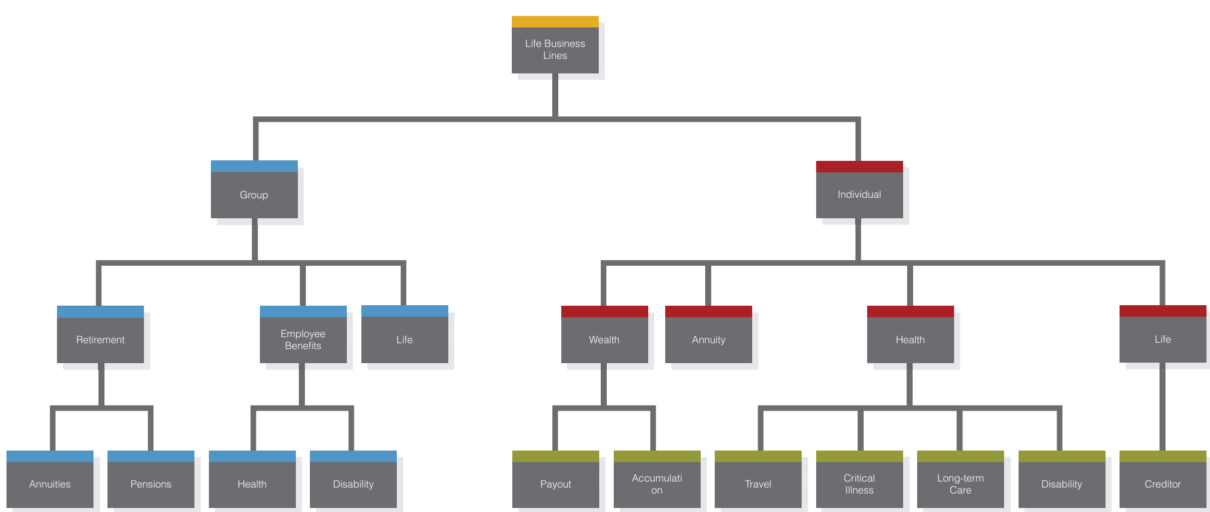
The fundamental distinction is between life insurers is based on the services provided to individuals and services provided to groups. Within Individual products, the fundamental four business lines are:

- Life insurance: this includes all types of individual life insurance (e.g., term, whole, universal, 'key man', etc.), as well as specialized products like creditor and mortgage life insurance. Living benefits and creditor insurance bridge the gap between life and health coverage.
- Health: includes a variety of product lines including individual disability, critical illness, long-term care policies, and the very specialized business of travel insurance.
- Annuities are mainly thought of as payouts to retirees, but accumulation annuities (e.g., RRSPs, RRIFs, RESPs, etc.) are also a substantial part of the business.
- Wealth includes a variety of investment products, both with and without guarantees, including segregated funds, mutual funds and GICs.

The group insurance business provides a range of services to groups of people, although in most companies, very small groups are treated as collections of individual policies. The major group lines are:

- Life insurance, usually simple term insurance for most employees with more specialized coverage for executives and partnerships;
- Employee Benefits involve a range of products including disability, supplemental medical, drug plans, wellness benefits and more; and
- Retirement services are typically geared to pension plans, or alternatively to accumulation annuities within a Group RRSP or similar vehicle. Between individual and group lines, money accumulating in RRSPs represents 34% of total annuity assets. (Source: Canadian Life & Health Insurance Association, Key Statistics, 2012) .

Exhibit 4.5 Life Insurer Business Lines



Segment Overview

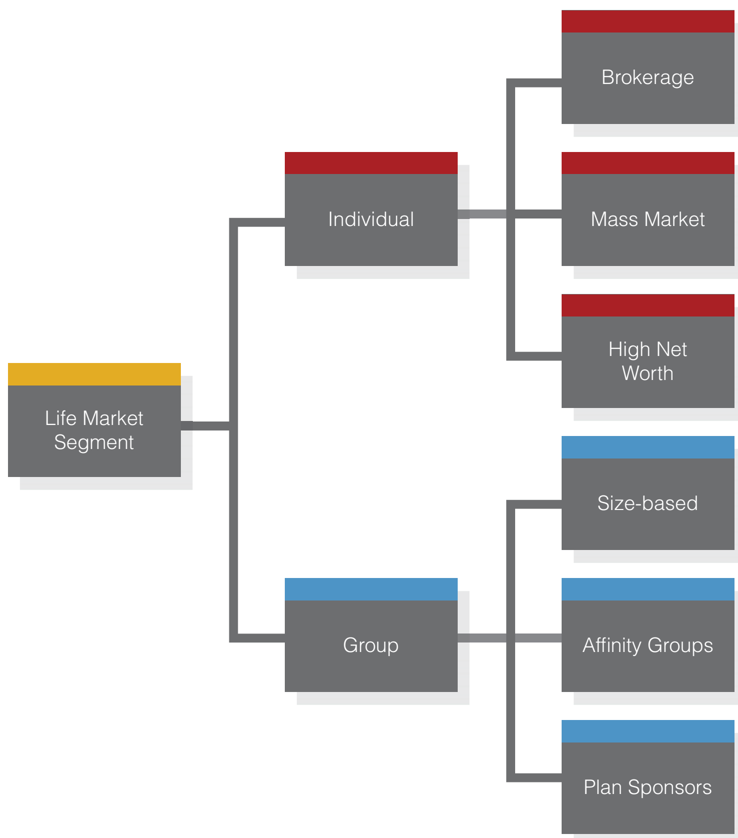
The market segments within the domestic life insurance market largely echo those in the P&C market with some minor variations; individual and group lines remain the major dividers. From there, the distinctions are often based on distribution channels (Exhibit 4.6).

Looking at the individual lines, we deem the 'brokerage' segment the most significant. This segment would include both agents and brokers, who act as intermediaries between life insurance companies and their clients. The brokerage channel includes a range of financial advisors with life insurance licenses, who also typically have a mutual fund license or a colleague with one. The brokerage segment sells a full range of insurance products, largely focused on the middle class and upper middle class. This includes individual annuities, both accumulation and payout.

While the middle class target of the brokerage might suggest it is a 'mass market' segment, the establishment of individual relationships between a financial advisor and a client distinguishes it from the usual mass market business. In our view, the mass market is one reached by direct mail, web-based sales, telemarketing and other techniques with a broad impersonal reach. The products sold in the mass market are typically simplified products that require minimal explanation, since advice is not given. This typically includes: term life; creditor life (decreasing term); travel insurance; critical illness insurance; and accidental death & dismemberment (AD&D). Banks often sell these products, although with the exception of creditor insurance, banks cannot build on their banking relationships to sell these products.

The HNW worth segment is characterized by specialized needs that require a more tailored type of advisor (e.g., PPI, Cap Advisors, etc.). Often these needs involve estate and trust planning, where insurance instruments are vital to the protection of inter-generational assets. Insurance instruments are also widely used for tax-efficient investing. The firms focusing on HNW also design specialized life insurance products for their clients, and with the size of life insurance policy they typically write, they have considerable clout. There are not many firms specializing in this business, but they control a considerable amount of assets. HNW advisors often work on a fee-for-service basis rather than working

Exhibit 4.6 Life Insurance Market Segments



for commission.

The group side business is segmented by the number of employees (at the customer). In some companies, small groups (even as many as 40-50 employees) may be treated as individual insurance clients. This is generally an intermediated market. Below 100 employees, brokers largely handle the group business. With 500 or more group members, benefits consultants usually handle the design and marketing of the group services. In the middle range, the likelihood of using a consultant increases with size. The fundamental product lines are life and employee benefits.

While affinity groups might seem no different than employer-sponsored groups, the fundamental difference is that affinity group members individually decide on their participation in the group and pay for the services themselves. They need marketing and persuasion at the individual level, which is usually done by targeted marketing and advertising to group members, typically by direct mail or direct e-mail. The most common affinity group includes customers of a premium credit card, and while they don't decide to buy the insurance benefits directly, those benefits are part of what they buy when they choose to buy and use a particular credit card. Many people are also familiar with affinity groups from alumni and professional associations, where the choice of participation is certainly individual.

We were uncertain about identifying Plan Sponsors as a separate segment, since essentially they are businesses. By plan sponsors, we mean pension plans and group retirement plans. There are two reasons for identifying this as a separate segment. First, pension plan and other retirement services are often bought independently of employee benefits. It is a separate decision with separate criteria and separate advisors. Second, large multi-employer pension funds often buy investment management services from insurance companies or their asset management subsidiaries, making this a distinct line of business. The sums of money involved can be quite large and the business is tightly contested.

Bank-based Life Insurers

In the life insurance markets, banks tend to sell product-by-product, while life insurers build relationships through agents and brokers. At least with regards to distribution, banks need "employees" while insurers need independent entrepreneurs with sales skills. Most commentators believe that banks are just waiting to be able to sell insurance through their branches, so that they can better build on their banking client relationships. Having said that, most commentators don't believe that day is "in sight" at the moment.

For products themselves, insurers typically build the products from the ground up doing the design, underwriting, and everything else. Banks often sell products manufactured by others. Sometimes insurers say bank products are too simple, but it is this simplicity that enables banks to provide insurance protection to markets that have been under-served. Packaging and pricing a standardized product can make buying easier and more cost-effective. Particularly in the younger age groups, not everyone wants personalized service and the anticipated pressure for buying it is thought to entail.

In 2011, only two bank-based insurers were in the top 20 for Life & Health, namely RBC Life Insurance and BMO Life Insurance. They were #9 and #12 in premium revenue. For Accident & Sickness Insurance, RBC Insurance was #1 in direct premiums written.

Canadian Insurance Top Broker (Statistical Issue, May 2012) provides

information on three significant bank-based life insurers (we were unable to find comparable information on the other two major banks).

- BMO Life Assurance and BMO Life Insurance combined saw a 4% decline in total revenue between 2009 and 2011 with combined total revenue dropping from $1.154B to $1.109B. ROE in 2011 was 9.66%, down from previous years and below the bank hurdle rate of 17%.
- RBC Insurance had a 9% decline in revenue from 2009 to 2011 with total revenue declining from $1.927B to $1.727B. Declines were completely due to a fall in investment income, as premium revenue increased by 2% over the same period. ROE in 2011 was 2.70%, which is well below the typical bank hurdle rate of 17%.
- Scotia Life Insurance is a much smaller provider, but earned a higher ROE of 22.09% in 2011. Total revenue increased from $0.038B to $0.048B between 2009 and 2011 for an increase of 27%. With revenue equal to less than 3% of RBC's total revenue, it is clear that Scotia Life has different aspirations for its business. As we understand it, they are selectively investing in opportunities that meet the bank hurdle rate, especially creditor insurance.

As for expansion outside of Canada, we note that Scotia Insurance already offers creditor and other selected types of insurance in markets where it owns a retail bank. In these markets it typically distributes the product and pays claims. It leaves the creation of the product to a local insurer and focuses on its distribution capabilities.

Generally speaking, banks are reluctant to pursue opportunities outside of Canada for two reasons. First, they believe they have ample opportunity for growth in Canada. Second, with the exception of TD in the US and Scotiabank in a number of countries, Canadian banks have not developed the foreign market knowledge needed to succeed internationally.

Market Dynamics

The economy is seen as the major driver of the market over the past five years. The bank financial crisis has led to tougher capital requirements for insurers, but more importantly, the low interest rate environment (and sometimes low equity returns) have reduced investment performance and put downward pressure on profitability. The economic environment has made life insurers more risk averse.

While there are challenges on the revenue side of the business, companies have become more focused on cost reduction. Faced with slow growth, companies have turned to improving their cost-efficiency and productivity. They have invested in people and systems to achieve this. Some of the main gains are:

- Consolidation for economies of scale and strength including consolidation of companies, product lines and distribution;
- Increased use of technology in group markets, both mobile and web, to better communicate with employees and with consultants and to reduce paper-based communication;
- Creation of innovative products; and
- Geographical expansion to find areas with better growth potential.

Looking out five years, most commentators believe that interest rates will remain relatively low but that equity markets will improve, thereby allowing life insurers to build profitability through improved investment income. There is a sense that Lifecos have their risk management problems under control and can move forward.

Insurers will strive to achieve profitability by becoming more efficient and by looking for non-traditional opportunities. There is a sense that the next five years will see some new products and more aggressive growth efforts, especially from smaller companies.

Lifecos also realize that there are business lines where they can expand, even in a mature market like Canada. Some of these business lines aim to build personal relationships with group clients, giving insurers an opportunity to retain their assets at retirement while selling them optional products they need during and after their working years. With growth in the SME market, there may also be opportunities for group insurance sales to smaller companies.

Without a doubt, there will be more focus on retirement markets. Payout annuities and RRIFs are the two methods for 'decumulation' in use now and growing, but each has drawbacks that offer an opportunity for innovation. In addition, younger generations (e.g. Millennial) just entering the accumulation stage of their lives may have different priorities that offer innovation opportunities on the accumulation side too.

Bank-based insurers will also aim to expand their footprint, relying on technology and direct-to-consumer marketing to accomplish this, even if they can't capitalize on their branch network. Several commentators noted that younger consumers are under-insured, and, as we observed, this is a group that can be reached more readily by deployment of technology.

Regulation

As one commentator asked, "Is there another industry as regulated as Financial Services?" There are different regulations to govern the companies handling of investments and reporting for its own account: for its insurance products, its investment products, for pensions and more. Compliance is time-consuming and costly for the industry, but accepted as part of doing business.

At the corporate level, the comments on regulation largely echo those in section 3.2 of this report, particularly with regards to the regulatory push on increasing capital and reserves in response to Solvency II. This affects pricing, as well as how aggressively a company can expand. Tightened regulations on projecting investment returns and covering long-term risk make insurance products less competitive than asset accumulation products. That skews the marketing effort and profitability.

In addition to solvency requirements, there is a considerable regulatory burden attached to being a publicly traded company. The burden is particularly large for the two large insurers (i.e., MFC and SLF) listed on both the NYSE and the TSX.

At the business line level, **the major impact of regulation is the need for regulatory compliance for business lines** like pensions and investment, where a company has to deal with different rules in each province (and country). Regulators in Canada are diverse: at the company level, there is OSFI (Office of the Superintendent of Financial Services); at the level of insurance products, pensions and distribution, they must deal with FSCO (Financial Services Commission of Ontario) and other provincial members of the Canadian Council of Insurance Regulators (CCIR) and some provincial pension regulators; for investment-related activities including distribution, it is also important to consider the requirements of the OSC (Ontario Securities Commission) and other provincial CSA (Canadian Securities Administrators) members. We suspect that the MFDA (Mutual Fund Dealers Association) also imposes its own regulatory requirements. **There are an enormous number of areas of compliance, but no standardized set of reporting requirements.** Compliance efforts consume considerable labour and there is a shortage of people to work in this area.

For the most part, commentators suggest that individual business lines are more affected by regulatory burden than group lines. For large group plans with employees spanning provincial and national boundaries, however, we understand that even group business lines can lead to complex reporting.

According to a recent Swiss Re report (Canadian Life & Health: A stable industry navigates the financial storm, November 2010), new International Financial Reporting Standards (IFRS) will change the boundaries that define an insurance contract. They would also sever the link between insurance liabilities and the investments held to support these liabilities. These changes, if instituted in unaltered form, will make popular products like annuities more expensive and less competitive, as well as requiring insurers to increase their capital. The industry is discussing alternative approaches similar to those instituted in the US and UK, as a means of mitigating the potential impact.

According to a recent TD Securities report, the discussions have been fruitful. In December 2012, "**OSFI announced revisions to Lifeco capital rules that should have a modest positive impact.**" (Source: TD Securities, New Capital Framework: A Closer Look, January 23, 2013). OSFI has also removed some uncertainty about regulation by releasing its timeline for capital rule revisions to 2016. TD also suggests that when all of the new capital rules are adopted in January 2017, Canadian life insurers will be "comfortably capitalized" to meet the requirements.

Nonetheless, it is clear that **deleveraging of investments is an inescapable consequence of new regulation. This means that profitability will likely be dampened for the foreseeable future** (Source: Swiss Re, Canadian Life & Health: A stable industry navigates the financial storm, November 2010).

Macro-Economic Trends and Investment

Having discussed these issues in the two preceding chapters, there is a danger of excessive repetition. We will keep comments brief.

The financial crisis, economic stagnation, low interest rates and returns on equities (coupled with deleveraging) have slowed business growth. Regionally, Western Canada is seeing growth, while the rest of the country is flat-to-down.

In a recent global review of the industry (Source: SwissRe, Global insurance review 2012 and outlook 2013/14, December 2012), the key observation was "The global economy is currently fairly weak… Monetary stimulus will remain accommodative in the major economies well into 2015, providing the stimulus necessary to sustain growth, but with low interest rates reducing insurers' investment returns." The same report predicted the equity rally we are seeing this year and continuing low bond yields into 2014.

While Canada suffered from some of the global macro-economic trends, it was less impacted by the financial crisis than other markets. With an upswing in the global economy, Canadian insurers are generally seen as well positioned to capitalize on opportunities both at home and abroad (Source: Swiss Re, Canadian Life & Health: A stable industry navigates the financial storm, November 2010).

Demographics

The aging of the population has an impact on clients and on staffing. The Mature Market (Age 50-64) continues to be the major buyer of investment products, increasingly joined by those in their 40's saving for retirement. It is unclear whether the current under-50's will be able to pick up the "slack" on investments when the current Mature Market reaches retirement. Looking at the growing ranks of retirees, there is a greater need for decumulation products and investments that generate a steady income than before. Furthermore, with many people (especially professionals) now working past age 65, group benefits are just beginning to tackle what to do with benefits for full-time workers age 65 or older.

In the workplace, we see a wide range of transitional arrangements to keep people working full or part-time at retirement, in order to offset the loss of experienced people in the workforce. There is a real challenge in balancing retirement transitions and new entrants, especially in the increasingly 7/24 financial services environment.

Moving to the other end of the scale, Generation Y (also called "Millennials" or "Gen Y", born c.1978-2000) began slowly but it is now starting to make more financial decisions. They are looking for wellness promotion and preventive benefits rather than the traditional illness remediation benefits. This affects the kinds of employee benefits they want and what it will take to retain them in competitive environments.

Compared to preceding generations, Gen Y are also more prone to buying insurance and other financial products online with advice coming from blogs, online forums, friends and multiple financial institution websites (Source: Investor Education Fund, Learning and Key Events: Age 20-34, September 2009). They pose a significant challenge for the traditional financial advisor. They are skeptics who place far less trust in the views of financial advisors than preceding generations.

On the employment side, Gen Y looks for a different workplace environment: rotational work experience, working from home, and flexible hours. Their expectations are very high. To retain good talent, insurers need to meet those expectations with leadership training and management positions. Regardless, Gen Y are far more prone to move because of other opportunities or because of 'banging up against the walls of the employment pyramid'.

Technology

In an era where risk management is increasingly important and regulation is increasingly strict, the big technology challenge is to measure and value assets and risk for a multitude of products spread across regions that are independent of one another for regulatory purposes. This must be done at the company and the jurisdictional levels. The systems must also be capable of stress testing under a range of scenarios to meet regulator concerns.

For sales and retention, technology is pushing things down to the individual level – marketing, administration, monitoring and more. Technology gives insurers more 'touch points' with clients, which in turn provides more opportunity for cross-selling and upselling. At the level of the individual sales agent/broker, the challenge is effective online communication and provision of marketing materials. Technology support for compliance purposes is also on the rise.

Group benefits remain a technology-intensive business. There are high volumes of information with high levels of accuracy needed in managing it. Employees often have flexibility to choose alternative benefits, and regardless, they want to know the status of their claims. This is now dealt with online. Everything from issuing certificates to plan personalization to paying claims or telling the client about their status can now be handled online (or will soon be).

Overall though, technology for administration is old news. The real front line of technology is using the Internet and social media for direct-to-consumer marketing, sales and service. As we understand it, online sales of insurance and investment products are growing in popularity, especially with Gen Y buyers. Banks have necessarily pursued this direction, but life insurers are now looking at this alternative distribution channel too.

As recently reported in Investment Executive, "Toronto-based Manulife Financial Corp. has seen a growing number of clients go online to purchase its brand of Cover Me insurance policies, which are specifically designed to be easy to buy online. Online sales now represent 30%-40% of all of Manulife's direct-to-consumer sales, according to Bob Doyle, director of direct-to-consumer marketing for affinity markets at Manulife, up from just 8%-10% about four years ago. The remaining 60%-70% of Manulife's direct sales are conducted via telephone." (Source: Investment Executive, "Click", June 2013).

And as we understand it, both insurance companies and banks are struggling to grasp how social media can help their marketing. These are early days in social media marketing, but there is little doubt this will be a major strategic direction in the next 5 years.

Growth

Commentators are split on growth opportunities, but generally see steady growth in their business over the next 5-10 years. This is a mature market, so there is no expectation of 'shooting stars'. There is general agreement that **investment-related business lines will experience growth,** both individual wealth management and group retirement services. The baby boom bulge will keep investment and annuity business buoyant for the next 5-10 years. Equity research analysts echo these sentiments and as we pointed out in chapter 2.

In Group business lines, there is a move to 'designer benefits' tailored to each individual plan member. Wellness programs, including those that are largely self-help, are also expected to grow.

Equity research analysts (Source: TD Securities Action Notes, June 7, 2013) point to other opportunities mentioned by only a few commentators:

- Income replacement protection and life coverage for younger Canadians, which many believe are massively under-insured;
- Tied to the under-coverage is a need for more products to serve the self-employed market cost effectively; and
- For those running small businesses, there is a need to "catch-up" with the benefits that larger competitors offer in order to retain staff.

Across business lines, there is a general sentiment that **product innovation is critical for success**. Well-designed products are both saleable and profitable. It takes real expertise to build them.

Besides growth in client-facing businesses, insurance companies will see employment growth in areas like risk management, compliance and financial modeling, both at the technical and managerial level.

Growth in Canada is expected to be less than one-fifth of growth in international markets, which suggests that **capable insurers will be expanding internationally**. MFC and SLF are the most likely candidates for expansion outside the G8 markets.

There is no simple formula for success that comes out of our look at market dynamics and growth. What comes through is a sense that it takes a broad range of capabilities to make an insurer successful. Product innovation, good underwriting, effective marketing and sales, solid investment management, efficient administration systems, good client service and great claims handling are all needed skills for success. Wrap this in professional risk management and add capital and leadership skills to complete the comprehensive picture. It is a business that requires knowledge and skill to navigate, and some of this can only be acquired through work experience. The supply of talent is not equal to the demand.

Talent Gaps

In terms of staffing, **projections of 5-6% hiring per year seem to be consistent with expected growth rates.** For many high skill positions, the rate of exit from retirement is equal to or greater than the hiring rate. The cohort to fill these positions is still getting the experience they need.

There are a few general themes that cut across the talent shortages in all areas:

- **Technical skills alone are not enough.** Soft skills including communications, interpersonal skills, collaborative leadership skills and business acumen are needed for advancement in any technical field;
- Financial services are viewed as desirable. Within financial services, **insurance is viewed as the kid who isn't "cool".**
- **The Gen Y desire for work variety is at odds with the industry desire to build specialized experience;**
- **Insurers have not fully adapted to the lifestyle desires of Gen Y** including: flex hours, work from home, and job mobility; and
- **Retention is more of an issue than hiring.** "Churn" is a big factor with new hires for all four of the reasons just mentioned.

The three biggest talent gaps are: Actuarial, Sales, and ICT. To a lesser extent, there are shortages in Marketing, Risk management and Claims adjudication. Underwriting and Analytics were shortages in P&C, but neither was mentioned often as a concern in the Life & Health business.

Actuarial

The demand for actuaries is industry-wide. With a great number of retirements among senior actuaries over the next 5-10 years, the shortage is expected to get worse.

There are lots of new grads coming out of university programs, but it is a long process to bring them up to speed. As well, Actuarial Sciences draw serious math students. These students often lack the soft skills necessary for advancement, including clear written and oral communications, as well as managerial skills. Drive and ambition are also critical for advancement, but many enter the industry thinking that technical skills are enough. In areas like Group benefits and pensions, where the actuary often has contact with clients and brokers, soft skills are especially a necessity.

There is a high churn rate for new entrants, for all the reasons mentioned in the introduction to talent gaps. The consensus is that the insurance industry needs to sell itself as a good place to work and not just a place to "drop-in" to an available job. Part of this "sell" must be on-the-job. More pay, more work variety, and job rotation are part of what insurers need to offer.

While not mentioned in the interviews, as an Industrial Psychologist it is also clear that the industry needs to provide a realistic job preview guided by people who love the work. The skills truly required are far broader than most candidates know. Along with this, Actuarial Science programs should begin incorporating business skills into their programs more formally. Taking a lead from Ryerson University, which provides a business communications course to engineering students and others, we suggest it is time for the university-based Actuarial programs to recognize communications as a necessary job skill.

The Canadian Institute of Actuaries reports that they have 1,008 members in Ontario and 630 in the GTA (source: e-mail from Public Affairs, Canadian Institute of Actuaries, 2 May 2013). Overall, 31% of Actuaries work in life insurance directly. By simple extrapolation, we would conclude there are about 310 Life industry actuaries (fellows) in Ontario and about 200 in the GTA. Based on responses in our interviews, we would estimate there are about 150 actuarial students at work in the GTA. There is no independent confirmation of these numbers at this point, although the TFSA-CoE Workforce Survey should provide useful information.

When looking at the market for actuaries, it is worth bearing in mind that 44% of actuaries end up in consulting firms, 5% in reinsurance and another roughly 2% in risk management. Taking this into account, one must halve the talent supply being produced by the universities to get a good reading of the talent supply available to life insurers. (Source: Canadian Institute of Actuaries, Annual Report 2011-12).

Sales & Marketing

As one commentator said of sales positions, "There is an unlimited need". Sales is more than financial advisor work with individuals, but also includes group benefit sales and relationship management with clients, brokers, and even call centres. This demand will only grow.

At the top of the list of talent gaps is the need for "financial advisors", especially in the area of wealth management. The financial advisors as a group are relatively old, and retirees are selling off their book of clients, rather than bringing in new talent. The result is consolidation in the industry. It is difficult for a new entrant to get established. Insurers hope that these sales positions will be filled by MGAs (i.e., Managing General Agents – "Brokers" in everyday language), if the MGAs can attract and retain people. The massive need for sales capabilities even has a few firms talking about reviving their agency system, which had financial advisors working as commission-based employees for the life insurer.

Salespeople are needed for group benefits and group retirement products too. Group reps are employees getting a salary, so the "personal risk level" of a group rep job is considerably less than for a financial advisor. As we understand it, it is not hard to get applicants for a group rep position. The difficulty is in vetting the candidates. Finding suitable candidates who can acquire the necessary knowledge and skills is a challenge, and equally challenging is retaining them after they have the knowledge and some work experience. Because of this, many firms hire internally from among staff with some job tenure.

In terms of Marketing, group benefits are mentioned mainly because of retention difficulties. **The area of marketing where there is a real talent gap, however, is social media marketing and direct-to-consumer.** These are both high growth. There are few people with the training that insurers are looking for and even fewer who have enough experience to be credible. This looks like an issue that requires both curriculum change and more co-op work or paid internships.

ICT (Information & Communications Technology)

The retirement of experienced staff is more of a threat to business continuity in ICT than in any other area. Many large companies are operating with legacy systems and it is only the older IT people who know about programming and development on those systems. Full-time, part-time and contract jobs (whatever they will take) are being offered to try to keep these skills available to the company. While there are plenty of new IT grads, they don't know legacy systems. As one commentator remarked, "No one goes to school in IT to learn about old stuff."

But even for the "new stuff", there are real shortages of talent. People are often applying who know 80% of what is needed, but the last 20% is quite costly for companies as new entrants learn it on-the-job.

The biggest deficit among applicants, as we understand it, is the programming and development skills needed for administration and distribution systems in insurance. Part of this deficit is that the developer needs some knowledge of these functions to be truly effective. We find that there is again a need for more than ICT technical knowledge. There is a need to understand financial information, product support and marketing. We would also suggest that there is a need for some creativity at the user-interface, since the systems that insurers need are aimed at facilitating distribution and not just keeping records.

The link between ICT and marketing also comes up in another area. While ICT people know about social media and social networking as users, there is no sense of how to use it for business purposes, especially marketing and client retention. The same issue was mentioned as a gap in ICT for P&C insurance too.

In addition to all this, we come back to the original points we made about talent gaps. New entrants want to move up in the company. There is no training on communications, management or finance to help them advance in their company. **The need for cross-disciplinary training is one that should be remedied for ICT, as well as the other technical jobs.**

Risk Management & Compliance

In areas like compliance and risk management, there is a real demand for people in mid-career. Here the challenge is both convincing people to join the industry and then paying them enough to retain them. Large accounting and law firms are likely to hire them away at higher pay once they get the experience they need to be valuable. Commentators suggest that risk managers are not sufficiently valued by the industry. As a result, they are easily poached by banks and other industries that value their insurance experience as well as their underlying expertise.

Claims Adjudication

"No one grows up and dreams of being a claims adjudicator" says one of the commentators. The job is unknown to most and lacks the "cool" factor to draw new grads. Yet there is a real demand for claims adjudication in the life insurance industry. The demand is particularly acute for 'disability claims adjudicators'. This is a high skill job needing considerable training and on-the-job experience. The pool of talent for the job is largely unknown.

06

SUMMARY AND RECOMMENDATIONS

Summary and Recommendations

Summary

The study posed two fundamental questions. In this section, we will briefly address each question.

What business reasons will drive changes in staffing in the regional insurance industry over the next 3-5 years?

Growth opportunities will drive staffing changes. Growth opportunities themselves are driven by regulation, availability of capital, the economic environment and demographics.

For P&C insurance, the main opportunities for personal lines are:

- Direct-to-consumer sales, especially online and social media;
- Affinity marketing; and
- Specialized products for High-Net-Worth clients.

For P&C Commercial lines, the main growth opportunities are:

- Industry sectors with high growth (e.g., natural resources);
- Cross-border coverage; and potentially; and
- Increased sales to Small-Medium enterprises.

For life insurers, there is general agreement that investment-related business lines will experience growth, both individual wealth management and group retirement services. The baby boom bulge will keep investment and annuity business buoyant for the next 5-10 years.

In Group business lines, in addition to group retirement products, there is a move to 'designer benefits' tailored to each individual plan member. Wellness programs, including those that are largely self-help, are also expected to grow. Other potential opportunities are:

- Income replacement protection and life coverage for younger Canadians;
- More products to serve the self-employed market cost effectively; and
- For those running small businesses, "catch-up" benefits that will help retain staff.

For Canadian P&C insurers, international expansion is not really feasible. They lack the capital and the knowledge to expand internationally regardless of growth opportunities.

For life insurers, growth in Canada is expected to be less than one-fifth of growth in international markets. Capable insurers will be expanding internationally. The availability of capital and talent to help buy, build and maintain international supply lines will play a critical role. Top-notch talent with international experience will be at the forefront.

What can be done to enhance the competitiveness of the insurance industry in Ontario over the next decade, both in terms of revenue and employment?

There are a few general themes that cut across the talent shortages in all areas. Understanding these themes is key to solution:

- Technical skills alone are not enough. Soft skills including communications, interpersonal skills, collaborative leadership skills and business acumen are needed for advancement in any technical field;
- Financial services are viewed as desirable. Within financial services, insurance is viewed as boring;
- The Gen Y desire for work variety is at odds with the industry desire to build specialized experience;
- Insurers have not fully adapted to the lifestyle desires of Gen Y including: flex hours, work from home, and job mobility;
- Retention is more of an issue than hiring. The talent shortage is often for people with 5 or more years of experience, rather than new hires; and
- Companies invest money to help people get the experience they need, then those people are hired away by competitors.

Sometimes competitors are new entrants, and sometimes, they are competitors from other markets (e.g., US, UK) hiring Canadians away. For some types of talent (e.g., actuarial and sales), the competitor may well be an insurance brokerage.

Recommendations

Education & Training

1. For entry-level quantitative or technical jobs, like actuarial and ICT, it is critical that students learn soft skills. Business communications, including both writing and presentations, should be part of the curriculum and more. These skills are critical to advancement and reducing churn;
2. More co-op and/or internship programs are needed to help new entrants get experience;
3. Foster more cross-disciplinary training, combining both courses and work/co-op experience. An example might be introductory finance for ICT or Actuarial students;
4. Incorporate credentialing programs offered by Financial Industry Training organizations into course credits for recognized post-secondary institutions;
5. Develop bridging programs for career shifters, perhaps in partnership with some professional associations or employers; and
6. Increase financial support or tax relief for co-op or on-the-job training programs that lead to employment in the FS industry.

Actuarial Roles

Looking specifically at Actuarial jobs, we would add:

- Educate and train more actuaries; and
- Develop actuarial specialties in enterprise risk management and compliance and focus some of the incremental enrolment on these specialties.

In terms of Marketing, the area where there is a real talent gap is social media marketing and direct-to-consumer marketing. These are both high growth fields. There are few people with the training that insurers are looking for and even fewer who have enough experience to be credible. This looks like an issue that requires both curriculum change and more co-op work or paid internships.

ICT also has a few areas where talent deficits are known, especially administrative systems and technology to support marketing and customer retention. These issues speak to specialty training, but without a clear indication of the availability of jobs, it may be difficult to support these specialties. Once again, this looks like an issue requiring both curriculum change and more co-op work.

Perhaps the most difficult area for dealing with talent gaps is the need to program and develop legacy systems. With enough desperation, perhaps monetary incentives can be introduced. Thinking about a model often used in the past, an insurer could pay for the education of an ICT student who is willing to train and work in legacy systems as part of their training. A five-year contract at fair market rates that obligates the student to repayment of tuition (at a rate of 20% forgiveness per year) if they leave early might prove effective. We recognize that the kind of 'indentured worker' component of this would require some real thinking, but on the positive side, it provides a student with both tuition and a job. We believe there are enough people who want this security to make it attractive to students. We have less faith in its attractiveness to industry, but that depends on the seriousness of the talent gap. For industry, the upside is that they get someone to fill a difficult role for a nearly guaranteed 5-year period.

Compensation & Work Conditions

1. Encourage employers to adapt working conditions to meet Gen Y needs such as work rotation, work from home and flex hours;
2. Support Industry-wide compensation studies. They would let insurers know what other types of firms (e.g., consultants, brokers) in their industry are paying to hire and retain people. Comparisons with comparably skilled people in other FI would help insurers in positioning too. It would also help develop realistic expectations for students; and
3. The industry needs a better sense of why people actually leave the company that trained them. Independently study why people move to a new company, especially in another industry. This could help the industry develop strategies for retention.

Promotion

1. Encourage industry associations to get some of their more exciting speakers to talk to students about the latest topics in order to build excitement about the industry (e.g., detecting fraud, protecting/underwriting FI against hackers, using social media to crowd-fund, etc.);
2. The insurance industry needs to do more marketing within preparatory programs. Students need both a realistic job preview and a sense of why this career can be exciting. A group of five people aged 22-26 talking about what they like would be more effective than an individual for Gen Y. Also important is a person saying what they don't like, and how they deal with it;
3. Help HR departments think more about Human Capital and less about filling jobs. Provide HR departments with better information about how people in other business sectors can be re-deployed readily into financial services;
4. Provide incentives to get skilled Canadians to return home;
5. Attract qualified foreign professionals with a "transition to Canada" program done in cooperation with specific employers; and
6. Adapt the TFSA Workforce Survey to get more precise numerical information on shortages by commissioning periodic special surveys.

Closing

We are certain there are other possibilities for stimulating growth that the industry might offer, but these are outside the scope of our work. For those who are interested, we would suggest taking a closer look at remedies to issues like: regulatory harmonization; catastrophe funds; stemming fraudulent disability claims; providing better overseas support to Canadian insurers, etc.

In accord with our mandate, we have focused the remedies in this report on fostering growth by improving the availability of necessary talent. This is a practical and useful starting point for further strengthening the insurance industry in Ontario.

07

APPENDIX 1: PROJECT SCOPE

Appendix 1: Project Scope

Note: Scope of the project is documented in the proposal below, as accepted by the TFSA-CoE.

Work Proposal: Opportunities in Insurance

The study provides an overview of the insurance industry with a focus on two key areas and their implications:

- Key business trends, both international and domestic; and
- Talent attraction and mobility.

Based on our discussions, there are two primary questions that the study needs to address:

- What business reasons will drive changes in staffing in the regional insurance industry over the next 3-5 years?
- What can be done to enhance the competitiveness of the life insurance industry based in Ontario over the next decade, both in terms of revenue and employment?

When focusing on staffing, the study will consider both the life insurance and property-casualty insurance markets. The two markets differ dramatically. When focusing on competitiveness, we will focus primarily on the life insurance industry. Having said that, it should be understood that the life insurance industry is made up of several different business lines with differing prospects.

To address both competitiveness and staffing in life insurance, we will have to consider opportunities and issues by business line, focusing on the following:

- Individual product lines including life insurance and annuities (deferred and payout);
- Group benefits including retirement plans; and
- Related asset management (including segregated funds).

Answering the two primary questions, we need to also address some related issues.

- What is the structure and dynamics of the international life insurance industry?
- Where do Canadian life insurance companies fit in?
- Why have Canadian "independent life insurers" fared better than bank-based life insurers internationally?
- What are the success factors that drive growth in the industry, domestically and internationally, especially with regards to workforce skills?
- What are the medium-term prospects for Canadian insurers post-2008?

Our intention is to produce a report that focuses on the two primary issues providing conclusions and recommendations supported by evidence. The supporting evidence will come from personal interviews, a review of relevant literature, and an analysis of pertinent databases.

Project Steps

The project steps we anticipate are as follows. Many of these steps will take place simultaneously.

1. Meet with TFSA to review the objectives and methods.
2. Review TFSA briefing material including the Pilot Survey and other supporting evidence.
3. Conduct an independent literature review with a focus on the structure and dynamics of the life insurance industry and success factors.
4. Develop a draft interview guide for use with key informants in insurance companies. We assume that interviews in the P&C industry will be shorter, since they will solely deal with drivers of staffing and their impact.
5. After review by TFSA, finalize the interview guide.
6. Arrange interviews with 24-30 key informants, in-person if available, or alternatively by phone. The bulk of the interviews will be focused on life insurance companies. We understand that TFSA will assist us in contacting potential respondents and asking for their cooperation.
7. Find additional evidence to confirm or disconfirm assertions made during interviews where possible.
8. Prepare a final report with Conclusions & Recommendations, as well as supporting evidence.

08

APPENDIX 2: INTERVIEW GUIDES

Appendix 2: Interview Guides

Interview Guide – Domestic Life Insurance

1. **Structure**

   1.1. Which major players in the Life Insurance market are expanding most aggressively?

   1.2. Which broad product lines are showing the best growth potential? Why?

   1.2.1. What types of people are most needed to help these business lines grow?

   1.3. What are the major structural trends in the industry? Why?

   1.3.1. Investment and wealth management– consolidation, acquisition, international growth?

   1.3.2. Individual lines (including annuities)

   1.3.3. Group products

   1.4. 1.4. What are the differences between independent and bank-based life insurers?

   1.4.1. How does this affect the kind of people they need to employ?

   1.4.2. Which domestic P&C companies can compete internationally? Who? Why (not)?

   1.5. Why have several Canadian life insurers fared so well in international markets?

   1.5.1. Why haven't bank-based life insurers expanded outside Canada?

   1.6. What is the role of reinsurers in facilitating growth, both domestically and abroad?

2. **Dynamics**

   2.1. What major forces drove change in the industry over the past decade? What was their impact?

   2.1.1. How are the next five years likely to differ? Why?

   2.2. What role does the political-regulatory environment play in growth/stagnation?

   2.2.1. How does the regulatory environment affect business?

   2.2.2. How will actuarial and accounting standard changes affect business?

   2.3. What has been the impact of the economic cycle? Regional differences?

   2.4. How is technology affecting the business? Clients? Getting business? Retention? Growth?

   2.5. What is the impact of shifting business or personal demographics, both for clients and staff?

   2.5.1. What are the shortages of key skills in the market? Reasons? Remedy?

   2.5.2. Voluntary and involuntary retirement? Transfers?

   2.5.3. Positioning for underwriting? Actuarial? Compliance? Risk management? Sales?

   2.5.4. What are the most serious shortages? Why?

2.6. Looking at your company, roughly how many actuaries and underwriters do you have?

  2.6.1. How many will be lost to voluntary or involuntary retirement over the next 5-10 years?

  2.6.2. In recruiting for these roles, what will be your primary focus? Experience, education, etc.?

  2.6.3. How will you source these positions? Actuaries? Underwriters?

  2.6.4. Given business volume trends, how many people are you likely to need?

2.7. Other companies have reported shortages of people for risk management, compliance, IT and sales. Given expected retirements and business trends, what are your needs in those areas?

2.8. Will likely changes over the next five years differentially help or hinder growth for any particular types of insurer or product line? Why?

2.9. What do you see as the major areas of employment growth in life insurers in the next 5-10 years? By business line?

3. <u>Success Factors</u>

3.1. Regionally, how do you assess prospects for growth? By business line?

3.2. What are the success factors that drive growth in your (each) business line?

3.3. What role do workforce skills play in success? What helps? What hinders?

3.4. To what extent do skills shortages hinder job creation?

  3.4.1. If skills shortages mentioned, ask: How do you deal with these skill shortages now?

  3.4.2. What do you think we should be doing to remedy these shortages?

3.5. Finally, what can be done to help Life insurers grow?

  3.5.1. Are there educational or training initiatives that can help?

  3.5.2. What can be done to "bring junior employees up the learning curve" to be ready for more senior positions?

Interview Guide – International Life Insurance

1. Structure

1.1. Who are the major global players in the life insurance market? Where are they active?

1.1.1. Which companies are expanding most aggressively? Where? Why?

1.2. What factors typically drive market entry?

1.2.1. Besides growth potential, what else? Domestic market maturity?

1.3. What are their typical entry strategies? Buy versus Build? Local Partner?

1.3.1. Are they leading with personal insurance lines, personal wealth lines, offshore wealth management or other business lines (e.g., annuity, creditor, disability, etc.)?

1.4. What is the role of reinsurers, especially in facilitating growth?

1.5. What are the most effective growth & survival strategies?

1.6. Where are life insurers exiting markets? Which companies? Why those markets?

1.6.1. What has pushed recent exits from Asia by some EU & US life insurers?

1.7. Where do Canadian life insurers fit in?

2. Dynamics

2.1. What major forces drove change in the industry over the past decade? What was their impact?

2.2. 2.2. How are the next five years likely to differ? Why?

2.3. 2.3. What unique forces are at work in different regions? Economic? Demographic? Technology?

2.4. 2.4. How will regulatory, actuarial and accounting standard changes affect business?

2.5. 2.5. What shifts in growth prospects & market attractiveness are we seeing?

2.5.1. Regionally, how would you assess prospects for growth?

2.5.2. Personal lines? Group products? Specialized lines?

2.5.3. Wealth management? Investment Management?

2.6. Globally, how will the positions of the major players shift over the next 5-10 years? Why?

2.7. How will Canadian insurers fare in the face of global and domestic changes (SLF, MFC, GWL)?

2.7.1. Domestically, in Canada?

2.7.2. In the US? GWL in the face of EU economic crises?

2.7.3. SLF & MFC in the face of economic slowdowns in much of Asia?

2.7.4. In response to growth in Latin America?

3. **<u>Success Factors</u>**

3.1. What are the success factors that drive growth in the industry?

3.1.1. Why have Canadian life insurers done so well outside Canada?

3.1.2. Why have they been more successful than Canadian bank-based insurers internationally?

3.2. How do success factors differ by region?

3.3. What role do workforce skills play in success? What helps? What hinders?

3.4. How much of the day-to-day operations are driven to low cost countries?

3.5. To what extent does international business stimulate job creation at home for Canadian life insurers? What types of jobs? What kinds of numbers?

3.6. To what extent do skills shortages hinder job creation at home?

3.6.1. If skills shortages mentioned, ask: How do you deal with these skill shortages now?

3.6.2. What do you think we should be doing to remedy these shortages?

3.7. What do you see as the growth prospects of Canadian life insurers in the next 5-10 years?

3.8. Finally, what can be done to help Canadian life insurers be more successful?

Interview Guide – Domestic P&C Insurance

1. **Structure**

   1.1. Which major players in the P&C market are expanding most aggressively? Commercial? Personal? Specialty? Why?

   1.2. What are the major structural trends in the industry? Consolidation? Exit? Entry? Why?

   1.3. Are there systematic differences between domestic and international P&C companies?

      1.3.1. Why have foreign P&C companies been so successful in Canada?

      1.3.2. Which domestic P&C companies can compete internationally? Who? Why (not)?

   1.4. Where do bank-based P&C companies fit in? Auto/Home? Creditor? Any commercial?

   1.5. What is the role of reinsurers, especially in facilitating growth?

2. **Dynamics**

   2.1. What major forces drove change in the industry over the past decade? What was their impact?

      2.1.1. How are the next five years likely to differ? Why?

   2.2. What role does the political-regulatory environment play in growth/stagnation?

      2.2.1. How does the regulatory environment affect business?

      2.2.2. How will actuarial and accounting standard changes affect business?

   2.3. What has been the impact of the economic cycle? Regional differences?

   2.4. How is technology affecting the business? Clients? Getting business? Retention? Growth?

   2.5. What is the impact of shifting business or personal demographics, both for clients and staff?

      2.5.1. What are the shortages of key skills in the market? Reasons? Remedy?

      2.5.2. Voluntary and involuntary retirement? Transfers?

      2.5.3. Positioning for underwriting? Actuarial? Compliance? Risk management? Sales?

      2.5.4. What are the most serious shortages? Why?

   2.6. Looking at your company, roughly how many actuaries and underwriters do you have?

      2.6.1. How many will be lost to voluntary or involuntary retirement over the next 5-10 years?

      2.6.2. In recruiting for these roles, what will be your primary focus? Experience, education, etc.?

      2.6.3. How will you source these positions? Actuaries? Underwriters?

      2.6.4. Given business volume trends, how many people are you likely to need?

2.7. Other companies have reported shortages of people for risk management, compliance, IT and sales. Given expected retirements and business trends, what are your needs in those areas?

2.8. Will likely changes over the next five years differentially help or hinder growth for any particular types of insurer or product line? Why?

2.9. What do you see as the growth prospects of P&C insurers in the next 5-10 years?

2.9.1. How does this differ by business line?

3. Success Factors

3.1. Regionally, how do you assess prospects for growth? Commercial? Personal? Specialized?

3.2. What are the success factors that drive growth in the industry?

3.3. Where do you see the potential for growth in your part of the business? Why?

3.4. What role do workforce skills play in success? What helps? What hinders?

3.5. To what extent do skills shortages hinder job creation?

3.5.1. If skills shortages mentioned, ask: How do you deal with these skill shortages now?

3.5.2. What do you think we should be doing to remedy these shortages?

3.6. Finally, what can be done to help P&C insurers grow?

Interview Guide – International P&C

1. Structure

1.1. Who are the major global players in the P&C market? Where are they active?

1.1.1. Which companies are expanding most aggressively? Where? Why?

1.2. What factors typically drive market entry?

1.2.1. Besides growth potential, what else? Domestic market maturity?

1.3. What are their typical entry strategies? Buy versus Build? Local Partner?

1.3.1. Are they leading with their personal insurance lines, commercial lines or specialty?

1.4. What is the role of reinsurers, especially in facilitating growth?

1.5. What are the most effective growth & survival strategies?

1.6. Where are P&C companies exiting markets? Which companies? Why those markets?

1.6.1. What drove AXA and ING exits from Canada?

1.7. Which Canadian P&C insurers have substantial US or international activity?

1.8. Domestically, what are the differences between independent Canadian-based P&C insurers (e.g., Intact, Dominion, Co-operators, Guarantee, Economical, etc.), Bank-based P&C insurers (Desjardins, The Personal, RBC, TD, Scotia), and foreign P&C insurers (e.g., Zurich, Aviva, Allstate, State Farm, etc.)? Product lines? Distribution?

2. **Dynamics**

2.1. What major forces drove change in the industry over the past decade? What was their impact?

2.2. How are the next five years likely to differ? Why?

2.3. What unique forces are at work in different regions? Economic? Demographic? Technology?

2.4. How will regulatory, actuarial and accounting standard changes affect business?

2.5. What shifts in growth prospects & market attractiveness are we seeing?

2.5.1. 2.5.1.Regionally, what are prospects for growth?

2.5.2. 2.5.2.Personal? Commercial? Specialized?

2.6. Globally, how will the positions of the major players to shift over the next 5-10 years? Why?

2.7. How will Canadian insurers fare in the face of global and domestic market changes? Why?

2.7.1. How will Canadian bank-based life insurers fare in the P&C market? Why?

3. **Success Factors**

3.1. What are the success factors that drive growth in the industry?

3.1.1. Why have Canadian P&C insurers remained domestic while life has thrived internationally?

3.1.2. Why have the European P&C insurers been successful globally?

3.2. How do success factors differ by region?

3.3. What role do workforce skills play in success? What helps? What hinders?

3.4. How much of the day-to-day operations are driven to low cost countries?

3.5. To what extent does international business stimulate job creation at home for Canadian P&C insurers? What types of jobs? What kinds of numbers?

3.6. To what extent do skills shortages hinder job creation at home?

3.6.1. If skills shortages mentioned, ask: How do you deal with these skill shortages now?

3.6.2. What do you think we should be doing to remedy these shortages?

3.7. What do you see as the growth prospects of Canadian insurers in the next 5-10 years?

3.8. Finally, what can be done to help Canadian P&C insurers be more successful?

June 2014