Of Special Interest

Insurance Technology and Innovation: Invest, Buy or Build

2020 marked the Mayer Brown's Insurance Industry Forum's seventh year bringing together industry leaders, insurance regulators and leading bankers and advisors to the industry to discuss global trends and recent developments in insurance M&A and corporate finance. This year's forum was held virtually over two webinars in consideration of the global pandemic.

During the virtual forum's second day, a panel of insurance industry professionals discussed insurance innovation and the implications for M&A transactions in the sector. The panel was composed of Root's Jon Allison, Plug and Play's Nick Daley and CB Insights' Mike Fitzgerald. Mayer Brown's Paul Chen moderated.

Here we sum up the takeaways from the discussion.

Competition Rising

The panelists agreed that although technology has accelerated innovation in the insurance industry, which has enabled insurance companies to better serve their policyholders, it has also presented new challenges. For example, insurance companies have had to accelerate their transformation to digital processes not only to meet consumer expectations but also to keep up with competition. The panel noted that competition for insurance customers is growing beyond companies that just focus on insurance. Insurtech companies are using technology to target particular niches in the industry and large technology companies are emphasizing customer experience to meet a broad spectrum of a consumer's needs—whether those needs are financial, insurance, health or lifestyle-driven.

R&D Lagging

Despite the increased competition, the panel noted that traditional insurance companies continue to underinvest in technology and innovation. It was noted that not a single insurance company is among the top 1,000 companies across all industries in terms of R&D spend. Most of the R&D expenditures have gone toward analyzing how to use technology to modernize infrastructure and improve operations rather than to integrate revolutionary and cutting-edge innovation into the business. This comparatively low R&D investment could very well be due to the nature of operating in a highly regulated industry but also a function of risk-reward in an industry where the risk of failure has greater consequences. Regardless of the cause, the panel agreed that more insurance companies would need to increase their investments in technology and innovation going forward due to the acceleration of digitization in consumer markets in general and the rise of competition from technology companies and insurtechs.

M&A Increasing

The panelists agreed that the drive to accelerate digitization in the insurance industry would likely result in more M&A transactions. The panel noted that certain insurance companies have been increasing their lead in technology and innovation for several years, and companies that started off as smaller insurtechs have recently been gaining scale and momentum by transforming themselves from technology-enabled distributors or managing general agents to underwriting insurance by acquiring or forming insurance companies. To build up scale and capabilities quickly, insurance companies, insurtechs and technology companies alike are likely to need to look to mergers and acquisitions.

Additional Takeaways

The panelists also noted:

- After a decline in insurtech startup investment in the second quarter of this year due to the impact of COVID-19, insurtech start-up funding has resumed its upward trend. In fact, the third quarter set a record for investment amount driven partly by six mega-round investments, including capital raisings by Next, Hippo and Policy Bazaar.
- The investment data supports the concept that successful insurtech companies launched a few years ago are widening the lead against smaller insurtech companies in terms of growing market share and securing capital. Lemonade completed its IPO earlier this year, and Root is launching its IPO.
- In general, regulators and insurtech companies are collaborating more, which has helped them focus on solving problems related to the convergence of technology and traditional insurance regulatory concerns. This in turn is likely to lead to more transactions between insurance carriers and insurtech companies and also among insurtech companies looking to increase product scope and operating scale.
- The insurance industry may not be appropriately taking into account the technology growth factor in valuing traditional insurance players, especially when discussions are often still focused on loss, reserving client base and high valuations for up-and-coming insurtech companies.

If you would like to receive the recording of either or both webinars, please reach out to either author of this article.

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