THE INSURANCE Insider
MGA REVIEW

Summer 2019

MGAs face flight to quality

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Raising the bar

Who would want to run an MGA these days?

In fact, the answer is quite a lot of people, actually.

Over the past decade, the traditional (re)insurance market has made it increasingly difficult for entrepreneurs to flourish.

Red tape can choke creativity, and the complexity of corporate decision-making and compliance is frustrating for those fleet of foot.

Even the barriers to entry to Lloyd's, the industry's traditional home for big thinkers and ambitious business leaders, have become impossibly high for many.

> "The MGAs of the future need to be leaner, more cost-effective and tech-enabled. They cannot be adding needless cost in a distribution chain that already has several mouths to feed"

So it's unsurprising that the idea of setting up your own business and being in control of your own destiny – with the potential of a significant exit sum at the end of it – has appealed to so many, and the MGA market has mushroomed as a result.

But market conditions for MGAs are changing.

Paper providers are under pressure, and their returns are dwindling. They are looking to regain control of their underwriting, to bring matters back into their own hands.

This was most clearly demonstrated at 1 Lime Street, where Lloyd's push to improve performance as a whole led to a retrenchment of delegated authority capacity, as carriers looked to determine which MGA partnerships give them more bang for their buck.

This capacity, coveted for its licensing and rating privileges, is not easily replaceable in the company market.

Insurance's bulging expense ratio is still an endemic problem across the industry and you would be a fool to think that efficiency isn't at the top of every carrier's priority list.

Cutting back on MGA relationships is an easy, albeit blunt, solution to that problem.

The theme of this year's Managing General Agents' Association conference is "survival of the fittest" – and that Darwinian theme could not be more apt at this point in time.

Those MGAs that adapt will win.

The MGAs of the future need to be leaner, more cost-effective and tech-enabled. They cannot be adding needless cost in a distribution chain that already has several mouths to feed.

Product innovation, actuarial capabilities and full confidence and authority in claims handling are becoming increasingly attractive.

And of course, MGAs still need to do the basics of providing unrivalled expertise and distribution, impeccably.

The beauty of the MGA market is its diversity, and there will be variations on this recipe for success.

But there is no denying that the playing field has changed. Paper providers will be demanding and finding alignment with these partners as they adapt to their own challenges will be crucial.

The desirability of launching a new MGA remains – but new entrants must be minded that carriers' expectations will be higher than ever.

Catrin Shi
Acting Managing Editor,
The Insurance Insider

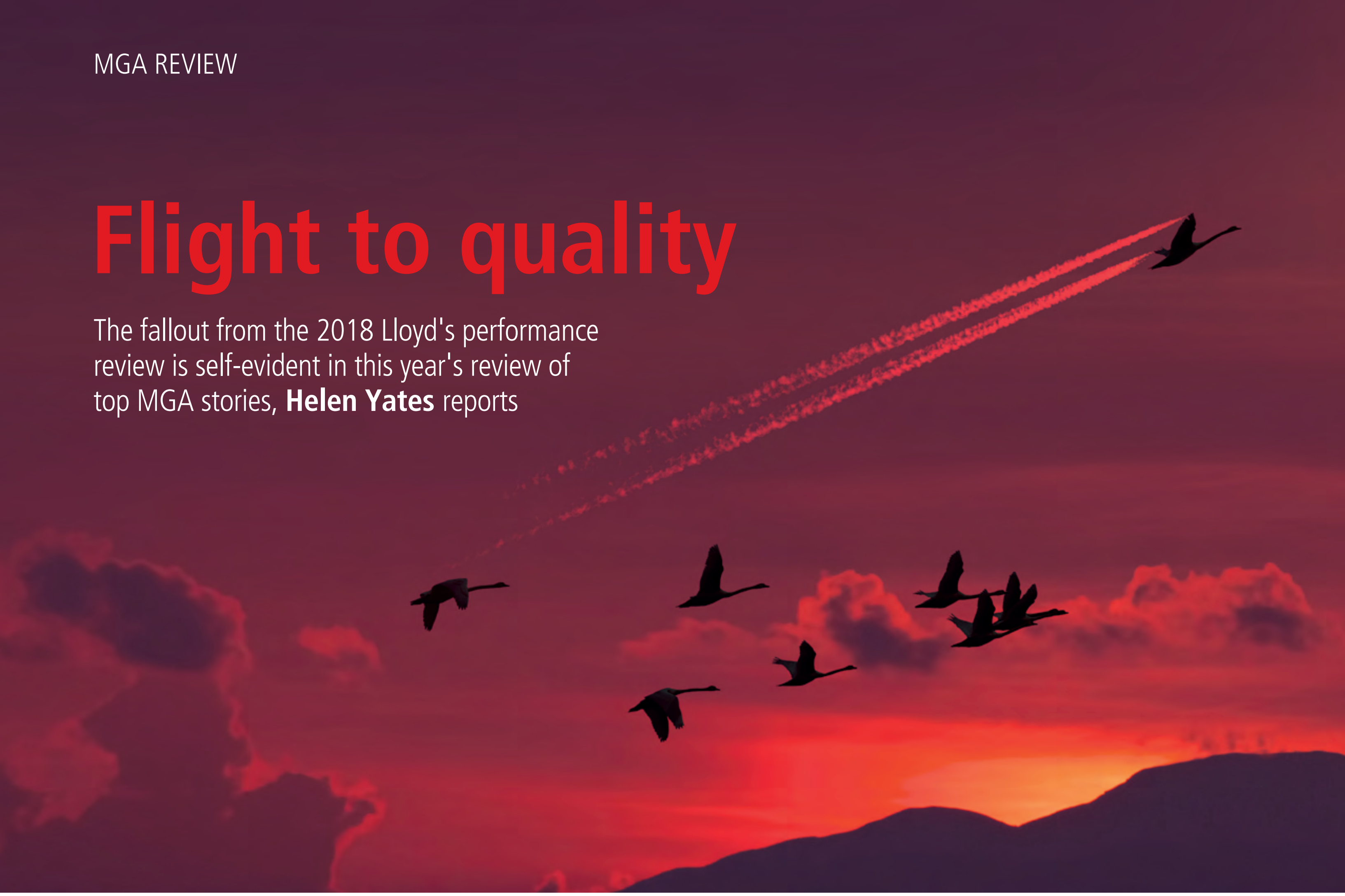
Message from the sponsor

Davies Insurance Services is delighted to sponsor this special MGAA supplement.

The popularity of the MGA sector continues to grow, but that growth comes against a backdrop of even greater challenges for MGAs and their capacity providers.

At Davies Insurance Services we continue to support MGAs throughout every step of their formation and operation.

Technology will play a greater role in the ability of MGAs to deliver risk mitigation to clients and drive efficiencies. We look forward to meeting the market at the conference and demonstrating the wide range of services we can provide to the sector.



Flight to quality

The fallout from the 2018 Lloyd's performance review is self-evident in this year's review of top MGA stories, **Helen Yates** reports

What a difference 12 months makes. In last year's report our MGA review focused on new entrants and a healthy pipeline, but predicted a stress test was around the corner. And now, mid-way through 2019, it is clear that stress test has arrived.

In particular, the fallout from last year's Lloyd's performance review is having an impact, with a flight to quality. The MGA bubble may not have burst just yet but its growth trajectory has slowed, with Lloyd's backers showing a more selective approach than in previous years. Their efforts to trim acquisition costs and be more selective with delegated authority capacity is driving a shake-up within the wider MGA market.

According to one unnamed broker, speaking to *The Insurance Insider* in January: "The most sophisticated MGAs realise that this will work as a clear-out of the worst-performing MGAs, and they will ultimately enter 2019 with less upfront competition. They also realise that the market would have been in a worse position in 2019 if Lloyd's hadn't taken action the way it did."

Investment firm BP Marsh recently revealed that MGA business proposals had been outstripped by attractive potential broking investments. And in early June, when heavyweight MGA CFC Underwriting said it had broadened its line-up to include players outside the Lloyd's market for the first time, it was certainly a sign of change.

Previously backed 100 percent by Lloyd's, CFC announced it had brought in paper from five company market sources to supplement its Lloyd's paper. It is understood that bullish growth ambitions drove the decision to seek additional support from outside Lloyd's.

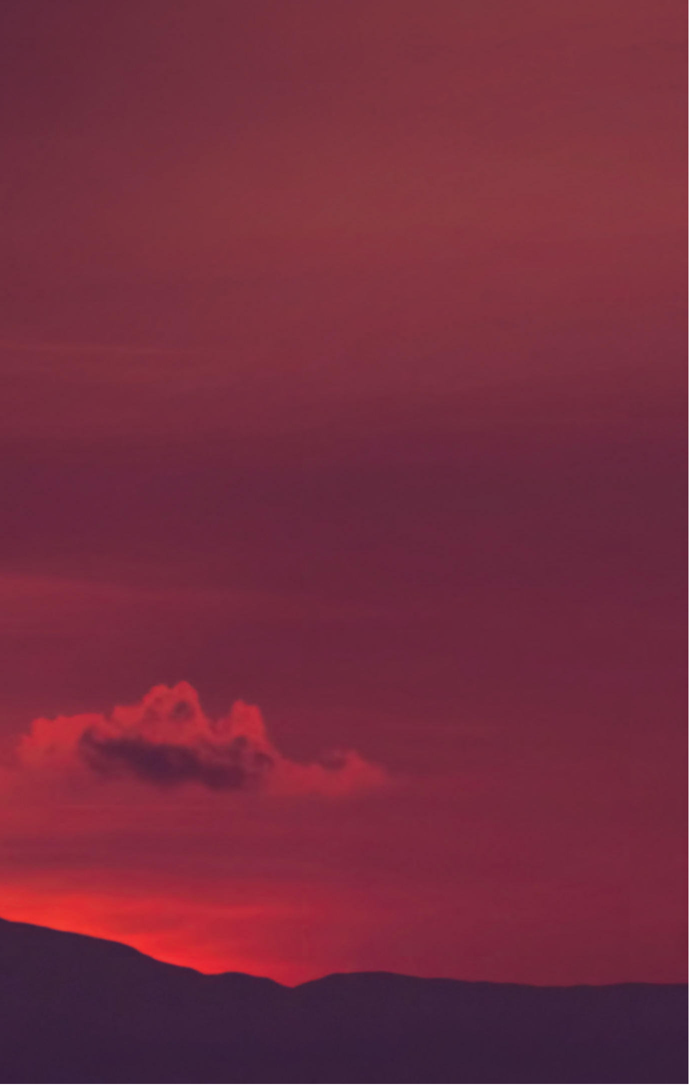
This followed the announcement in May that Aspen Insurance had decided to place its MGA, Aspen Risk Management Ltd, into run-off having – it is understood – failed to secure a buyer. The move followed "a review of our insurance strategy", according to the Apollo Global Management-backed insurer.

And in February, Standard Club abandoned its plans to set up an MGA after Syndicate 1884 became a Lloyd's Decile 10 victim. The shipowners' mutual was working on a proposal to continue writing on a delegated authority basis, backed by company market paper, but decided against the scheme.

> "The MGA bubble may not have burst yet, but its growth trajectory has slowed, with Lloyd's backers showing a more selective approach than in previous years"

In April, the CEO of Pro Global Holdings, Artur Niemczewski, predicted a process of natural selection in the MGA sector. He suggested successful MGAs would need to "genuinely add value" and play in non-standard sectors: "If the MGA sits there and is just an intermediary and the risks are standard, clearly someone will come in and say 'Why are we paying extra money?'"

Set against that backdrop, the highlights of the past year reveal a search by MGAs for backers beyond Lloyd's, a slew of new entrants focused



on specialist lines of business, a surge in interest in MGA incubators and the continued movement of senior talent – some of them victims of the performance clampdown – seeking to re-enter the market.

Niche play for start-up MGAs

In January, US-focused Waypoint Underwriting Management received coverholder approval from Lloyd's. The MGA is to write accident and health (A&H) business on behalf of ArgoGlobal Syndicate 1200. ArgoGlobal A&H class underwriter Adam Zawia said the approval would help the carrier expand its access to A&H expertise in the US.

Meanwhile, in February, former Aspen active underwriter Ed Beckwith returned to the market in collaboration with former Pembroke head of tax Tom Cartwright to set up a tax insurance specialist MGA. The new venture, Certa Insurance Services, used Integro-owned MGA incubator platform Svalinn for the launch and already has a strong Lloyd's backing.

Also in February, MGA Trilogy established a UK construction product with capacity from Great American International Insurance. Meanwhile, Hiscox launched a binder in partnership with UK MGA Stride Insurance Group, targeting mid-market residential and retail business. The month closed with Nigel Gladwell, former president and CEO of Acrisure-subsidiary Upstream Brokers, leaving to launch energy MGA Bayshore Underwriters.

Energy remained a theme in April, when MGA Aurous Risk Partners secured its first energy binder with capacity from Arcus Syndicate 1856. The MGA will be able to write risks throughout the European Economic Area via Arcus' presence on the Lloyd's Brussels platform.

In May, drone MGA SkyWatch. AI signed up nine retail brokers to distribute its Starr Companies-backed aviation insurance, as the InsurTech diversified distribution away from an app. Meanwhile, construction sector-focused MGA Ensurance set up a terrorism and sabotage product with the hire of two underwriters from MGA Omnyy.

In June, Medical Protection Services launched an MGA with paper provided by Everest Syndicate 2786, through which it will write a medical malpractice account produced directly by MPS from its UK and international networks. Although not an insurer, MPS is a mutual society that defends doctors, dentists and other healthcare professionals and organisations around the world.

Also in June, Willis-backed MGA platform Innovisk Capital Partners established a specialist M&A MGA. Themis is based in London and is the third UK vehicle established via the platform.

A slice of the action

In March, Arch Insurance International revealed an investment in personal lines MGA Archipelago. Archipelago was founded by former Aon executives Angus Simpson and Richard Coleman, and writes only intermediated business in the UK, catering to mid- to high-net-worth individuals.

In April, Tokio Marine Holdings' US arm Tokio Marine HCC acquired the 51 percent stake in US MGA NAS Insurance that the group did not already own. NAS offers cyber and professional liability insurance. Tokio Marine bought a 49 percent stake in the MGA in February 2014 through its UK arm, Tokio Marine Kiln.

Also in April, Pro Global Holdings acquired two-year old MGA incubator Vibe, with plans to use it as a launchpad to expand into distribution services. It was followed in May, by the acquisition of MGA platform K2 Insurance Services by Lee Equity Partners.

In May, MS Amlin announced it had taken a minority stake in cyber MGA Envelop Risk, with global MD James Few taking up a board position. The MGA was also backed by insurance industry entrepreneur Peter Hastie. It was launched in April 2018 under the leadership of CEO Jonathan Spry, the founder of New Nordic Advisors.

Meanwhile, Nexus acquired Capital Risks MGA in May. The warranty and indemnity MGA has been renamed Nexus Transactional Risks. In June the acquisitive London-headquartered MGA hired Marc van der Veer as CEO of European ventures from Ardonagh to continue its strategy of buying niche European specialty MGAs.

People moves

In February, the Managing General Agents' Association appointed Markerstudy co-founder and underwriting director Gary Humphreys to its board. Markerstudy is the UK's largest MGA and was acquired by Qatar Re last year.

In April, Michael Ferber was named CEO of Dovetail Insurance, a digital MGA that is part of Marsh's Victor underwriting platform. Ferber was previously chief information officer at US property cat specialist ICAT.

Meanwhile, Talbir Bains' MGA platform Volante has been on a hiring spree so far in 2019, snapping up Barbican's business group leader for cyber Graeme King in April and Antares' head of financial institutions Steve Redding back in February.

The MGA class of 2019

Chris Butcher explains why new entrants to the MGA market are increasingly looking to incorporate technology into their offering

Despite a challenging UK and international insurance landscape, when it comes to the will to launch MGAs, the momentum has not been diminished.

Every year at the Managing General Agents' Association conference there is no shortage of interest. The insurance market is dynamic and innovative and MGAs are viewed as an efficient way to quickly bring new products and ideas to market.

There remains an appetite from experienced insurance professionals who have identified opportunities in the market, and they continue to seek underwriting capacity to make the most of these.

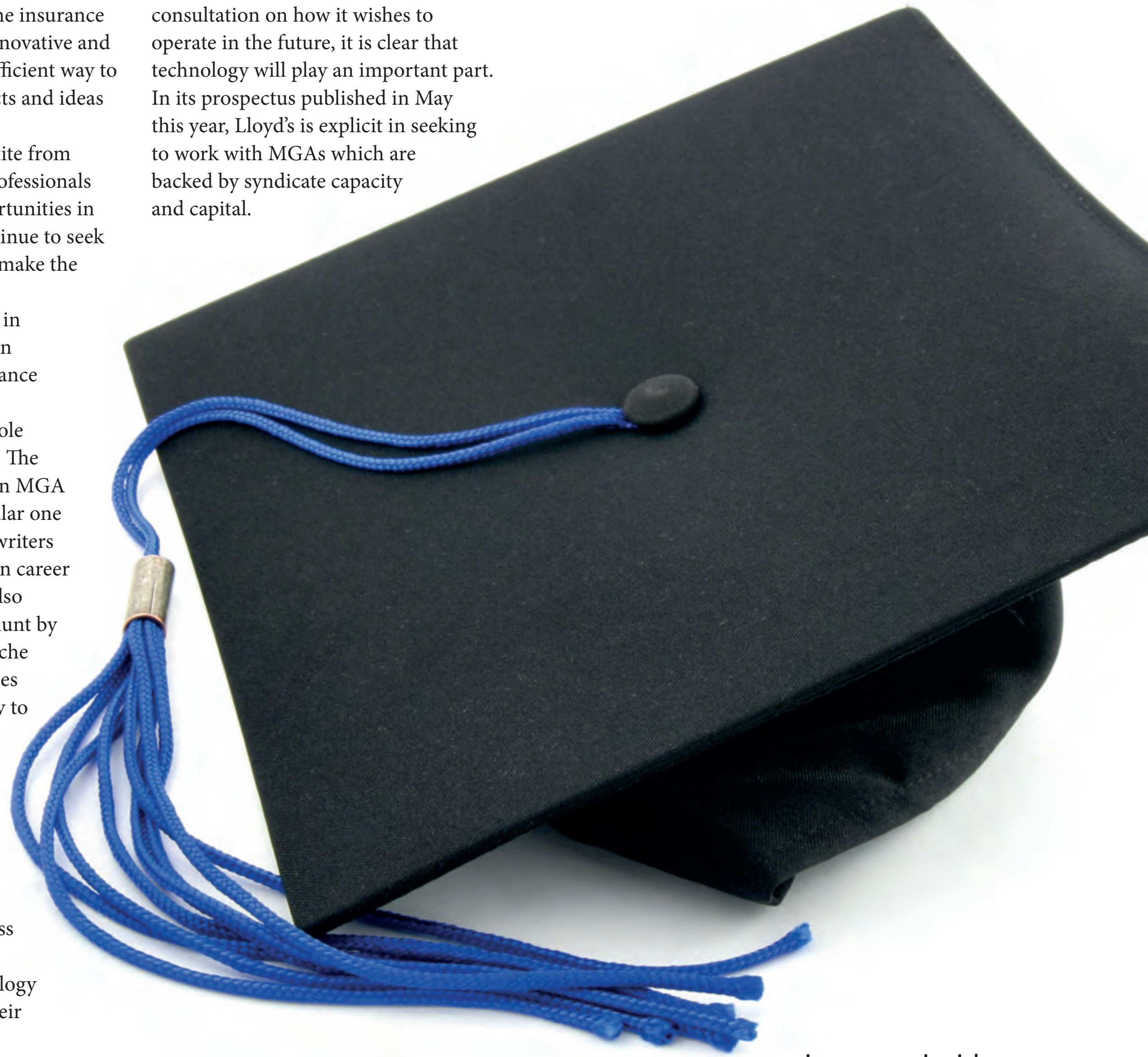
Ongoing M&A activity in the industry has created an environment where insurance professionals may be left questioning their future role in a new combined entity. The option to launch their own MGA operation remains a popular one for entrepeneurial underwriters or brokers with less certain career paths. The movement is also driven by the continued hunt by some in the market for niche and specialist opportunities that will put their capacity to more profitable use.

InsurTech collaborations

What has changed noticeably over the past 12 months is that those looking to shape a business case for a new MGA are increasingly using technology as the key attraction in their offering. These new entrants view the use of new technology as part and parcel of their operations, not only to win business but also to create further efficiencies and to push down costs.

At a time when the Lloyd's market is undergoing its own period of consultation on how it wishes to operate in the future, it is clear that technology will play an important part. In its prospectus published in May this year, Lloyd's is explicit in seeking to work with MGAs which are backed by syndicate capacity and capital.

"It is clear that regulatory pressure is also shaping the MGA market in 2019 and dictating the way in which new start-ups are being formed"



Many start-ups are using InsurTech and believe that this new approach will enhance their ability to win the backing of capacity providers. For insurers and reinsurers, these MGAs are a perfect testing ground for such technology – which, if successful, can then be scaled-up quickly and potentially more widely integrated in other classes of business.

The use of new technology and systems is not simply restricted to emerging areas of the business. It is also being applied by those that are looking to create operations to access the more traditional B2B classes. They are keen to work with brokers and believe that a technology-enabled front end will prove to be a significant positive in their operations.

Many are using technology to better assess risks by delivering broader and richer data on which they can base their risk selection and pricing decisions. Either working with their brokers or direct with their clients they are using data more effectively and finding new systems which can deliver those benefits.

This allows MGAs to potentially offer solutions that are not currently available. Such an approach should ensure that volumes of business and the pipeline of start-up MGAs remain stable throughout 2019 and beyond.

Lloyd's has recognised the need to deliver efficiencies and to reduce the cost of doing business and it is those frictional costs that MGAs believe they impact via a more responsive operating model.

The "syndicate in a box" model, one of six options outlined by Lloyd's, has created a new option for some MGAs as they look to shape their structure. It could be part of an MGA's route to market and there have been conversations as to how such a system would work and the benefits it could bring to new or existing MGAs.

Regulatory scrutiny

It is clear that regulatory pressure is also shaping the MGA market in 2019 and dictating the way in which new start-ups are being formed. In the wake of the Financial Conduct Authority's (FCA) review of the wholesale broking market there is little doubt that the regulators now have the insurance industry and its stakeholders in their sights.

The Prudential Regulation Authority is understood to be looking at the MGA sector given its operating model. There is said to be some concern that MGAs underwrite risks and are deploying capacity but do so without themselves holding reserves. From the regulator's perspective they are acting as insurers, but from a significantly lower capital base.

It is clear that the regulator will continue to monitor the sector's efforts to meet the requirements of the Insurance Distribution Directive, falling as they do within its remit. We have seen, and continue to see, that MGAs which have established their business and their client base are now looking to move away from the authorised representative status to seek full FCA authorisation.

Such authorisation requires a clear set of standards when it comes to internal procedures. We have found, as we work through the process with our MGA partners, that they require a significant amount of work before they are confident that their internal procedures are at a level that would meet the regulator's requirements.

Few, if any, MGAs are formed by those who come from a compliance background. By their nature, MGAs are focused on a business area believed to be underserved, ignored or ripe for disruption and are typically driven by those from an underwriting and broking background.

This is changing slightly as those with a technology background, who can see how those systems can benefit the insurance sector, are now engaging with capacity providers. The issue then is to demonstrate to the capacity provider how this new way of working can translate into better underwriting.

The final quarter of the year will no doubt be focused on Lloyd's blueprint for its future and how MGAs can fit into the new framework. It is certain to provide opportunities for those targeting the speciality and emerging risk classes, such as cyber. It may also provide options for those who are looking at more commoditised products.

But as MGAs look to seize these opportunities they cannot ignore their regulatory and internal responsibilities. The business needs to be built on a foundation that focuses on compliance, automation and the efficient delivery of products. A track record in underwriting or broking is no longer enough to launch a new start-up. The next generation of MGAs will need to collaborate with entities or individuals that can offer compliance and tech knowhow.

Chris Butcher is CEO of Davies Insurance Services

The Syndicate-in-a-Box route to market – a glimpse of the future

Lloyd's new Syndicate-in-a-Box option could make joining the market much easier and more cost-effective for new, innovative entrants. The joining process promises to be fast, streamlined and digital, making it much easier to bring capital to market and attach it to risks. Capital providers are matched with risks or syndicates based on pre-set preferences, with the option to set up syndicates remotely, avoiding the expense of setting up an office in London.

Risks are placed electronically and there will be access to all the data and services available in the Lloyd's ecosystem. The Syndicate-in-a-Box model will allow participants to buy centralised services from other market players or third-party providers – functions like HR, payroll, reporting and claims. As syndicates grow, they can outsource more of these services or bring them in-house as is needed.

Everyone is set to benefit from these lower costs – not least customers.

The other benefit from Syndicate-in-a-Box is access to Lloyd's Centre for Innovation, a centralised hub of both Lloyd's market and third-party data and insights.

Source: Lloyd's

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Automating for the future

Tim Rayner explains why the MGA sector is at the heart of the London market's modernisation efforts and looks at how far it needs to go

Ask anyone in the London market and they will say the MGA sector remains an attractive use of underwriting capital. However, as the market continues to grapple with unacceptable acquisition costs, pressure on rates and increased competition, MGAs and their capacity providers are looking at how technology can enhance their operations and deliver efficiencies.

Lloyd's gross written premium from binders in 2018 totalled £12.5bn (39 percent), with a further £1.6bn (5 percent) coming from lineslips. In September, Lloyd's will announce the results of its consultation process on the Future at Lloyd's prospectus document, launched by CEO John Neal in May. One of the initiatives referenced in the prospectus is the creation of a Lloyd's Risk Exchange which will facilitate the placement of less complex risks, with target costs at a fraction of what they are today.

The MGA sector is a ripe testing ground such initiatives, given the generally standardised and simpler products that are offered by these intermediaries. Technology can and will have a range of benefits for the MGA sector, where there are very high volumes of policies transacted via a variety of facility-type placements into the London market.

Technology is available today that can increase the speed of delivery of products to market and will enable the London market to get closer to the end insurance buyer. There is a broad move towards greater use of technology to reduce back-office costs and the frictional cost of doing business, particularly in specialty lines.

This has created a need for MGAs to not only understand the benefits technology can bring, but also how best to deploy it in order to remain relevant and competitive in a potentially reduced value chain.

> "The greater the number of parties in the value chain the more parties that need to be remunerated, so the cost of acquisition needs to be reduced"

Why speed is of the essence

The role technology will play in the market's interaction with MGAs and coverholders was discussed recently at the Verisk Vision conference in London. The panel session, moderated by Sequel CEO Ian Summers, posed a range of questions that highlighted both the importance of the MGA sector and the need to ensure that the market works to meet the challenges that it faces.

It is interesting that there remains a debate around how the allocation of aggregate capital could potentially be affected by advances in technology and the ability to deliver easier and quicker access to data. Some at the event said they were struggling to understand why there has been such a limited adoption of real-time data initiatives despite the benefits they can bring.

Tim Rayner is business development director at Sequel

At the heart of the issue remains the question of product distribution and ease of transacting business through the value chain. The plans for the Lloyd's Risk Exchange aside, the market needs to examine how it can enhance the way it gets its products to market via MGAs. Whatever the systems the MGA has in place, the continued reliance upon a monthly bordereau stifles efforts to increase speed, introduce efficiencies and reduce acquisition costs.

The London market is not standing still, however. Its Target Operating Model is making a difference, although there is growing frustration that the market continues to move at such a slow pace. Nevertheless, tangible progress is being made and a number of initiatives are underway that have provided valuable insight into the issues the MGA sector faces.

The work Sequel has carried out in the MGA sector has resulted in the development of Sequel Coverholder Workbench (Workbench), which underwent a successful pilot in late 2018. Workbench offers an ecosystem of services, delivered via the cloud, that reduces costs and delivers operating efficiencies to MGAs of all sizes.

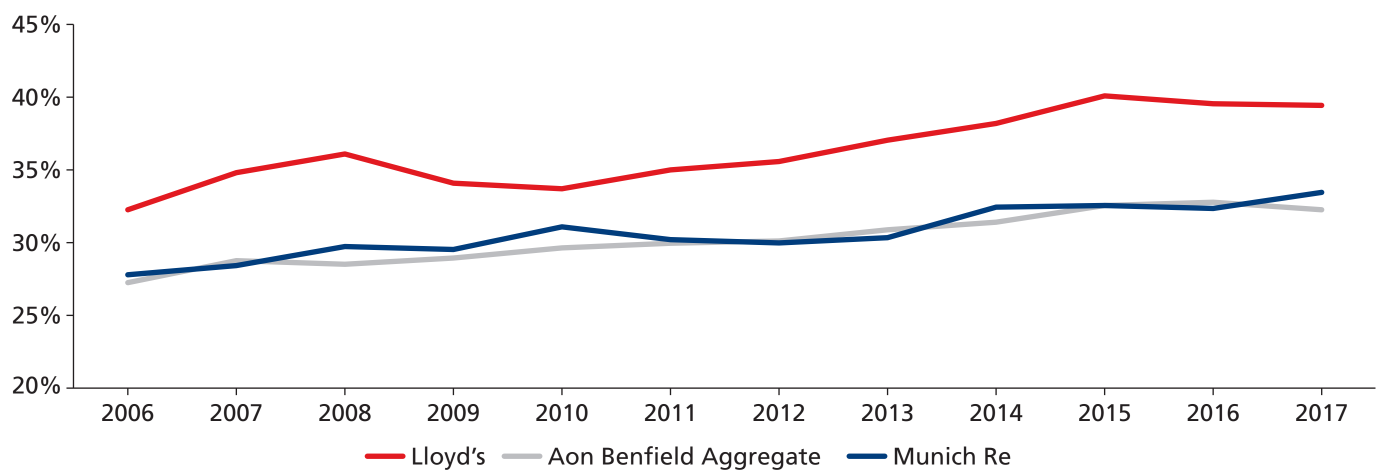
At present, the general view is that it takes too long to launch and distribute new products through the value chain. One potential solution to this problem is the move towards cloud-based product distribution to enable a global risk exchange or marketplace. Full API (application programming interfaces) would allow existing MGA systems to be integrated with the solution, thereby keeping adoption costs to a minimum.

The greater the number of parties in the value chain the more parties that need to be remunerated, so the cost of acquisition needs to be reduced. But for the market there also needs to be greater control on the utilisation of its capacity.

> "The MGA sector is a ripe testing ground for new technology initiatives, given the generally standardised and simpler products that are offered by these intermediaries"

Adoption of a platform of this nature would allow MGAs to access and compare products. Crucially it will also provide underwriters with the ability to obtain real-time data to support underwriting decisions, monitor performance of their products and allow them to quickly adapt coverages or rates when changes to market conditions require immediate intervention.

Expense ratio trends – reinsurance and specialty insurance



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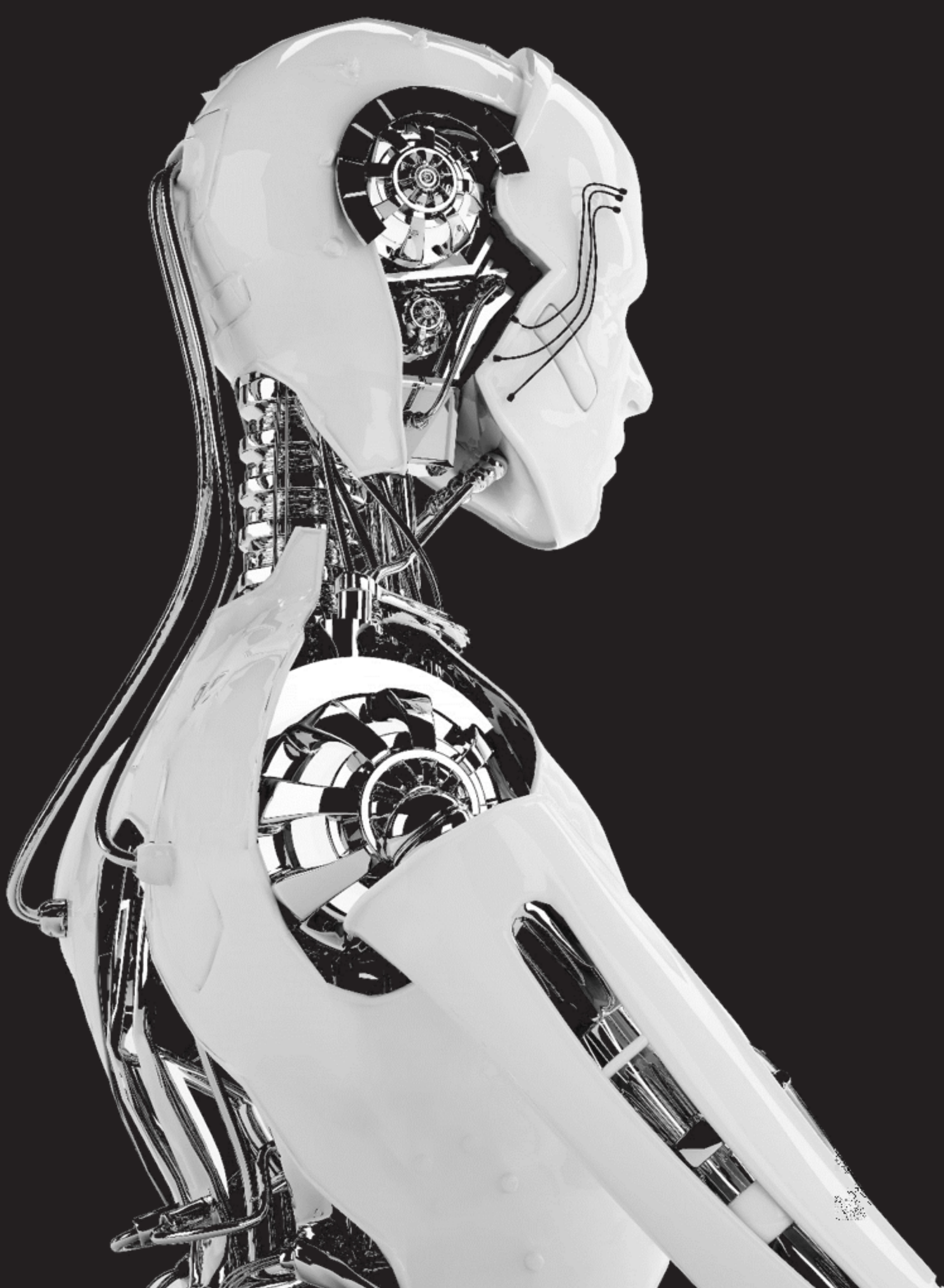

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