Grow or go: Taking a portfolio approach to growth

KPMG International

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Taking a portfolio approach to growth

In today's insurance environment, victory belongs to the bold. Margins are under pressure and competition is heating up; insurers can no longer afford to 'sit' on businesses that are under-performing or sub-scale.

By taking a portfolio approach to their businesses, insurers can start to assess the value and performance of their assets to make bold decisions on whether to 'grow' (build) or 'go' (exit) the business.

Time for bold decisions

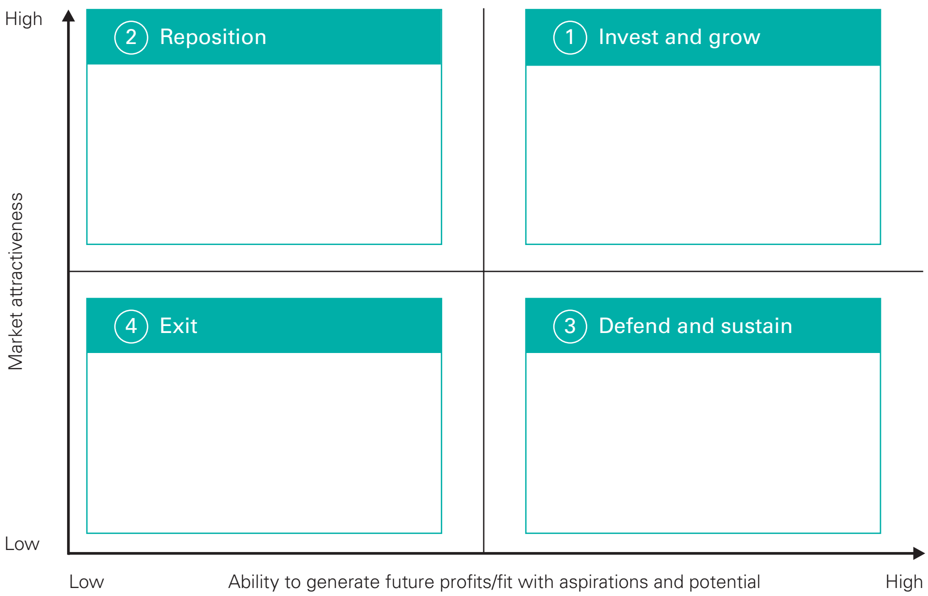
Facing continued low interest rates, growing rate pressures in the property and casualty (P&C) sector and high levels of competition in both the P&C and Life sectors, it seems clear that margins will continue to face downward pressure for the near future.

Not surprisingly, most have already undertaken massive cost reduction initiatives in an attempt to shore up margins. And now, with little room left to cut, some are starting to take a more critical and strategic view of their business as a whole.

Our experience suggests that insurers need to take bold action and make difficult decisions now if they hope to create shareholder value and grow their business. The reality is that too many insurers are carrying businesses that are sub-scale, underperforming or simply distracting for management.

To help organizations assess their businesses and local operations, we have developed a diagnostic tool that segments businesses in the following way:

Portfolio review — financial output



Source: KPMG International, 2015

Assessing businesses and local operationss

- Does the business or operation meet the group profitability and return on equity (ROE) thresholds?
- Can the business realistically achieve 'above average' market share growth?
- Does the business or operation target customer segments that play to your strengths?
- Does the distribution strategy support the broader strategic goals of your organization?
- Does the business or operation create value within a diversified strategy?
- Does the business or operation allow management to focus on strategic objectives?

If you answered 'no' to any of these questions then it may be time to make a 'grow or go' decision.

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Grow or Go?

Many insurance organizations are already executing on their 'grow or go' strategies.

Grow:

- AIG acquires Ageas' UK life protection business for USD$270 million.
- Willis Group acquired Gras Savoye Miller Insurance Services LLP and PMI Health Group.
- Bermuda based Endurance acquired Montpelier Re Holdings.
- Acquisition of Lloyd's of London insurer Amlin Plc by Japan's MS&AD.

Go:

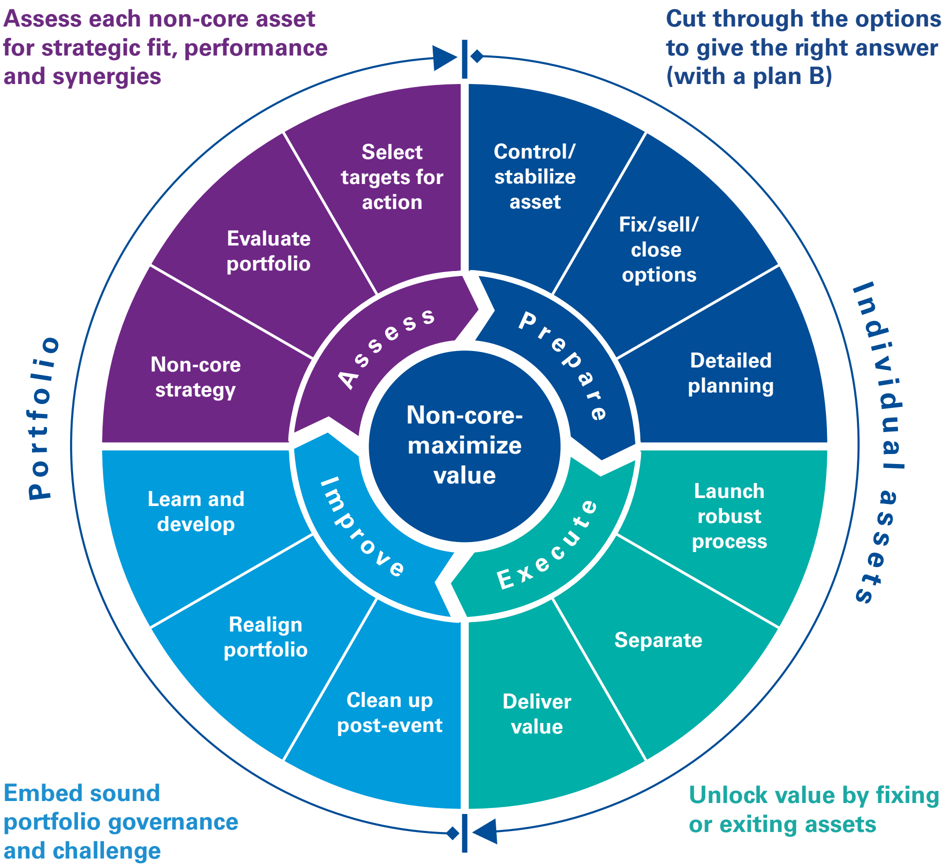
- AXA looks to sell its Portuguese operations to Ageas for USD$215 million.
- Zurich Insurance sells its general insurance retail business in Russia to OLMA group and is winding down its general insurance business in the Middle East.
- AXIS Capital Holdings winds down its retail insurance operations in Australia.
- Genworth Financial, Inc. to sell its non-core lifestyle protection insurance business.
- RSA to exit its business in Russia.

Taking a portfolio view

We firmly believe that there are significant opportunities to help insurers enhance shareholder value by taking a portfolio view of their assets. And, in doing so, insurance organizations should be able to make clear decisions about whether to 'go' (i.e. exit those markets and businesses that do not meet the strategic objectives of the organization) or 'grow' (i.e. committing to targeted investment to drive transformational change and improvement initiatives that will allow the business to compete effectively).

Indeed, by looking at non-core businesses as a portfolio of assets insurance executives should be able to properly ***assess*** each businesses' strategic fit, performance and synergies which, in turn, will enable them to identify opportunities to ***improve*** the business through portfolio realignment.

Taking a portfolio view will also provide insurance executives with the insight needed to ***prepare*** a fix, close or sell strategy that drives a clear approach for non-core assets and then move through to a robust ***execution*** plan with appropriate governance.



Source: KPMG International, 2015

Note: Transactions listed in this article have been adapted from a variety of publicly available sources.

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GO: A bespoke approach to divestment

In those cases where the assessment process leads to the decision to 'go', insurance executives will need to develop a smart divestment strategy for the business. Interestingly, our experience suggests that the divestment process has evolved considerably over the past decade.

Whereas in the past, the normal approach to selling a business involved rigid auction processes based on standard checklists and documents such as Information Memorandums and Vendor Due Diligence reports, most now recognize that this approach may not be fit for purpose to maximize value.

Instead, insurers are now taking a more bespoke and focused approach to divestment that is largely influenced by four key factors:

- economic conditions
- sellers taking control
- wider buyer populations
- business model changes.

8 practical tips for successful divestment

- Conduct a rapid readiness assessment: Focus on informed planning and preparation.
- Evidence the sales messages: Prove why the business would be an attractive purchase.
- Present a robust information package: Make sure messages are consistent and coherent.
- Deal only with credible bidders: Work with bidders you know and trust to deliver.
- Anticipate the value chips: Assess any issues or uncertainties that bidders could use to negotiate the price.
- Be clear about the impact of separation: Don't underestimate the costs and operational implications.
- Manage the 'soft' issues: Ensure you have the required skills, agility and capability to meet the objective.

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GROW: More than just scale

Insurers need to have sufficient optionality and diversification to respond to a rapidly changing business environment. And while not all divisions and local operations need to be 'market leading', they do need to demonstrate how they can make a positive contribution to the overall strategic ambitions of the organization.

For some, the answer will come in the form of inorganic growth within their sub-scale businesses. For others, targeted investments to support product growth initiatives or new distribution arrangements offer a lower-risk solution.

However, while many deals have been driven recently by organizations with a (fully understandable) strong focus on costs and efficiency, we often find that scale, in itself, is not a good enough reason to support a deal. Indeed, we believe that acquisitions must also bring complementary capabilities (such as new expertise in specific product lines, increased geographical reach or new distribution models) in order to create a sustainable platform for future growth.

Assess your options

— What capabilities (products, distribution channels, technologies, etc.) do you need in order to meet your strategic aspirations?

— What assets are currently available to help bridge any gaps in your capability needs?

— Do you have the alignment and appetite for making the required investments or partnerships?

— Do you have a plan or strategy for integrating these assets to drive growth?

GROW: Responding to a changing environment

New technologies, changing customer demands, new ways of doing business and the threat of innovators disrupting the traditional business model are all changing the way that insurers view their portfolio of assets and businesses.

Clearly, understanding and capturing the benefits of innovation is a critical imperative and there are major opportunities available for companies willing to invest in new technologies. Recognizing this, many insurers are now starting to develop new models and ways of working with the Financial Technology (FinTech) community.

Interestingly, our experience suggests that — in this rapidly evolving space — outright acquisition may not always be the right answer. As our recent report, The Power of Alliances, by KPMG International demonstrates, many insurers are now exploring the value that could be generated by investing in partnerships, alliances and innovation hubs in order to broaden their exposure to new innovations and technology solutions.

Expect near-term deal activity to be focused on:

— The acquisition of companies that offer complementary capabilities (such as the ability to access customer segments in a user friendly format driven by the customer).

— Partnerships to support and develop innovation (such as incubators and innovation hubs).

— Partnerships that create infrastructure to reduce the protection gap.

— Joint ventures and alliances that bring together complementary skillsets (such as behavioral analytics capabilities to support sales and product development).

Key takeaway: Be bold

Regardless of whether the decision is to 'grow' or 'go', insurers need to start facing up to the difficult decisions that must be made about their underperforming assets.

Simply put, insurers can no longer afford to sit on businesses that are not delivering value; they must make bold and decisive decisions and then execute on them in order to win in this environment.

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How KPMG can help

Around the world, our global network of insurance professionals work with many of the leading insurance groups to plan, execute and implement their growth strategies through a broad range of services.

Our initial process is built around a strategy stress test, which provides insurance executives with a review of the achievability of their ambitions based on market conditions, taking into account the changing regulatory agenda and any profit pool and growth analysis and operational considerations that may impede or accelerate your ability to execute.

Our dedicated Insurance Deal Advisory team encompasses strategy, market entry, M&A, due diligence, restructuring, valuations and integration and separation related support operating in all of the key global markets.

Our team can help you:

- achieve corporate growth, realize synergy potential and profit objectives
- create and execute on a well-developed growth strategy
- release capital and enhance liquidity from sale of core or non-core businesses
- restructure or wind down of non-core businesses
- implement an optimal separation plan
- identify international business portfolios and new opportunities
- identify a wide pool of potential opportunities in your core markets
- understand value drivers, opportunities and risks related to potential acquisition targets
- design and execute an effective post-deal integration.

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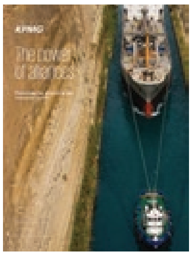
Recent publications



Power of Alliances
November 2015

This report focuses on three main areas of partnership where insurers have been particularly active: bancassurance, Financial Technology (FinTech) and innovative distribution. The report provides actionable insights and lessons to help you create more sustainable and value-driven partnerships and alliances.

Demystifying the Public Private Partnership Paradigm: The nexus between insurance, sustainability and growth
June 2015

Insurers are increasingly coming together with the world's political, development, and policy leaders to help respond to many of the world's most pressing challenges such as climate change, disaster resilience, saving for retirement and economic stability. In this report we explore catalysts to creating new and innovative partnerships that are addressing these challenges and will fill the protection gap.

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Designed by Evalueserve.
Publication name: Grow or go: Taking a portfolio approach to growth
Publication number: 133105-G
Publication date: March 2016