2024 Canadian Insurance Outlook

Charting the future course of the Canadian insurance sector

Building a better working world

Executive summary

Insurers face a critical crossroads. While they've made significant strides in navigating the turbulent regulatory and economic environment in recent years, they're confronting continued uncertainty.

The proliferation of advanced technologies such as artificial intelligence (AI), evolving customer demands and emerging risks are reshaping the industry. Adapting to the evolving regulatory landscape alone, including the implementation of IFRS 17, Insurance contracts, has been a monumental undertaking across the industry. While it didn't hold insurers back from functioning, implementation certainly moved other priorities to the back burner. Now these complexities are reemerging.

To name a few?

- Legacy modernization and cloud migration
- Environmental, social and governance (ESG) priorities
- Product innovation
- Service enhancements
- Digital transformation

With most of the implementation efforts of the new financial reporting standards behind us, the industry is now striving to ensure stakeholders understand the results and consider whether any changes are needed to make the comparisons more meaningful.

But the broader operating environment isn't static. Everywhere we look, emerging risks — and attractive opportunities — abound. Insurers must now shift their focus or risk falling behind their peers, new market entrants and industry disruptors.

In this year's Canadian Insurance Outlook, we focus on pivotal topics that are defining the strategic discussions across property and casualty (P&C) and life and health (L&H) insurers. These strategic focus areas are evolving against a backdrop of continued economic uncertainty. The spotlight this year is on how insurers are differentiating themselves through societal value creation; the indispensable role of data, analytics and AI; and how insurers can capitalize on strengths to drive profitable, near-term growth.

How is the insurance industry changing?

Canadian insurers are contending with a barrage of evolving customer demands, technological disruptions, an increasing regulatory burden and other emerging risks. Below we pain t a picture of just some of the risks that are shaping the industry's future:

01.

Evolving customer expectations

02.

Technological advancements

03.

Regulatory reforms

04.

Emerging risks

01.

EVOLVING CUSTOMER EXPECTATIONS

- Customers are demanding personalized insurance products and services, including savings and life products, tailored to their unique needs and preferences. Given the challenges posed by increasing mortgage rates, Gen X customers are particularly focused on life insurance as a means of financial protection for their families in the event of unexpected circumstances.
- There's an increasing desire for transparency and accessibility, with customers seeking online self-service options and digital platforms for policy management and claims processing.
- We're seeing shifts towards usage-based insurance models and on-demand coverage, driven by a desire for flexibility, affordability and customized solutions.

02.

TECHNOLOGICAL ADVANCEMENTS

- Rapid advancements in data analytics are enabling insurers to better understand customer behaviours, enhance risk assessment, and personalize products and pricing.
- Integration of artificial intelligence and machine learning algorithms in underwriting, claims management and customer service are leading to improved efficiency and accuracy.
- Use of digital platforms, including mobile apps and online portals, are enhancing customer experiences, streamlining processes and facilitating faster claims settlement.
- Cloud migration is enhancing insurer agility, scalability and cost effectiveness, enabling rapid service deployment, improving disaster recovery and reducing hardware costs. Keep in mind: this comes with a significant investment and upfront cost. A significant challenge persists in the form of legacy systems, which might be more pervasive in life insurance than P&C.

03.

REGULATORY REFORMS

Canada's insurance industry is taking on a heavier burden of regulatory reforms and requirements. These include a myriad of guidelines and requirements set up by the Office of the Superintendent of Financial Institutions (OSFI) around:

- Guidelines for assurance on capital to promote reliability and transparency in capital calculations, financial stability and risk management
- Climate risk guidelines aimed at addressing the potential impacts of climate change on insurers
- Culture and conduct guidelines to promote ethical practices and consumer protection
- Third-party risk management standards to ensure effective oversight of outsourcing arrangements
- Cybersecurity measures to safeguard sensitive information

These regulations necessitate increased compliance obligations and reporting standards, as well as investments in technology, resources and expertise to uphold regulatory compliance and mitigate operational and financial risks.

Additionally, regulatory changes aimed at promoting consumer protection, data privacy and transparency necessitate increased compliance measures and operational adjustments.

At the same time, potential changes in insurance distribution regulations to allow for new market entrants, alternative distribution channels and innovation in sales and service models are looming.

That's to say nothing of the evolving tax landscape insurers face in Canada today. Several significant legislative changes have been introduced, including a global minimum tax requirement set at 15% for large multinational enterprise (MNE) groups, a digital services tax (DST), excessive interest and financing expenses limitation rules (EIFEL), enhanced mandatory disclosure rules and denial of dividend-received deductions for financial institutions, including insurers.

These changes come alongside an increasing number of tax audits in the insurance sector.

Put simply: tax regulatory and policy changes are happening at record speed, challenging insurers' tax departments to keep pace and pushing businesses to reexamine operating models across the entire enterprise, including the tax and finance functions.

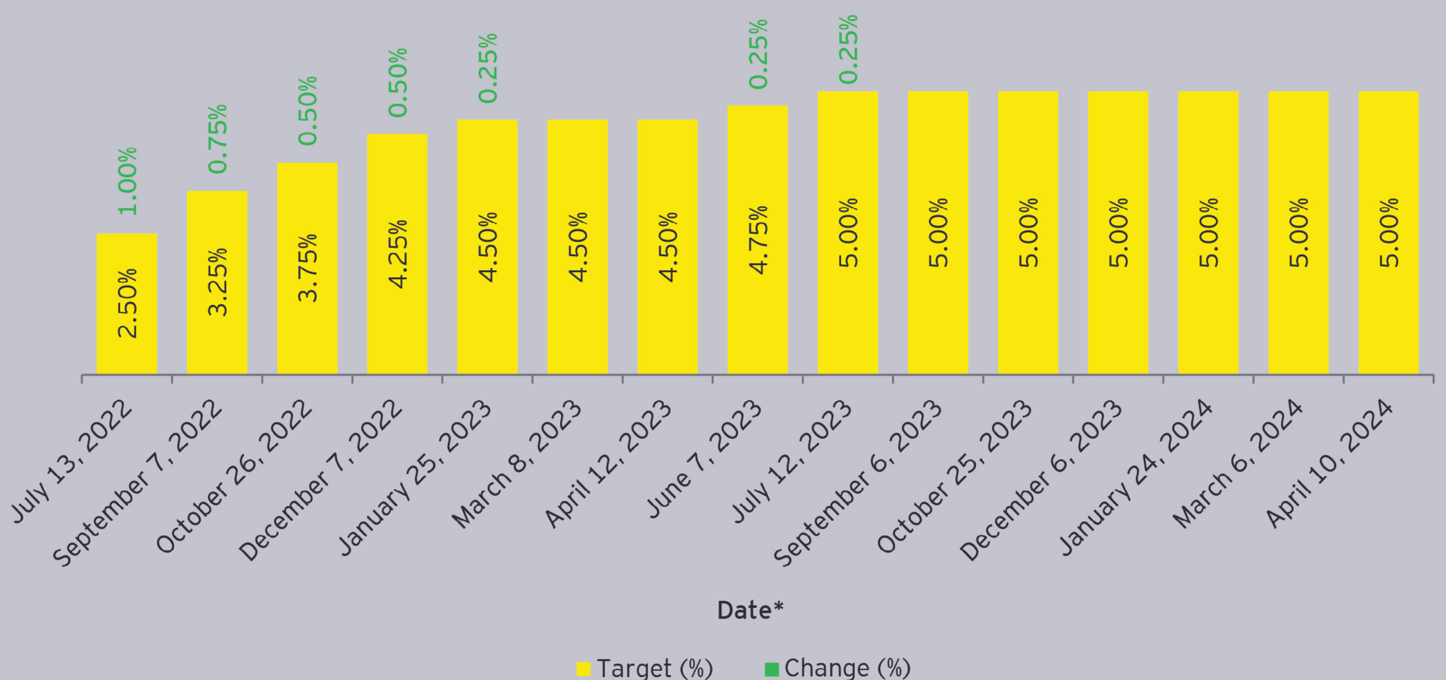
04.

EMERGING RISKS

- Growing "protection gap" challenges reflect a perfect storm brewing, in which supply-side constrictions driven by underwriting and pricing challenges are leaving more people uninsured or underinsured for their needs.
- Demographic shifts demand innovative solutions for life and health insurers.
- Inflation-driven increases in claim costs – and regulators turning down rate increases in certain provinces – are creating a strategic dilemma over whether to pass along rate hikes to customers or scale back increases.
- Geopolitical uncertainty and its downstream impacts to the Canadian market are affecting global supply chains and have led to persistently high costs for insurers.
- Intensifying climate-related events are leading to increased claims costs.
- Cybersecurity threats now require pioneering coverage solutions and risk management strategies.
- Evolving liability risks from new technologies require proactive development of insurance products.
- Upticks in car theft pose significant new threats to personal and commercial auto insurers.

Snapshot of selected economic and demographic trends impacting the Canadian insurance industry

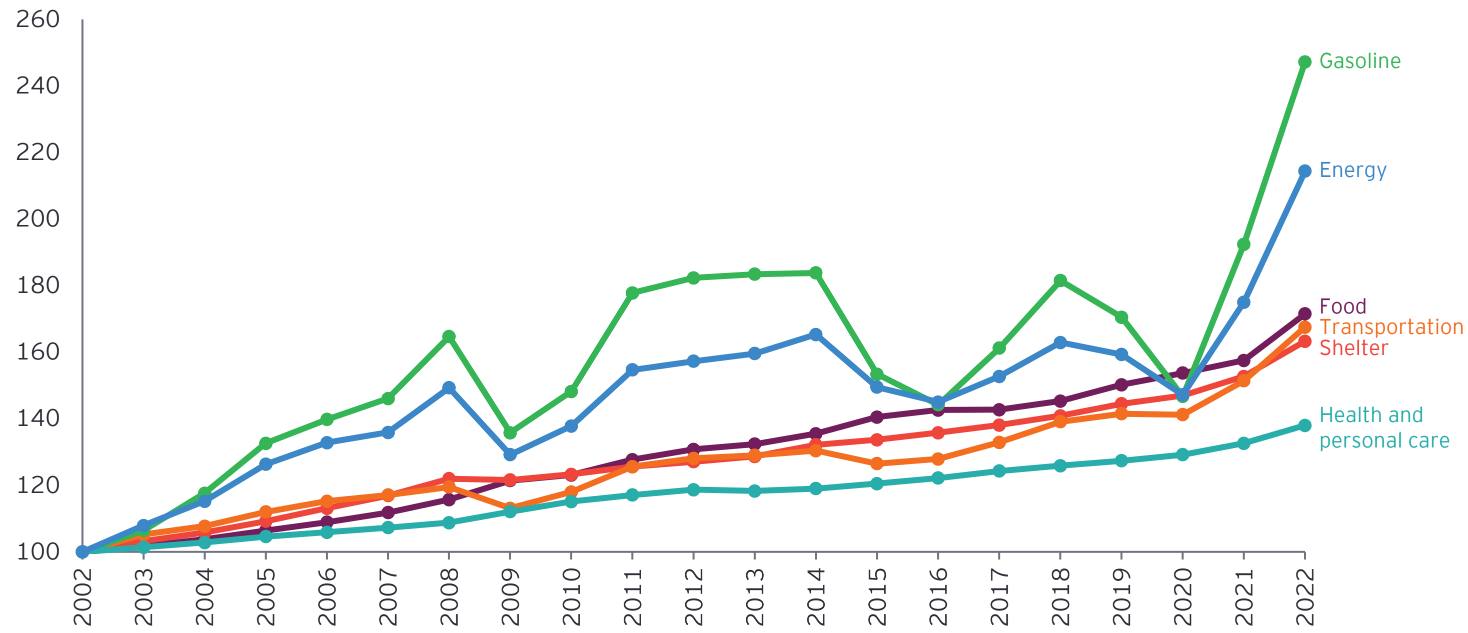
Bank of Canada policy interest rate



Source: Policy interest rate - Bank of Canada

Consumer price index

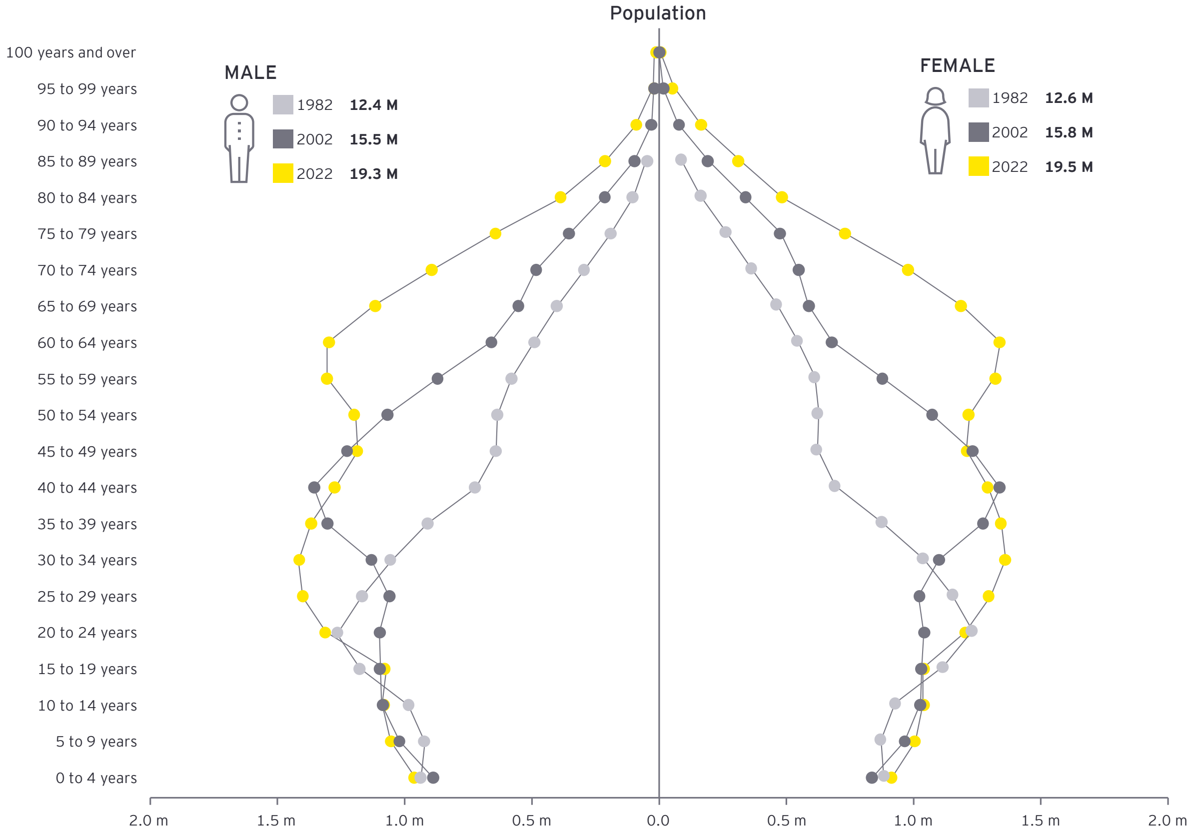
2002=100



Source: Statistics Canada. Table 18-10-0005-01 Consumer Price Index, annual average, not seasonally adjusted. https://www150.statcan.gc.ca/t1/tbl1/en/tv.action?pid=1810000501

Population estimates

Total Population	1982	2002	2022
	25,116,942 (25.1 M)	**31,360,079** (31.3 M)	**38,929,902** (38.9 M)



Source: https://www150.statcan.gc.ca/t1/tbl1/en/tv.action?pid=1710000501

Motor vehicle theft - 2021-22

(26.7% increase year over year)

In 2021

83,416

Automobile Theft

In 2022

105,673

Automobile Theft

Source: Police-reported crime for selected offences, Canada, 2021 and 2022 (statcan.gc.ca)

As seen above, Canadian insurers are juggling an environment that's changing rapidly and defined by a heavier regulatory burden. But keep in mind: alongside risk comes opportunity.

CHAPTER

01.

Societal value creation has become a key differentiator for insurers

The insurance industry finds itself in a promising position to enhance societal value, catalyzed by regulatory pressures and the emerging emphasis on ESG considerations. How so? The IFRS 17 reporting guidelines offer insurance companies an opportunity to reassess their financial transparency and risk mitigation strategies, in turn driving greater financial resilience. This holistic approach to economic value promotes better-informed decision-making, boosts resilience in the face of growing market uncertainties and ultimately benefits society by generating trust and confidence among stakeholders.

Moreover, integrating ESG considerations about insurance offerings resonates with the growing consumer trend towards sustainable consumption. This positions insurers to create innovative, socially responsible products that align with societal values and contribute to resilience in the face of emerging risks.

How are insurers looking to prioritize enhanced financial transparency, implement more detailed ESG reporting and prepare for the future of work?

Regulatory pressures are driving emerging opportunities for enhanced financial transparency, strengthening risk assessment and mitigation and making insurers more financially resilient.

IFRS 17 opens the door to increased transparency and better-aligned KPIs

The insurance industry relies on KPIs to tell its performance story. This doesn't change with the adoption of IFRS 17. However, the standard, and the significant enhancements to systems and data it triggered, impacted both GAAP and non-GAAP measures. Whether due to data source changes, refined definitions with increased granularity or the availability of equivalent GAAP measures, a cursory review of investor education presentations and new MD&A disclosures is telling of the changes and the new information now available:

Therein lies the opportunity.

The new required financial disclosures create opportunities to gain a deeper understanding of insurers' inherent economic value, profitability and risk profile. Through benchmarking over time, insurers' disclosures are poised to become more aligned and comparable, which could reduce the cost of disclosure, enhance differentiation and help stakeholders make better-informed decisions.

Redefined operating profit, combined ratio, return on equity and the new business contractual service margin metrics bring new potential for insurers to tell their performance story and become primary tools for stronger business decision-making and guidance. For example:

More granular disclosures and understanding of business profitability.

Enhanced visibility into new business value: While the life and health insurance sector has historically used non-GAAP new business value metrics, IFRS 17 introduces an alternative in the form of the new business contractual service margin.

Consistent definition of insurance revenue: IFRS 17 establishes a uniform definition of insurance revenue across insurers, ensuring comparability and facilitating benchmarking.

Insights into changes in service profit emergence: Disclosures of experience changes offer valuable insights into what causes the differences between expected and actual insurance results.

Redefined operating profit: what changed?

The new financial reporting requirements, and the accounting choices made, have prompted insurers to adjust their definition of operating profit, resulting in varying impacts across insurers. Insurers use adjustments to exclude the impact of certain factors from net profit to derive the operating profit metric. In many cases, refinements of pure accounting impacts provided a more balanced view of changes after IFRS 17 adoption.

Revamping combined ratio and return on equity: what changed?

The combined ratio remains a widely reported KPI for P&C insurers. While variations continue to exist in how insurers calculate combined ratios, we noted a relatively consistent way to adjust for IFRS 17 changes to underlying losses and general expenses.

The one-time impact of IFRS 17 implementation affected the insurers' shareholders' equity, either negatively or positively, depending on the type of insurance business and therefore the measurement model, expense deferral choices, durations of assets and liabilities, and the reinvestment yield cycle impac). As a result, insurers introduced further definitional adjustments to maintain long duration comparability or modified targets to account for the changed basis.

Going forward, mechanisms such as the contractual service margin are expected to reduce fluctuations period to period, as deferring profit recognition helps absorb impacts related to future services, mitigating their effects on equity through the systematic release to profit and loss.

The introduction of IFRS 17 creates opportunities to gain a deeper understanding of a company's inherent economic value. It does so by considering factors like the organization's specific value proposition and sustainable profitability. Also, it includes a unique aspect of company-specific risk tolerance. Ultimately, this new framework allows organizations to gain valuable insights into their financial position, ensuring a more accurate understanding of their own underlying value. This offers a better understanding of the company's fundamental worth and helps stakeholders make informed decisions based on a comprehensive understanding of profitability, risk and a company's unique risk appetite.

ESG offers insurers a chance to differentiate themselves in a crowded marketplace.

The global business landscape is witnessing a seismic shift in light of the fast-paced transformations reshaping the environment. Case in point: ESG factors have emerged as critical drivers of sustainable success.

Today, companies are facing mounting pressure from stakeholders — including investors, customers and regulators — not only to assess and manage ESG risks and opportunities, but also to transparently disclose their sustainability performance.

Canadian organizations are incorporating material ESG issues into reporting frameworks and aligning disclosure practices with internationally recognized standards, including the International Sustainability Standards Board at the global level, as the Canadian Securities Administrators carry out consultations on standard adoption.

Being a key player in risk management, the insurance industry is no exception. As a response to this growing movement, the Office of the Superintendent of Financial Institutions (OSFI) introduced Guideline B-15 on climate risk management in March 2023, solidifying Canada's commitment to ESG integration in the insurance sector. Guideline B-15 will be effective fiscal year end 2024 for domestic systemically important banks and internationally active insurance groups headquartered in Canada, and effective fiscal year end 2025 for all other in-scope federally regulated financial institutions (FRFIs).

In developing Guideline B-15, OSFI recognized that climate change poses numerous threats to the safety and soundness of institutions and the financial system more broadly. OSFI expects such climate-related risks to diversify and intensify over time, drive other financial risks such as credit, market, insurance and liquidity risks, and lead to strategic, operational and reputational risks for institutions. Such risks could even potentially threaten the long-term viability of an institution's business model.

OSFI Guideline B-15 serves as a regulatory framework for insurers to effectively assess, manage and disclose climate-related risks. It requires both life and P&C insurers to develop comprehensive strategies for identifying, assessing and mitigating climate-related risks. In addition, the guideline provides a principles-based approach to disclosing relevant, consistent and verifiable information.

For life insurers, B-15 encourages the evaluation of potential climate impacts on policyholder behaviour, mortality and morbidity rates, as well as investment and product sustainability. P&C insurers, on the other hand, are expected to consider the rise in frequency and severity of weather-related events and adapt their underwriting, pricing and claims management practices accordingly.

Now is the time to double down on governance frameworks and start building future-focused reporting structures that will enable carriers with the processes and people in place to effectively comply — even as those ultimate requirements continue to evolve.

Furthermore, integrating ESG considerations into product development and underwriting decision-making not only aligns with ethical and sustainable principles, it also presents an opportunity to create innovative, socially responsible insurance products that resonate with consumers and contribute to long-term resilience in the face of emerging risks.

Doing so now is a chance to build for the future and differentiate the business in the eyes of stakeholders, including choosier customers who are now more apt to make buying decisions based on sustainability factors.

Workforce readiness investments can fuel sustainable success.

With evolving customer expectations and mounting pressure to maximize operational efficiency in a complex global operating environment, the insurance industry faces an urgent need to adapt and innovate. These dynamic forces are reshaping the foundations of value creation and charting a new course for the future of work.

Business capabilities are evolving in response to these market forces. Workforce roles, skills and ways of working need to shift in turn. As digital self-service and intelligent automation impact many processes across the insurance value chain, we expect to see operational efficiencies in the core insurance competencies of underwriting and claims in the medium term.

However, over the last two years, underwriting vacancies have held constant and there has been a material increase in claims recruitment. We believe increased turnover post-pandemic, service level challenges and claims backlogs linked to cyclical and structural pressures that reveal stark and persistent differences between employer and employee priorities may be drivers of this scenario.

This inflection point is a meaningful opportunity for insurers to ensure their workforce is future ready in light of these changing realities. How so? The long-hypothesized shift to direct distribution in personal lines has yet to materially impact the Canadian market, with carriers continuing to distribute far more through intermediaries than in other mature markets. In fact, conversely, the highest number of insurance vacancies in the last two years have been in sales roles across both P&C and life and health.

Insurers are taking a number of key steps to elevate their workforce readiness in the face of these trends, including:

PRODUCTIVITY

Insurers are reviewing the efficiency and effectiveness of current operations and looking to optimize roles and processes, and capture benefits from technology investments.

CULTURE

While most Canadian insurers have landed on a hybrid work model, most have not yet reached a stable and mature stage. It is vital to be clear and specific on the desired culture in the organization and have a robust understanding of where behaviours and ways of working are currently supporting or hindering that desired culture. Taking a strategic, culture-first approach may influence the ultimate work model insurers settle on in the medium term.

ORGANIZATIONAL DESIGN

Many carriers are evaluating their organizational designs to right-size and future-proof structures and roles. Capabilities such as digital, transformation, data and analytics are particularly in the spotlight, both in terms of the capability required and the way that capability is delivered, such as centralized, hub and spoke or decentralized.

TALENT, LEARNING AND DEVELOPMENT

With an aging insurance workforce, decreasing interest in the industry among younger talent and competition for transversal skills with other sectors, the talent agenda has never been more important. Insurers are considering how they can acquire, retain and develop talent in a more agile and effective way. To achieve this, insurers are considering the capabilities required in HR and learning and development teams, and looking to future-proof these functions.

Demand for technology, digital and analytical roles has been steadily increasing, with some mature insurers exploring global talent pools to fill scarce roles. From the skills perspective, customer experience, data, analytics, artificial intelligence (AI), transformation and cybersecurity are increasingly infused into many roles across the insurance value chain, not just specialist roles.

Insurers are focusing on climate risk, loss prevention and education as key capabilities and an important part of the role carriers play to support the communities they serve. Future-proofing the workforce in the face of these trends will require insurers to review productivity, strengthen culture, rethink organizational design and double down on talent, learning and development.

How can insurers take action now?

- Substantially increase your leaders' understanding of IFRS 17 understanding and conduct deep dives on how the new world metrics will influence profitability actions and business decisions.
- Review current enterprise-wide ESG reporting and build future-focused reporting structures to effectively comply with the evolving standards.
- Develop a robust future state view of the organization, roles and skills required, informed by business strategy and market trends. In conjunction, assess the current workforce from a capacity, capability and demographics (e.g., proximity to retirement) perspective to understand likely talent gaps, and create a workforce and talent plan to proactively address talent gaps.

CHAPTER

02.

The imperative role of data, analytics and AI

With the emergence of generative artificial intelligence (gen AI), and with data and analytics increasingly becoming table stakes, insurers have made significant investments to maintain their competitiveness and growth trajectory. AI is no longer a "nice to have" to compete in a hyperconnected world; it's the backbone of modern business as it fosters better decision-making.

To start with, a long-term data strategy can allow insurers to consolidate disparate data sources, fostering trust in decision-making and enabling personalized services through data analysis. Effective integration with existing data platforms can optimize operations, enhance agility and foster scalability. Gen AI can then further elevate the operational efficiency, customer experience and employee engagement across the insurance lifecycle.

Use cases for AI are continuing with tremendous potential benefits. For insurers, customers and intermediaries, it can elevate operational efficiency, reduce claims costs and elevate the user experience.

In this chapter, we'll discuss how the industry is employing data, analytics and gen AI, including specific use cases, with a spotlight on finance transformation.

Make data, analytics and AI the organization's backbone

Similar to data, AI is no longer just nice to have to compete in a hyperconnected world. It's the backbone of modern business as it fosters better decision-making and open ecosystems to unlock collaboration with key partners. Having a solid data foundation is now an essential prerequisite to effectively unleash the power of AI. Potential use cases abound.

What do those implications look like in practice?

Data strategy	Advanced analytics and AI	Cloud integrations	Early value extraction from GenAI	ESG focus
Done right, long-term data strategies enable insurers to rationalize siloed and disparate data sources to envision a single source of truth, while building trust and confidence in their decision-making.	By analyzing the data, insurers can make better and more informed decisions tailored towards their customers' real sentiments and needs.	Integrating existing data platforms and warehouses to employ existing data capabilities and support new capabilities can help optimize the cost of operations, enhance operational agility, and foster long-term scalability.	Connecting gen AI capabilities with claims/policy processing platforms supports core operations and provides indicative benefits.	ESG provides insurers an avenue to chart new and unique products that offer better rates and accessibility.

What does that look like from the insurance perspective?

- AI-powered fraud-detection systems can address the shortcomings of earlier applications and can help augment human analysts' judgments by supplying them with valuable intel.
- It can accelerate claims processing by taking over some of the heavy-duty manual work and often downright dangerous inspection tasks.
- AI-based intelligent interactive voice response (IVR) solutions can help customers get their queries answered instead of being in queue to get hold of live agents.
- Connected vehicles now produce, store and transmit terabytes of valuable data that insurers can use for better actuarial analysis or pivot to new business models based on consumer demands.
- Rapid document digitization with optical character recognition (OCR) can help insurers transition from paper-based forms and printed documents and improve operational efficiencies.
- Embedding AI and intelligent automation in monotonous, detail-oriented, accuracy-demanding workflows can help streamline claims processing.

Balancing the benefits and risks of AI will also be important for insurers as they create strong governance structures around responsible AI use. Risks include data security and privacy, bias in the system, cybercrime and accuracy of output.

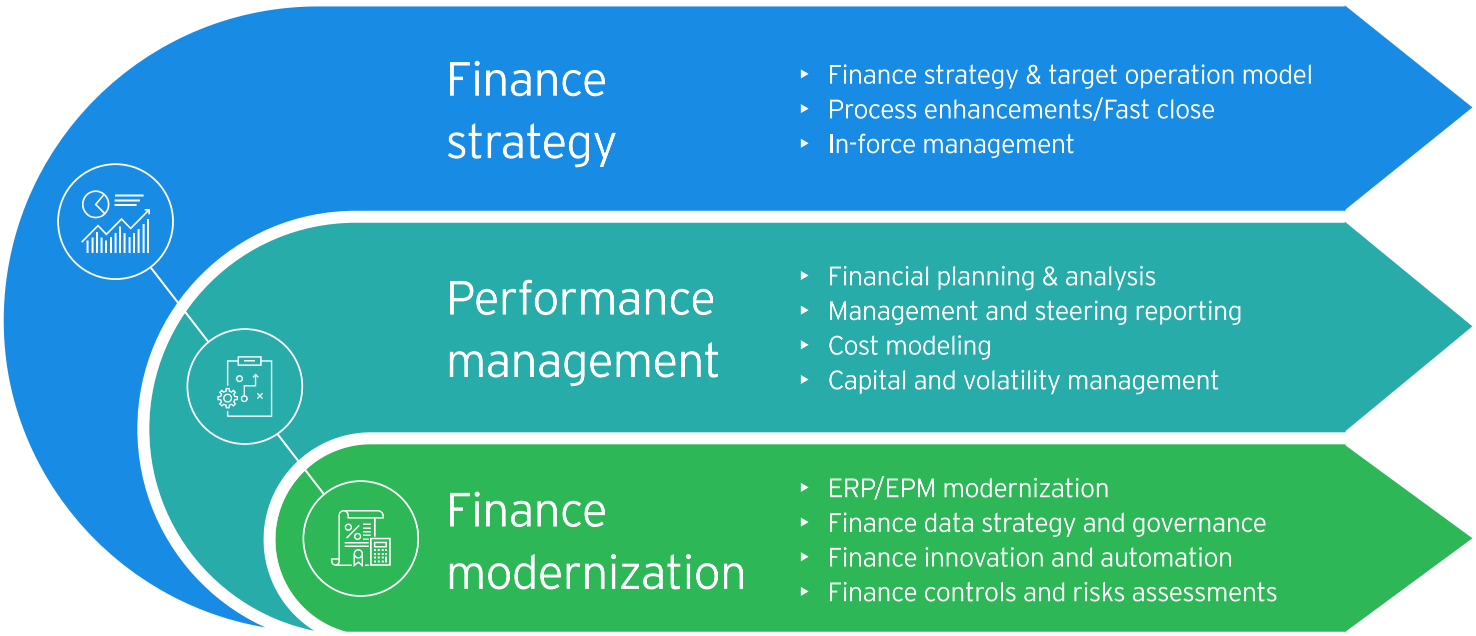
Spotlight on finance transformation as a strategic imperative

On the theme of viewing data as a strategic enabler, CFOs have long been proponents of the more forward-looking strategic impact of a finance function of the future. The monumental effort of implementation of IFRS 17 has further highlighted the inefficiencies and lack of real impact of finance operations in the sector. That makes rethinking finance transformation critical to strategically supporting the sector's digital shift and emerging challenges.

Embarking on a finance transformation journey requires tailoring the approach to address each insurance organization's specific challenges and goals. In the past, it was difficult to make a strong business case for finance change against competing priorities. However, the urgency for change is intensifying, shifting from optional to business critical. A mere tweak to reengineer core finance operations is insufficient; a new strategic intent must be pursued to fully unleash finance's potential to be a strategic advisor for long-term growth.

It's imperative to renew the building blocks of the finance organization to enhance finance's role as a business partner. This includes modernizing the technology and ecosystem to not only accelerate the processes, but also to optimize the workforce model and unleash the real power of data.

One prevalent example is the emphasis on a smarter and faster financial close process and the link to high-quality data as a foundational building block. Additionally, linking AI to the finance transformation agenda will enable insurers to fully exploit the benefits of predictive analytics and enable faster, smarter decision-making.



How can insurers take action now?

- Start viewing data as a strategic enabler of the long-term business strategy. Gone are the days of positioning data as a byproduct or a means to an end.
- Embark on a transformation journey with intention. This isn't about layering in new technology here and there. It's about rethinking the way you work overall.
- Drive a mindset and culture shift that seeks to weave digital and a spirit of innovation across the business. Enable people with the tools, resources, time and — critically — permission to test and try .
- Align finance operations with organizational goals to unleash long-term success and foster resilience in an ever-changing landscape.
- Consider finance transformation beyond a one-time project. Ground this effort in finance strategy, performance management and finance modernization.
- Embed digitization, automation and data-driven decision-making at the core of your finance transformation to unleash its full potential, while keeping the business safe.

CHAPTER

03.

Profitability under pressure: insights into the insurance sector's cost optimization and growth opportunities

As profitability pressures mount in the insurance industry, cost transformation has been elevated to the top of C-suite agenda. Many insurers have already identified key levers and benefits and are beginning to focus on a comprehensive implementation and benefits realization strategy.

Successful cost transformations anchor on the organization's mission, values and strategy, and can be used to both improve profitability and fund initiatives to help build future strategic capabilities.

Evolving customer behaviours and disruptive technology trends present both a threat and an opportunity for the industry. Insurers are exploring both organic and inorganic means to defend and grow market share, including expansion across customer segments, products, coverages and distribution channels, as well as more vertical integration and partnerships. Post-pandemic there has been a resurgence of M&A activity, with a shift in focus from adding scale to improving profit margins and seeking revenue diversification.

In an increasingly consolidated market, carriers are exploring beyond traditional insurance services, with significant transaction activity in the insurance distribution landscape. Potential ESG performance factors and digital transformation imperatives are also key in potential acquisitions, further shaping the M&A decision-making process.

In this chapter, we will explore how insurers are doubling down on strategic cost optimization as well as exploring inorganic growth opportunities.

Improving the cost base to reinvest in growth and innovation

Insurers' long-term focus on transforming business models has accelerated to a near-term focus on efficiency and effectiveness due to profitability pressures. When considering cost, insurers have traditionally focused on a bottom-up approach, addressing tactical drivers of cost.

This approach risks diminishing returns if focused purely on tactical levers repeated over time (e.g., reducing headcount and discretionary spend) without more strategic consideration for optimization.

Taking a more top-down approach to address the strategic drivers of costs, considering client segments, products and services, geographical presence, distribution channels and strategic operating model design is more difficult, but is likely to create more sustainable results.

Cost transformations may have a variety of cost objectives and time horizons. Insurers should be clear on which of the following cost objectives they're looking to address, as each objective will influence the design of the cost transformation roadmap.

We view cost levers through three distinct layers: strategic, structural and operational. Successful cost transformations typically assess the business across these three layers to identify a balanced portfolio of change from strategic to more structural and immediate operational efficiencies.

More strategic levers require investment and longer timeframes for return on investment, though typically they create more sustainable benefits. However, they may not achieve the more immediate efficiency targets that operational levers deliver. Considering which levers to pull in a structured way, balancing strategic and tactical solutions, will help reduce risk and increase sustainability.

Historically, many programs have failed to deliver on benefits that have been identified. High-quality implementation and benefits realization requires significant executive alignment, sponsorship and commitment, combined with an empowered program management office to report and challenge the achieved benefits from each initiative. This requires mitigation of the risk of costs creeping back up once the focus has moved elsewhere, working in partnership with finance to lock benefits achieved into budgets and forecasts.

Post-pandemic M&A activity renews pathways to growth

The Canadian insurance market is constantly evolving, as industry participants navigate changes in the regulatory environment, evolving customer needs, and the opportunities and threats of disruptive technologies .

The key players in the sector continue to seek maximum returns on capital while taking advantage of opportunities for growth through inorganic – and increasingly organic – channels.

The uncertainty of the pandemic has subsided, and we have seen M&A activity return to more typical levels in all subsectors.

In the core life insurance and P&C insurance categories, the large Canadian carriers are focused on adding scale, improving profitability margins and seeking diversification of revenue streams. For these subsectors, market consolidation is generally more mature, which has limited the number of large-scale M&A deals in recent years. The focus has been on opportunistic acquisition opportunities, bolt-on transactions and horizontal integration. This activity has started to push the carriers outside of traditional insurance services, which can give rise to new customer and revenue opportunities.

The largest pocket of M&A activity in the Canadian marketplace is in the insurance distribution landscape. In recent years, we've seen an unprecedented level of transaction activity with P&C insurance brokers and managing general agencies (MGAs), as well as life MGAs and third-party administrators.

The fragmented market is primarily composed of small- and medium-scale businesses, with many owners facing retirement and succession challenges, which has been a factor in the rise in transaction activity.

Also fuelling the activity level has been the rise of private equity (PE) capital injected into the space through the efforts of several large consolidators. These consolidators are executing rollup acquisition strategies, attracted by the cashflow profile and growth opportunities in the insurance distribution market.

In addition to the traditional approaches to expansion, there is a notable trend of vertical integration and embedded insurance at the point of sale, and this is likely to continue to grow. Embedded insurance, in which insurance is intuitively incorporated into the purchase of a product or service, offers a new avenue for growth by augmenting the customer experience and increasing the convenience factor.

At the same time, vertical integration is reshaping the industry as insurance companies expand into non-traditional services. A life insurer's investment in medical clinics is a salient example of this. By integrating health care services, life insurers can create a partnership between insurance and health care, which not only diversifies their portfolio but also provides a more holistic service to clients. Such innovative moves on the insurance value chain reflect the industry's willingness to break from convention and explore new opportunities for growth and customer engagement.

We expect this market momentum to continue into 2024 and beyond. However, higher interest rates could potentially soften investment activity while the cost of capital remains elevated.

There is also a growing focus on digital transformation and technological integration, with insurers actively engaging in M&A to acquire technology-driven firms. Target firms are being assessed from a dual perspective, encompassing both prospects and obstacles:

Prospects include their ability to enhance operational efficiency, foster innovation, and improve customer experiences through advanced digital platforms, artificial intelligence and data analytics.

Obstacles include assessing the target firm's sophistication in IT infrastructure and risk management processes to safeguard extensive customer data — such as data encryption and multi-factor authentication — as well as the financial commitment required to attain IT modernization and integration objectives.

Companies are also increasingly assessing ESG factors and integrating sustainability goals into their M&A decision-making processes. This includes evaluating potential targets based on their ESG performance and aligning business objectives with sustainable practices. This will remain top of mind for several years to come.

How can insurers take action now?

- Use cost transformation levers in new ways. Many of the levers are not new but need to be used in new ways across the value chain and with a broader ecosystem of providers.
- Apply cost programs further up and down the value chain beyond traditional uses to address operational functions.
- Consider outsourcing activities to non-traditional players such as reg-techs and professional services firms.
- Consider using FinTechs in technology architecture (i.e., intelligent technologies).

Summary

The confluence of regulatory pressures, shifts in the future of work, the growing importance of ESG considerations and the adoption of new performance management standards is shaping the Canadian industry in unprecedented ways. Now's the time for a proactive and adaptive response.

Reflecting on the previous decade, the industry has faced an onslaught of market forces and changing external and internal dynamics that have influenced the business landscape. This underscores the increasing importance of being proactive and staying ahead of the curve as the new normal for insurers.

The Canadian insurance sector has the potential to harness these challenges as opportunities for growth, resilience and sustainability. Embracing these shifts and adopting a forward-thinking approach can help secure a brighter, sustainable future for insurers and the communities they serve.

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