



Critical Challenges Facing CEOs Today

Mr Patrick Kenny, President and CEO of the International Insurance Society, posits that if there was a ranking of CEO challenges for 2005, regulation would be near or at the top of the list, and that it is possible 2005 will go down as the Year of the Regulator in the insurance industry.

We know that regulatory actions are accelerating because of the globalisation of business and the internationalisation of capital markets. Improving corporate governance has been at the heart of many new regulations in recent years. This has, in turn, created a greater urgency for more standardised reporting systems. International companies seeking additional presence outside their domestic markets have favoured harmonisation of regulatory, accounting and reporting systems. But also, recent scandals have undermined public confidence in financial reporting, and investors, ratings agencies, analysts and regulators have therefore pressed for better standards, stricter corporate governance and greater transparency.

Tightening Regulatory Scrutiny Worldwide

The so-called Spitzer investigations of insurance in the US, begun in 2004 and focused most recently on the international brokerage community, are continuing in 2005. This regulatory scrutiny has brought substantive change within the industry in many sectors.

Also, the US Securities and Exchange Commission is extending its inquiries into insurance, and the National Association of Insurance Commissioners (NAIC) and insurance trade associations are smack in the middle of the hot issue of brokers' compensation. Even more important is the future of state versus federal control of the industry. Advocates of a federal system of insurance regulation in the US say the current state-based regulation is weak and in need of reform.

In the UK, wider powers given to the Financial Services Authority (FSA) over the general retail and London Market sectors were introduced in January 2005, with any company selling or advising on the sale of insurance needing the FSA's authorisation. Also, life and pensions sectors there have been under pressure to improve transparency and capital requirements. The UK actuarial profession has been the subject of a critical Treasury Report.

The powers of regulators have also increased in Europe, as new European accounting requirements are introduced. From the beginning of 2005, all listed insurers in the EU will be required to comply with the International Financial Reporting Standards (IFRS). Together with the US's GAAP standards, these are forming a basis for international alignment and transparency within the insurance industry.

On the other side of the world in Asia, China's regulators have recently opened the country in a wider way to foreign insurers while the capital entry threshold for foreign brokers has been halved beginning in 2005. Another developing

insurance market, India, is also looking at ways to encourage greater foreign involvement. Yet, regulatory tightening has also occurred in China, which recently ordered trust firms to report annual results and other data for the first time – enhancing transparency – as a result of investors who complained about the lack of disclosure.

Ratings Agencies Exert Influence

Ratings agencies have also forced change within the industry and influenced the ability of companies to raise capital. Ratings have significance in promoting or detracting from public confidence in companies, and as such are an important concern of CEOs. While the industry understands the important role of ratings agencies, there is also concern that they need to show more consistency and, yes, standardisation and transparency in their own reporting standards for companies. The question still remains: Are the ratings agencies the de facto regulators of the insurance industry?

Danger Of Over-Regulation

Is this new wave of regulation and supervision going to serve the industry well? What can CEOs expect from these changes? On the positive side, standards will increase transparency, which will put all companies on a level field. No one opposes that. But are more rules the enemy of diversity and ingenuity? Will they bring more capital volatility? And what will the impact be on cost? The rules vary for various business segments, life, non-life and reinsurance, and expenses of aligning to the new regulations will be considerable. Companies will need to devote more time to communicating with investors and shareholders.

CEOs Need Keen Sense Of Balance

Those CEOs I meet around the world hold widely differing views of regulatory change and influence in the industry. But regardless of differing cultural or geographic area, CEOs are working hard to balance integrity, accountability and transparency within their organisations. More are making certain that there are truly independent directors on their Boards to keep watch. They seek to recruit and promote people with great integrity and high levels of judgment.

They are mindful of the importance of transparency but also believe that there is a trade-off between meaningful transparency and stifling disclosure. They believe non-performance should be punished and performance criteria should include more than meeting financial targets. Finally, they say that the market itself has powerful corrective forces and

punishes those who fail to ensure credible results.

Other Pressing Issues

Beyond regulatory issues, there are many other important issues that will be challenges for CEOs this year, probably some that will surprise us. Some issues and questions likely to cross the desk of today's chief executive are:

- Will the industry see the need for more mergers and acquisitions?
- What will the impact of branding strength be on business success?
- How will organisations best develop human resources for the global industry?

M&A Activity

In December 2004 alone, a number of mega-deals in the communications, retail and pharmaceutical areas raised questions as to whether a merger boom was in full swing. In the US, Kmart and Sears, Sprint and Nextel, among others, have merged. In December, there was a total of US\$283 billion in mergers and acquisitions worldwide, outpacing the total deal volume during the same period in 1999.

For all of 2004, deals were up nearly 50% over 2003. In February, in the US, the first big insurance deal was the acquisition of Travellers Life business by MetLife, thus signalling the diminishment of the "one-stop" financial supermarket with the Citicorp/Travellers family, and a product-focused emphasis by MetLife.

How will CEOs in insurance respond? It is clear that the industry will reflect on whether potential deals have strong strategic rationale and whether it is going to be better to expand internally or via acquisitions. Many recent mergers failed to achieve what their partners hoped. With new companies continuing to be formed, capital does not seem

to be an issue.

The Value Of Branding

Global branding has been an important topic in the insurance area. While a successful, single global brand can reap powerful benefits for companies across cultures and countries, it is also clear that such brands can suffer when regulatory action is taken against companies and public image tarnished. There is likely to be a continuing debate within the industry between those who believe that one brand can build success around the globe, and others who believe that local and regional branding is more effective and meaningful.

Investment In HR

CEOs I know place top priority on investing in talented people. This means recruiting and training people with technical skills but also those who know languages and cultures – so necessary in a global world. The demands of today's global environment make entrepreneurial skills that adapt around the world a necessity.

It is clear that as insurance managers we need to not only analyse key trends, like regulatory and ratings changes, but we need to collectively and proactively manage the insurance cycle better and put our own house in order. This will deliver logical pricing, structure and stability, and will more likely yield consistent, stronger financial performance for the shareholder. Such proactive goals will allow insurers to plan more confidently for the future, and allow the industry to improve its ability to work with consumers, regulators and ratings agencies alike. ■

The International Insurance Society will hold its 41st annual seminar in Hong Kong on July 10-13, 2005, at the Grand Hyatt Hong Kong. Do check www.iisonline.org regularly for seminar updates.