



Sri Lanka Insurance Report

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KPMG Sri Lanka

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Introduction

As the pandemic rages on regardless of all the efforts taken by global leaders and health experts, the uncertainty around every aspect of life remains. The insurance industry was quick to respond to the pandemic and introduce digital capabilities that has resulted in a positive outcome for the insurers and bodes well for the future. An increased demand for some life insurance and non-life insurance policies, such as term, mortgage protection and health most likely accounted for the expansion of insurance business during the past year.

The insurance industry in Sri Lanka is a major component of the economy by virtue of the amount of premiums it collected in 2020 of Rs 209 bn, the value of assets on their balance sheets of Rs 796 bn and, more fundamentally, the essential social and economic role it plays by covering personal and business risks.

This KPMG report highlights the insurance market trends locally and globally to support a better understanding of the insurance industry's overall performance and health, supported by the GWP growth of 6% and assets growth of 14% compared to 2019.

We understand that the growth rates in the local market is being sustained in 2021 as well. However, consumer spend is impacted by both the decrease in disposable income and the psychological impact of COVID-19. Consumers in Germany, France and Hong Kong (SAR), China feel more calm and secure, fitting into the financially comfortable category. In Brazil, Japan, Italy and Spain, more consumers have stopped all non-essential purchases and are more selective, feeling more financially overwhelmed and financial recovery being the priority. KPMG research found that value for money, and its corollary price, is the single most important factor in decision-making.

In our view, the top three drivers for new investment in the insurance industry in the minds of local CEOs will be similar to the findings of the 2021 Global CEO outlook by KPMG, which are; Increase market share, On-board new digital technology to transform the customer experience/value proposition and Develop disruptive technologies that have potential to transform their operating model.



Insurers have historically lagged other sectors in their digitization efforts — now, we have reached a watershed moment. It is time for insurance to catch up and re-emerge stronger and better. We believe that investing in capabilities to respond to the seven key macro themes that we believe are particularly relevant to insurers in a fundamental way in order to thrive in the new reality may pay long-term dividends for an insurer.



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A strategy to enhance customer experience through digital transformation initiatives has worked well during the COVID pandemic for this sector. Further investments should help to improve growth and insurance penetration in Sri Lanka.

Insurance penetration in Sri Lanka which is reflected by the insurance premium generated by licensed insurance companies as a percentage of GDP amounted to 1.39% in 2020. Although insurance penetration had slightly increased in 2020 compared to 1.31%, which was recorded in 2019, it is still low compared to other countries in the Asian region and may be misleading due to a drop in GDP in 2020. The industry must also address critical societal need for affordable health care.

A greater awareness of medical insurance benefits due to hospitalizations resulting from COVID19 will lead to an increased demand for insurance products in this area. Insurers have a great opportunity to bridge the gap between coverage from existing policies and out-of-pocket expenditure towards healthcare by the public, through innovation, digitalization, and personalization.

Other challenges such as cyber threats, increasing climate change and sustainability awareness will require insurers to think bigger and differently in the years to come.

There is significant space to grow this business provided insurers shift towards a more holistic, simpler, and personalized solutions with a customer centric product strategy with an easy payment or usage-based model.

This will be attractive to the millennials and Gen Z population and promote protection in our society. COVID-19 might just prove to be the catalyst for innovation in insurance, unlocking greater levels of customer experience and personalization that has long been overdue.

The Insurance industry has faced a monumental challenge throughout this pandemic. KPMG insurance professionals have been reflecting intensively on and widely discussing with clients the nature of the issues and what it means for insurers. The seven macro themes included in this report are relevant to insurers and they must respond to thrive in the new reality. We believe that investing in capabilities to respond to these trends may pay long term dividends for an insurer.

"The greatest danger in times of turbulence is not the turbulence – it is to act with yesterday's logic." – Peter Drucker



Snapshot of Sri Lankan ECONOMY



Inflation

NCPI (Y-Y) 6.80
July 2021



Area

65,610
Sq. Km



Economic Growth

4.3%
Q1, 2021



\$ =

LKR
199.9000
INDICATIVE
July 2021



Unemployment Rate

5.5%
Q4, 2020
July 2021



Interest Rates

T-bill < 364 days 5.08%
T-bond < 3 year 6.86%
T-bond < 5 year 7.48%



Policy Rates

SDFR 5.00
SLFR 6.00



Population

21.9 million



Per Capita Income - 2020

Rs. 683,106
USD 3,682

“You don't need it unless it starts to rain, but if you don't have it with you when it's already raining, then it's too late to get it. Better to have it and not need it, rather than need it and not have it?”



Sri Lanka Prosperity Index (SLPI)

2018	0.811
2019	0.802



GWP – Health Insurance

Total GWP share	2020	10%
Non life GWP share	2020	15%

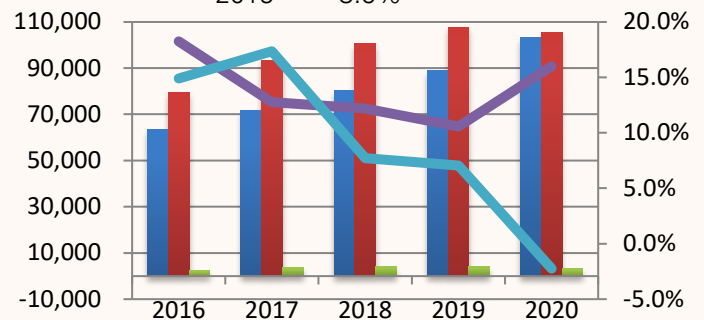


Annual Real GDP Growth

2019	2.3%
2020	-3.6%

Insurance GWP growth

2020	6.0%
2019	8.6%



Insurance Penetration

1.39% in 2020
1.31% in 2019



Asset Growth Rate – Insurance Industry

2019	14.33%
2020	10.55%

Movements of SLPI and Sub-Indices 2015 – 2019



COVID-19: **CUSTOMER** and **DIGITIZATION** in Insurance



Who hasn't asked at some point,

How will this pandemic affect me and my family? How will it affect our lives? Our jobs, education, graduation, birthdays, anniversaries, vacations, social lives? And then: Our finances? Savings? Retirement? To ultimately wonder, Are we sufficiently prepared to get through this? Do we have the protection we may need?

Insurance is fundamentally about protection. And while it cannot protect students from finishing their studies from home, without a proper graduation, insurance can protect against many of the financial impacts caused by the pandemic: travel insurance, health insurance, business interruption insurance, workers' compensation (WC), paid sick leave, life insurance, hospital indemnity, and disability, to name a few, are all types of policies that may provide relevant protection.

In some cases, to have adequate protection, certain terms needed to be revised; for example, the use of personal cars for commercial delivery, use of personal residences for WFH (work from home), or location of work for WC. Given the overall impacts to the economy, many carriers elsewhere in the world have also adjusted the payment terms around timing of payment, late fees and cancellation for non-payment even partial return of premium for reduced use (e.g., auto premiums).

Unsurprisingly, one of the outcomes of COVID-19 has been an enormous increase in customers contacting their insurer. With the in-person channel removed, and while some degree of patience has been needed as insurers learned to cope with volumes, companies sought to leverage the online channel, updated FAQs and conducted proactive outbound communication (mainly email) to reserve the phone for urgent claims. For most insurers, service standards thus remained at an acceptable level.

Six Pillars of Customer Experience

Have insurers done enough? KPMG's Six Pillars of Customer Experience - derived from ten years of primary research across 3,000 brands in 26 countries - identify the key universal principles that underpin successful customer relationships. These are:



Integrity: doing the right thing, being seen to act fairly and in the customer's best interests.



Resolution: responding to needs and finding solutions.



Expectations: setting, managing and meeting expectations.



Time and Effort: making it easy for customers to access information and get essentials.



Personalization: understanding the customer's individual circumstances.



Empathy: showing that you care, choosing the right emotional response.

The two Pillars that are most important to specifically address in these uncertain times are Integrity and Empathy.

How well customers feel their insurers have supported them through COVID-19 cannot be known; in the absence of any comprehensive independent research as yet. The COVID-19 surge aside, by the nature of insurance, routine customer contact is less frequent than in other areas of financial services or sectors such as retail or consumer goods, so the industry already has a relationship deficit to overcome. On average, insurers simply aren't as close to their customers as organizations in other sectors which, by definition, have more frequent touchpoints or interactions. However, COVID-19 might just prove to be the catalyst for innovation in insurance, unlocking greater levels of customer experience and personalization that has long been overdue.

Insurers responding to COVID-19 - but is there more to do?

Insurers have significantly increased their communication with customers - and shown a commendable degree of proactive customer-driven support. The digital transformation within insurers have offered more opportunities to interact with customers. There have been examples in numerous countries of insurers offering rebates on motor insurance given decreased levels of driving. In Sri Lanka, insurers introduced easy claims process and extended benefits for policy holders to cover difficulties of the pandemic.

While these are all positive actions, they also point to a problem: some insurance products have begun to feel out of step with the reality confronting customers, and thus with their needs. Do I have the cover I need, and do I need the cover I have? Many individuals have faced the huge stress and anxiety of sudden, severe income disruption, with an urgent need to reduce their outgoings. This has led them to question their insurance holdings. Is it fair to be paying the same level of motor insurance if your car usage has drastically reduced? What good is your health cover if it only pays for surgery at a time when routine operations have been suspended? Is travel insurance worth buying if disruptions like pandemics aren't included?

At the same time, other products are likely to feel more valuable to customers than ever. We can expect to see a spike in sales of disability and life insurance going forward, as well as maybe hospital indemnity, critical illness and/or business disruption policies with broader cover. Equally, income protection and other savings and retirement products that offer income certainty such as annuities and 'whole of life' products are likely to become much more in demand. Home cover may also become more valued than before given the amount of time people have been spending there and may continue to do if working from home remains more widespread.

Crisis driving innovation and change

As a result of the situation surrounding COVID-19, there is a unique opportunity for insurers to rethink and innovate as they adjust and respond.

First, there may be a need for new products. There has already been some fascinating early stage thinking in some insurers about products that would be payable in the case of pandemics or epidemics. The concept would be that there is a small lump sum payout to help a customer meet any kind of increased or new expenditure for certain defined events. For example, pandemics could be included, with a payout being triggered once a certain number of cases have been registered in the customer's province or region. In addition, products that are more similar to critical illness or riders on existing policies, which pay upon being diagnosed, could emerge as increasingly more popular around the world.

Second, there could be an increase in the appetite for usage-based insurance (UBI) products – where the premiums payable are based on the extent to which a certain activity is performed. The simplest example is for motor insurance where, through telematics and data analysis, a customer would be charged according to the actual number of miles they drive rather than paying fixed premiums over time. The main barriers to take up of UBI have always been data privacy and security concerns. But given the experience of so many motorists during lockdowns, there may be something of a shift in which the car moves from being seen as a fixed asset in an individual's life to more of a variable one, further supported by the rise in the popularity of shared or on demand mobility services – meaning that a UBI model could become very attractive at least to some.

A counter argument to this is that, in the wake of COVID-19, consumer willingness to take public transport will drop, meaning that personal car travel becomes even more ingrained than before. We will have to see how this pans out in the fullness of time. Hence the digital economy will upgrade UBI, on demand and "all in one" insurance products more openly

Customer expectations for insurance shifting to include help with financial anxiety

As the impacts of the COVID-19 situation continue, individuals all over the world are dealing with their financial situation on a personal level day-to-day, but they are also contemplating the implications going forward. Insurers have taken several ways to enhance how they meet needs of their policyholders during these unprecedented times. You can hear it when people discuss what has happened to the market values associated with their personal retirement savings.

Digitization, data, personalization on the rise

Perhaps the most significant changes will be in the way that insurance products are sold, serviced and the usage of customer data. These changes will lead to much greater levels of personalization and so change the customer experience and value proposition.

Insurance has long struggled with the fact that it is not as personalized as other products. The offerings are relatively standardized, and customers only buy their cover infrequently, sometimes indirectly through an agent or broker. For many customers, it is a grudge purchase. They don't particularly want to spend their money on insurance but know they ought to.

There are signs that, through the COVID-19 situation, this will begin to change. Insurers are recognizing that they need to bring more value to their customers, with more personalized offerings and communications on a more segmented basis. One of the notable features of the situation has been the great boom in online communication between people, including via video. It's anticipated that some insurance products will likely start to be sold through a 'digital first' advice approach – where customers engage with an advisor via a video call in the first instance, before the sale moves to other channels to complete. This could lead to much better value for money through reduced distribution costs for the insurer and increased access to personalized advice for the customer.

As we have noted, there is likely to be much higher demand than in the past for certain types of insurance. Insurers need to review their channel strategy approaches in order to serve this demand. This means greater investment in integrating their channels and creating digital pathways on an end-to-end basis. Customers are likely to become less tolerant of frictions and hand-offs in the process to third parties.

Lastly, the digital opportunity for insurers extends beyond the customer and broker interactions at the point of sale. COVID-19 has further highlighted the need for insurers to streamline, improve and digitize operations and claims functions. Insurers are more than ever recognizing the linkage between customer experience and the digital strategy, transformation approach and operational improvement.



A greater willingness for data exchange?

Historically, one of the key obstacles to creating greater personalization has been consumer reluctance to give insurance companies the personal data needed. But there are signs that this too will change post COVID-19.

For example, take the Sri Lankan government's COVID-19 tracking software 'Stay Safe'. Majority of Sri Lankans used the QR code to sign up for this after it was launched without questioning about privacy issues. It indicates that, through the COVID-19 crisis, people are more worried about their health than their privacy.

If this can be built upon, then it suggests that we could enter a new era where consumers are more willing to work collaboratively with service providers to obtain the products and services they need.

Through a more symbiotic relationship on data exchange between customers and insurers, more individualized and targeted products could be created. Insurers will be better able to unbundle products, breaking them down into different components of risk, and only pricing individuals or businesses for the components relevant to them. The customer will get more personalized cover and the insurer will be able to price it more accurately.

Distribution must digitize too

Better digitization and use of data will be key to this transformation – and in insurers' distribution channels, digitization will also be a key theme. While the direct-to-consumer (DTC) market varies greatly by country and by region, insurers have already started to explore or re-open conversations around pursuing a more omnichannel approach in recognition of the shifting willingness of customers to transact more on-line for their insurance needs.

Turning toward the broker community, the lack of digital enablement has become more apparent during the COVID-19 situation. In several counties, it has become clear that many broker businesses are simply not equipped to work digitally or remotely – especially at scale (e.g. renewals).

New business proposals (RFPs) have fallen away and many commercial renewals have simply been rolled over as the pragmatic solution rather than going through a new competitive pricing process. Even the quoting and submissions process, currently an expensive process for insurers, could be more streamlined; better digitization of the data exchange could help make the process more cost effective for all parties involved.



In Asia, agents generally work through face-to-face meetings with customers – and these were halted in their tracks by the virus. In some countries, the inactivity of agents and brokers has been such that insurers have had to look at making very low interest loans to help them keep going or give advances on commission. The Sri Lankan insurance industry was conventional before the pandemic and insurers remained with traditional ways of communications with their customers.

The situation in Asia has not been helped by the fact that wet signatures are still required in some countries. A growing pipeline of new business has developed in Hong Kong (SAR) and China, but this cannot be activated until the signatures are obtained.

It's likely there will be a concerted push by insurers in these jurisdictions to persuade regulators to allow digital signatures.

This could open the way towards new modes of working, with a general move to digital capabilities including digital underwriting to enable more straight-through processing, as well as for claims and fraud detection.

At the same time, there could be some restructuring of the broker market through M&A activity in countries such as the UK. Some insurers have begun scanning the market for potential opportunities with some distressed firms with very low levels of working capital. Insurers know that distribution is key to success, with wealth products in particular, and so are keeping a close eye on opportunities to bolster their networks.

However, there will need to be a good strategic and operational fit. In the wake of COVID-19, insurers will be focused on what a 'minimum viable distribution footprint' looks like – balancing reach with cost efficiency.

The critical priority, however, will be to increase the digital capabilities of broker and agent networks and integrate them with an insurer's own digital environment. This is key because, in commercial lines especially, most customers interact with an insurer through a broker rather than directly. If insurers are going to focus so heavily on digitization and personalization for customers, they can't afford for there to be a disconnect between the agent and broker worlds. The customer experience must be consistent with the insurer's value proposition all the way through, no matter how it is accessed.

Regulators are more and more interested in change

All of this then creates an opportunity to work even more closely with regulatory bodies. There is a need for insurers to work with regulators to ensure that regulations are helping not hindering this unprecedented opportunity to drive change in an industry that has traditionally been very slow to adopt in these areas. Recently, the ASIC/APRA (Australian Securities and Investments Commission¹⁰/ Australian Prudential Regulation Authority) released letters to General and Life insurers reinforcing the importance of doing the right thing in order to meet community expectations.

Coincidentally, this aligns perfectly with the two key pillars, mentioned before, of Integrity and Empathy. And in Sri Lanka, The Insurance Regulatory Commission of Sri Lanka regulates the insurance industry to ensure that the insurance business in the country is carried on with integrity, professionally, and prudently.

There are other regulators who have already or may be issuing similar commentaries or guidance; all of which can be viewed as an opportunity for the industry and regulators to work together.

All change please

Like so many other aspects of insurance companies' business that has been discussed elsewhere in this articles series, Implications of COVID-19 for insurers, the situation is likely to be the catalyst for some far-reaching customer relationship changes. How carriers interact with their customers, and how broker networks integrate with that, could begin to look quite different, quite soon.

In the future looking back, it will perhaps seem remarkable how COVID-19 changed so much that seemed so deep-seated, with a speed that no one could have imagined.





Making

CONNECTIONS

Global insurance

Recognizing the value of a connected enterprise in insurance

Today, insurance companies aren't just competing with traditional insurers - they are competing with everyone. As customers embrace the omnichannel and personalized experiences being offered by the likes of Apple, Amazon, Google, and a myriad of digital start-ups, they are beginning to demand those same experiences from everyone they do business with.

This shift is putting significant pressure on insurance companies to think differently about what they do and how they do it. To enable the customer experiences that will be required to be successful in the future, insurers must become connected enterprises.

The status quo isn't working

Historically, many insurers organized their operations around products (e.g. life, automobile, general), each with a different look, organizational structure, and supporting technology. The challenge with this model is that it is very fragmented. A customer that has multiple products with a company might need to call three different numbers in order to change their address. Such a siloed approach, and the disjointed customer experience it provides, is no longer an option. Customers know that integrated and personalized experiences are possible because they are getting them elsewhere. Insurers that stick to the status quo will quickly find themselves irrelevant.

Building a connected enterprise

With the rise of the pandemic in 2019, the importance of digital collaboration is gradually increasing in Sri Lankan Insurance industry. To be successful in the future, insurers need to connect their front, middle, and back offices in ways that respond to the evolving needs of their customers. This means more than linking disparate channels; it means connecting all functions and technologies so they provide the data needed to create personalized offerings and an unparalleled customer experience.

Eight critical capabilities for experience execution



Brand

Product, Pricing & Customer Strategy
Experience Centricity



Product/Services

Responsive Supply Chain
Partnerships, Alliances & Vendor Mgmt.



Interactions

Advanced Data & Analytics
Technology Architecture & Enablement
Seamless Commerce



People

Organization Alignment & People Capability

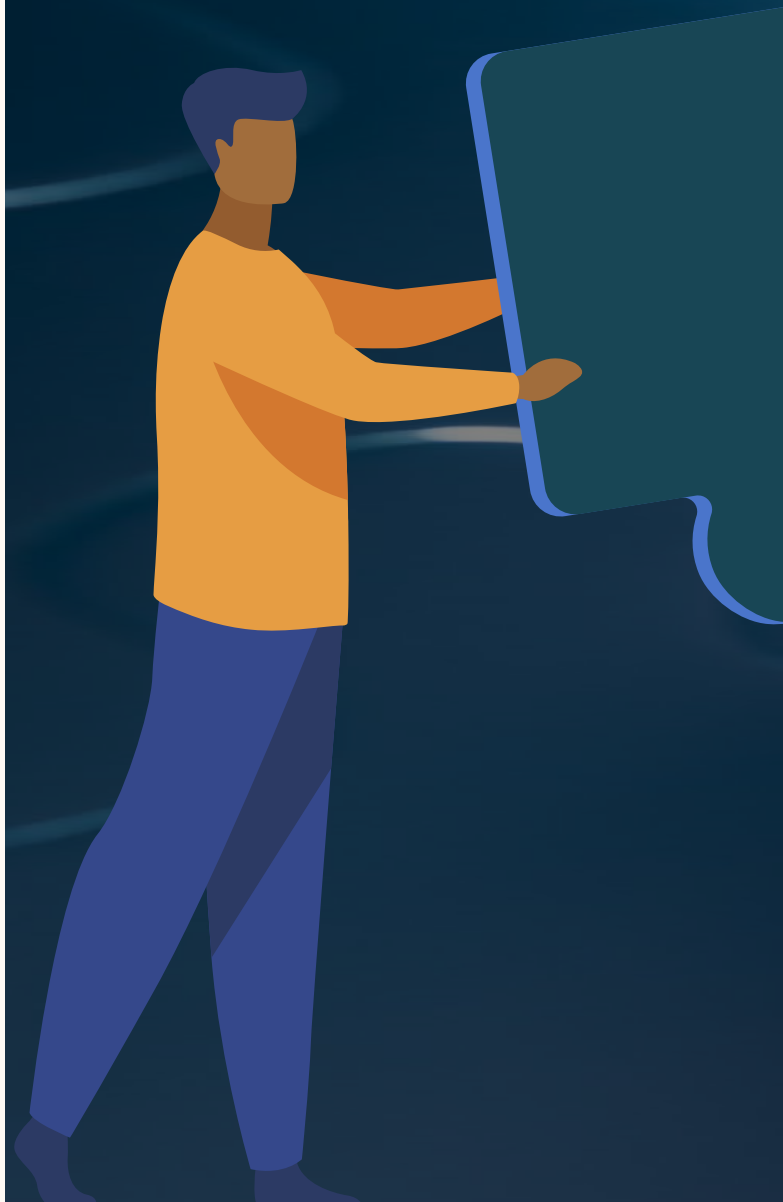
Most insurance companies understand the need to make big changes. According to a recent survey, 75% of insurance companies are making moderate to significant investments in one or more of the capabilities required of a connected enterprise. Of the eight capabilities underpinning a connected enterprise, the areas receiving the most investment are [customer] experience centricity, seamless transactions, advanced data and analytics, and technology architecture and enablement.

Starting off on the right foot

The transformation into a connected enterprise is a complex journey, one that can hold many obstacles for companies that are unprepared

Top five challenges to a truly Connected Enterprise

The transformation into a connected enterprise is a complex journey, one that can hold many obstacles for companies that are unprepared



So, what can insurance companies do to start off on the right foot? Here is a holistic five-step approach that insurers can take into account:

1. Gather rich customer insights: Before making changes, insurers need to develop a better understanding of their customers - their intent, purchasing behaviours, interactions, and most critical touchpoints.

2. Develop products and services entered around customer needs: Rather than looking to match products with customers, insurers need to develop innovative products and services that are customer-focused and responsive to customer needs.

3. Identify meaningful customer journeys: Based on customer needs and insights, insurers should identify key customer journeys - the process steps and what customer needs are at each stage of the process. This process is pivotal for identifying activities that require great empathy and activities where customers simply want quick, transactional service.

4. Design operations to be responsive and efficient: Using the customer insights built in the first three steps, insurers can redesign their organization to be responsive and efficient to their customer needs - from using AI to support transactional activities to providing richer human interactions when it matters most, all supported by robust technology and data and analytics. To be effective, this process also needs to include building end-to-end processes to support employees who will need to be agile, think like their customers, and really embrace customer-centricity within their roles.

5. Create a robust integrated digital support platform: Based on what they want to accomplish and how they want to engage with their customers, insurers can then develop an integrated digital platform for their organization focused on providing a single customer view. Such an integrated platform will be essential for service delivery in the future as it will provide the backbone needed to track customers interactions and provide the data required to provide highly personalized customer experiences.

Worth the investment

While shifting customer demand, increasing competition, and technology innovations are key drivers pressuring insurance companies to become connected enterprises, there are strong financial reasons to transform as well. In fact, companies that invest in becoming a connected enterprise have seen a two times overall return on their investment across many metrics – from overall revenue, customer engagement, and lifetime value to improved marketing costs.

The future
comes early:
**INSURANCE
WORKFORCE**
transformation
through COVID-19



Workforce successes and challenges faced by insurers as they rapidly moved to remote working due to COVID-19

.With the spread of COVID-19 right across the world, we're all doing it now. Whether it's from a spare room or the kitchen table, we're working from home, connecting with colleagues through video conferencing calls, and learning to do things differently.

Like every other sector, the insurance industry is in the thick of it. It's learning fast, adapting and evolving. So far, it seems to have gone better than many probably expected. Despite some inevitable teething issues, insurers have generally been encouraged by their ability to adjust.

Of course, it's not that remote working is anything new. A lot of organizations have utilized it to some degree for many years. But it has usually been confined to certain roles and, in some businesses, certain levels of seniority. The real difference here is one of scale. Whole businesses from top to bottom are doing it now, simultaneously, and almost without warning.

The fact that there haven't been any major failures in insurance is something to celebrate in itself. But that doesn't mean there isn't plenty of room to improve and refine the operating model. Insurers have kept the show on the road but of course customers have noticed the difference, with much longer waiting times across contact channels.

In conversations with clients, what becomes apparent is that those insurers who had already started the journey towards a digital transformation of the business have been able to make the huge step-change adjustments brought about by COVID-19 more easily and quickly than others.



In truth, the insurance sector as a whole was behind other industries, such as banking, in terms of embracing digital and more flexible ways of working. This crisis is forcing them to massively increase the pace and step up.

No going back now

What is clear is that, for insurance and indeed nearly every sector, there will be no going back. What we are seeing through the COVID-19 situation is the emergence of a 'new normal'. Its final shape isn't clear yet because the crisis is far from over and the future is impossible to read. But at the end of it, we will be living in a new reality, with different operating models, different value propositions and different employee expectations and experiences.

The key workforce realization that insurance leaders need to make right now: don't think about this as something for the next 12-16 weeks followed by a return to 'business as usual'.

For one thing, no one knows how long and how severely the pandemic will last, or how quickly and to what extent lockdowns can be eased in different parts of the world. So, remote working may be more or less enforced for much longer than just the next few weeks and months, at least in some parts of the world. Inspiringly, Sri Lanka's public sector also introduced work from home to continue operations and to safeguard the workforce.

But, perhaps more importantly, the principles of the new ways of working that businesses and staff are embracing are likely to be with us to stay. The real-time experiential changes that we are living through will drive a sustained transformation of working models. This is something that progressive businesses were aiming for anyway.

It is also true that COVID-19 is unlikely to be the only shock. There could be others in the future - another pandemic, a financial crisis, a major industry disruption. Insurers need to be prepared and agile enough to cope with whatever the future may throw at them.

Drill down in a few areas of insurers experiencing challenges

While many insurers are generally handling the remote working well, there are a few areas that have experienced more challenges than others. These would be ripe for improvement opportunities moving forward. Examples of some of those areas include:

- Human resources, given the need for EE hyper-care
- Call centers due to the increased activities around inquiries from policyholders
- Front office areas like sales support, marketing and distribution as they have traditionally opted for more face to face interactions with clients so coming up-to-speed on technology
- Policy endorsements
- Billing disputes
- Complex underwriting (specialty risks - taking longer as was done in huddle fashion before)
- Complex claims adjustments and handling
- Reinsurance reporting
- Settling and billing (mostly due to access to systems and complexity)
- Finance resources
- Offshore processing centers

Learning the lessons - the 5 C's

What has been learned so far and how are insurers approaching the challenge at hand? It helps to look through the lens of what KPMG calls the Talent Risk Framework, which sets out five key areas that are critical to managing and equipping a workforce in times of crisis or significant change. These are "The 5 C's" which are:



1

Capacity: Are there sufficient resources in the right locations, and are they equipped to do what you need them to do?

2

Capability: What are the key skills and capabilities required to ensure your workforce operates effectively on a sustained basis?

3

Connectivity: How will teams stay connected, motivated and engaged in this new and emerging environment?

4

Cost: How much will the workforce cost to run as you ensure business continuity?

5

Compliance: What are the regulatory implications of remote working for an extended period?

One of the most striking things that has been seen so far is the gaps coming to the fore are not connectivity or technology gaps but rather are to do with people and management skills. But suffice to say that while there have been some bandwidth issues, many insurers are coping well with moving to remote connectivity.

A distributed model with smaller, nimbler teams

The deeper challenge is to manage the remote workforce in order to achieve the right capacity in the right areas. This has already manifested itself in the huge spike that many insurers have experienced in inquiries and claims for travel and health cover, as an example, while other areas (such as motor) have declined. So businesses need the flexibility to respond and react quickly. They need a liquid workforce in which resources can be shifted as needed.

This is about the creation of a distributed model that brings the flexibility and functionality organizations need to operate in today's highly uncertain environment. It is something many insurers are having to learn quickly because often insurance organizations are relatively traditional with a high emphasis on presenteeism: the belief that teams of people need to be present together in the same place for the business to function. "I need to see my team to know they are being productive" is a common mantra in the industry. But COVID-19 is teaching us that teams can be set up and engage in different ways and still be productive.

It is also driving the adoption of smaller and nimbler teams - breaking down large functions into small working groups who can self-organize, connect highly effectively, and react quickly to changing requirements. It is proving the model for greater levels of very human interaction and connection on focused areas of work.

However, there are challenges. There are aspects in which remote working struggles to replicate some of the great advantages of face-to-face interaction. Many clients reported that the creativity and spontaneity, the snowballing of ideation, that occurs when a group of people come together to discuss an issue or a problem is very hard to reproduce virtually. This is something that needs further work and exploration to see whether there are solutions that can help.

One other area where the need for a distributed model may also apply is in the use by insurers of offshore processing centers such as in India. Their ability to function has been severely tested by the lockdown there, creating an urgent operational challenge that many insurers have already had to deal with. In the wake of this crisis, we may see insurers distributing more of this offshore work between more locations so as to minimise the operational risks.

The remote management challenge is key

In today's circumstances, it becomes essential to manage the capabilities of the remote team effectively. Do team members understand what the priorities are right now; do they have the tools they need; are the processes and protocols in place to help and guide them; is there sufficient structure to their working day?

It is certainly true that remote management is the hardest part of running a remote workforce. That is why organizations need to pay as much attention to how they are supporting managers and team leaders as to how they are supporting the workforce at large.

Managing a team that is not physically present, ensuring that people feel motivated and supported, helping them to perform at their creative best, looking after individuals' mental and emotional wellbeing in a strange and stressful time, setting goals and assessing performance - there is no real road map for this on the scale that we are presently seeing through COVID-19. Targets and performance measures are especially hard to set in such a fluid time - without a doubt, pay and reward decisions will be especially difficult this year.



Managing costs, ensuring compliance

This latter is part of the cost equation - and of course it is essential to establish a true picture of the costs of running the remote workforce compared to normal baseline costs. Some businesses may also be considering, or have implemented, measures such as unpaid leave, part-paid leave, or the furloughing of some staff. These are not easy measures to take.

A more flexible and remote workforce could result in the longer-term consideration of other aspects of compensation. In the future, we expect the overall organization-wide split in many insurers of time spent in the office against time working remotely to be roughly 50-50. Some staff may only physically come into the office once a week in the future. Even for call center operatives, we anticipate they may only come in three times a week. This could result in significant commuting cost savings for many staff - so could we see salaries adjusted as a result?

Another big cost area is real estate. We expect insurers and many corporates across the board to review their office portfolios in the wake of the crisis and potentially downscale them.



Working remotely also raises a number of critically important compliance issues that need to be managed. Data security becomes a key concern, with a need to ensure that staff only use approved communication and data transfer methods.

Compliance with regulated or business critical processes remains critical: management must ensure that the necessary electronic approval processes are in place, and consider whether any new measures need to be introduced for compliance

requirements to continue to be met. It is also essential that staff comply with social media policy and are reminded that phishing scams are likely to be especially prevalent at the current time. Staff remain the first line of defense in the three lines of defense model, and any lapses could have serious repercussions. This must also extend to any contract or third party supplier workforce - how are they being communicated with, are they clear about any new processes or protocols, and who is taking responsibility for overseeing the new working relationship?

An opportunity to embrace the future now

These are times of great change that have been thrust upon the industry. Those insurers that grasp the challenge and leverage fully flexible ways of working will position themselves for a new future. Those that don't invest sufficiently in enabling more digital workflows and that don't design new processes and tools to suit will fall behind and find themselves at a significant disadvantage even when this crisis dissipates.

In effect, the workforce challenge is to embrace the future at an accelerated pace and achieve in weeks and months what would normally have taken years. That is both the opportunity and the threat that COVID-19 poses



CEO Outlook of the **INSURANCE MARKET** in Sri Lanka



Through risk prevention and risk reduction and by sharing risks insurers help protect society, foster innovation and underpin economic development. Sri Lanka's insurance industry has a vital role in managing Sri Lanka's social security risks. This social security gap, which is growing wider every year, has to be bridged by the country's insurance sector.

It has been identified the need of establishing a structured Social Security System in Sri Lanka to fulfill the objectives of bridging the protection gap, a key Socio-Economic issue in Sri Lanka, which has negatively affected both Economic and Social/Human development in the country.

The key factors affecting the cause of low insurance penetration in Sri Lanka are, low disposable income levels and low priority towards insurance rather than protection in general public's spending, high dependency rate, free health care services and active participation of both formal and informal welfare schemes and micro level community based welfare systems in the country.

As a result of above a protection gap between insured losses and economic losses or uninsured losses is high. The protection gap eventually leads to economic and social issues which affect emerging nations and developing countries like Sri Lanka which have been caused due to natural/environmental disasters and human interventions such as accidents, injuries and sicknesses.

Properties, general public and economies with high insurance penetration recover much more quickly after a natural disaster or accidents than properties and general public that rely on government for their recovery.

We are on the vanguard of inculcating the benefit of insurance to the general public. Hence regulatory bodies and government plays a pivotal role facilitating our groundwork laid for a sustainable society while making significant contributions to the economy and society. Developing practical and accessible insurance solutions for all socio economic groups is the first step to increase the insurance penetration and focus should be on high risk segments and other economically vulnerable groups.

We are living in an unprecedented time and we are facing a dynamic and complex risk landscape which ushers us toward diverse, interconnected and complex risk factors. At the same time it has presented new avenues and opportunities for insurers to mitigate them as well. In order to confront these challenges every insurer has to step out of their comfort zone and take a holistic approach to broaden their horizons.

The pandemic has radically shifted consumer and employee needs, habits, and expectations, while compelling virtualization of insurer operations practically overnight.

Mr. Chandana L. Aluthgama
Chief Executive Officer
Sri Lanka Insurance
Corporation Ltd



It should be a responsibility of every corporate especially insurers to be accountable and to act responsibly to adapt to the situation by following the safety guidelines in dealing with employees and other stakeholders while providing uninterrupted service to customers with insurance being declared as an essential service.

Although insurers were compelled to operate in a volatile economic environment the industry faced the situation very well to serve customers to ensure their insurance needs are being met. Amidst the chaos the silver lining on the cloud is, we were fortunate to witness that there is progressive thinking among the customers as they have been very responsible and responsive towards the insurance. Premiums were settled using alternative ways as they truly understood the importance of insurance at this defining time.

We are heading towards a more challenging economic and social environment which has a huge impact on consumer lifestyles, spending patterns, buying behaviors and needs and wants. Insurance will be one of the most important commodities that we sell and insurance is a very responsible industry which provides a crucial service to the society.

As we are settling into a new reality we have immense challenges to overcome with strong and positive actions to minimize the impact focusing and relying on the capabilities and strengths of our human capital and technology.

Although the shift to technology driven insurance solutions are already underway, it is becoming a top priority as customers no longer prefer the insurance being handled in the traditional way with human interaction being a focal point.



On the contrary, in a country like Sri Lanka people still prefer a human touch when taking a lifetime decision such as insurance. Hence insurers must have a right balance between human and technology to provide a seamless insurance experience.



With technology playing a bigger role and data being shifted outside the traditional security perimeter, insurers need to plan and invest on cybersecurity to have a greater control over the risk of exposing sensitive data. Privacy is becoming a critical factor.

On the regulatory aspect, IFRS 17 standard will increase the transparency of insurers' financial positions and performance and is intended to make the financial statements more comparable with both other insurers and other industries. The change will be significant for the insurance industry as a whole and the change will affect both preparers of financial statements and users.

As Insurers we are facing a decisive time yet we are resilient with our prudent practices and we are ready to offer innovative insurance solutions to cater to different needs. Moving along the trajectory of change we will provide protection to individuals and society irrespective of the severity of the situation.



New **REALITY** for **INSURANCE**



Insurance Macro trends

Throughout COVID-19, the insurance industry — along with all business — has experienced a time of monumental challenge. The impacts of this health emergency have expanded into far-reaching economic and societal issues. It seems clear that as we emerge from this period, it will be into a new reality that will look very different to what existed before.

KPMG insurance professionals have been reflecting intensively on — and widely discussing with clients — the nature of the upheaval taking place and what this means for insurers.

We start by exploring seven key macro themes that we believe are particularly relevant to insurers and which they must respond to in a fundamental way in order to thrive in the new reality.

Some of the seven themes have been with us for some time but have become greatly accentuated and accelerated in the wake of COVID-19 — such as financial resilience or climate change response.

Others, though, are almost entirely new. The fundamental importance of health in terms of staff, customers, products and economic impacts — what we call The Age of Biology — is one such example. The New Reality Workforce is another because, although remote working has been with us for many years, COVID-19 has elevated it to a new plain altogether, completely overturning old norms.

We list it as number seven — but in fact the imperative to become Digital First, Digital Now is absolutely core and runs across every single macro theme. COVID-19 has shown us the inter-connectivity of multiple forces and the response must be digital ways of working and originating business that drive speed, efficiency and a better customer experience.

Insurers have historically lagged other sectors in their digitization efforts — now, we have reached a watershed moment. It is time for insurance to catch up and re-emerge stronger and better. We believe that investing in capabilities to respond to these trends may pay long-term dividends for an insurer.



The Age of Biology

Building organizational immunity across biology and economics

What it means

Biology has left the lab

Biology is playing an important role in the C-suite, the board room and throughout the workplace.

Health is now becoming a core competency across all organizations.

Balancing biology and economics

There is business tension between doing right for the collective and making a profit, getting back to work and keeping workers safe.

Impact on insurance

Health and safety concerns

There needs to be more flexibility, testing and physical spacing to accommodate a safer workplace.

In-depth cleaning will take place and availability of hand sanitizer everywhere will be the "new normal" in office spaces.

Technology will play a major role assisting with the balance between staying at home and returning to the office.

Product innovation

New products may emerge around pandemics or viruses, existing products (e.g. critical illness) may become more popular, and usage-based products (e.g. auto) may gain in popularity.

Prevention-related products will increase along with incentives around safety.



The New Reality Workforce

Building a versatile and adaptable workforce

What it means

Workforce change drivers

There will be bifurcation of workers into essential and non-essential employees, unprecedented unemployment and office closures.

The needs of frontline and knowledge workers must be balanced.

Workforce archetypes

Companies need to consider new archetypes combining technology and a flexible workforce.

Impact on insurance

Remote working becomes more permanent

Realignment of needs for physical versus remote working.

Expect impacts to infrastructure, risks (cyber, privacy, ergonomics at home), productivity, training/skills building and performance measurement.

Access to talent

There will be significant opportunities to acquire new talent (e.g. digital, technology and data) to upskill the workforce as organizations will be less reliant on location.

High volume workforces

Claims handling, contact centers will be reimagined as more automation is introduced and customers are more comfortable with digital interactions.



Ambidextrous Business Models

Playing across physical, virtual and digital

What it means

Oscillating models

Insurance organizations need to navigate a rapidly changing workforce, customer behaviors and business environments.

Insurers switched from an in-person environment to a virtual model overnight and it's likely that they will continue to oscillate between the two.

New core competencies

A rapid response to an uncertain environment will become a new core competency.

Businesses that can sense and respond to these new needs will both survive and grow.

Impact on insurance

Cost, continuity and resiliency

Continued strain on operations and the associated costs are forcing a fresh look at operations across-the-board.

Continuity and resiliency rating models becomes a core component of transformation efforts.

AI and automation

Will drive the change and re-thinking of operating models on an end-to-end basis.

Scenario planning

Becomes the norm for ongoing operations in a combined online/offline organization structure.



Building Financial Resilience

Ensuring freedom to maneuver

What it means

Capital, liquidity and cost

Insurers need to maintain sufficient liquidity and capital to continue to operate.

Managing cost pressures is a top, immediate concern.

Navigating uncertainty

CFOs are in the midst of the most uncertain, yet critical time for decision making.

Pulling the right levers across liquidity, capital and cost will be critical.

Impact on insurance

Solvency ratios

Volatility is expected and understood by stakeholders but requires increased modeling on a real-time basis.

Liquidity

More detailed cash management strategies evolving while removing barriers to trapped cash and capital.

There will be an increased use of scenario planning and analyses to gain real-time understanding.

Investments

Closer monitoring of low interest rates, equity markets and credit issues is required due to the downturn in financial markets. The impact on the valuation of commercial real estate/loans is essential given the possible shifts in those assets classes.



Climate Change

Preparing for a future of increased risk

What it means

Climate risk as a core business issue

Global temperatures are rising creating risk to the global economy, ecology, and human health and well-being.

Growing exposures from increased catastrophic weather events (e.g. hurricanes, wildfires) to pandemic risks are rapidly becoming a new reality, challenging the bottom line.

New thinking on ESG

Boardroom conversations around ESG are changing, particularly on corporate purpose, stakeholder capitalism, and climate risk and resilience.

Impact on insurance

Role of the insurance industry

Insurance can build socio-economic resilience and enabling economic development and entrepreneurial pathways for achieving climate change goals and targets.

Use of incentives and performance metrics helps to drive the right focus on ESG issues.

Mitigation isn't just the right thing - it is also a pathway to profitability; insurers can play a role in adaptation, working with public bodies to build interventions that make societies more resilient to the impact of climate change (e.g. flood defenses, building standards).

New products and business opportunities

There are new risks to insure, including risks related to new industries, such as wind farms and alternative energy facilities.

There are also emerging financial risks, such as those involved in carbon trading.

Insurers can move funding into greener investments, and will be challenged by stakeholders if they invest in initiatives deemed not good for the environment.



The Innovation Imperative

Unlocking new competitive advantages

What it means

Invest for growth

Radical waves of innovation are expected as insurers adapt to current environment.

Making the right bets in innovation may help insurers to capture market share and move into new markets.

Leapfrog

Innovation leaders will leverage this moment to leapfrog ahead of their peers.

New ecosystem of innovative firms will be the next wave of insurers.

Impact on insurance

Innovation at scale

Remote working happened so quickly proving that companies can move faster.

The appetite for large-scale, impactful innovation has increased and typical barriers seem to be removed or lessened.

Outsourcing to drive innovation

Insurers looking to cut costs and take advantage of innovative solutions and infrastructure are looking towards insurtechs.

Partnerships

Access to the latest technologies and new talent will be critical as insurers focus on operational excellence, AI and automation.



Digital First, Digital Now

Digitizing the organization

What it means

Customer-led digitization

COVID-19 is accelerating the digitization of business and operating models across the front, middle and back office

Modern technology infrastructure

Is critical in order to serve customers and enable employee productivity. Robust cyber security and fraud protection is required as risks rise.

Impact on insurance

Digital transformation is accelerating

The significant gap between customer expectations and insurer's abilities is driving insurers to connect their front, middle and back offices. Those who move the fastest will reap the competitive advantage.

Customer-first thinking

Direct-to-consumer sales will require significant and rapid upgrades particularly in many parts of personal insurance.

Brokers/agents need to be integrated at each step through digital interactions and interfaces.

Data

Movement must be seamless and protected through the different gates. Use of internal and external data becomes commonplace (e.g. underwriting).

Technology and infrastructure

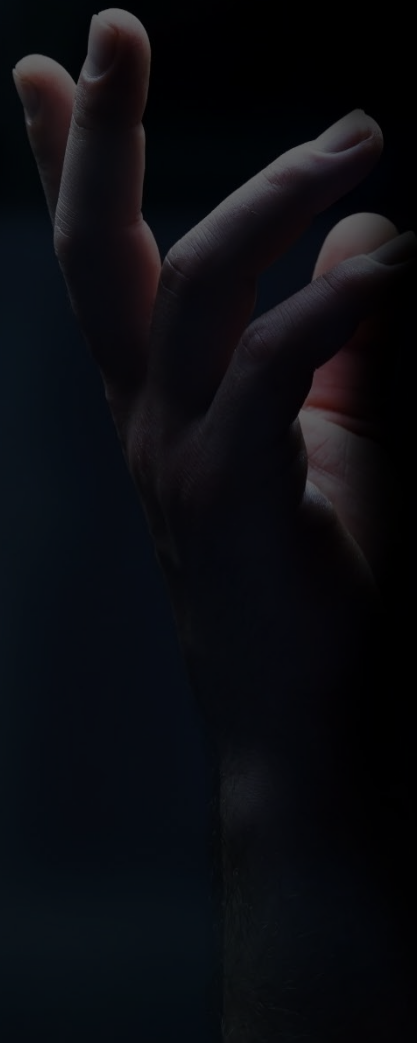
Mass movement to modernizing technologies, cloud services and decommissioning legacy systems.

Claims

Early focus for digitization — anything that can be digitized will be; from first notice of loss/claims submission through to ultimate payment of claims including all interim steps.

Finance

Will be a strong business partner and play a key role, enabling operations through deep analytics and predictive capabilities.



Feedback from
**LEADING
INSURERS** on the
front line of IFRS 17
IMPLEMENTATION

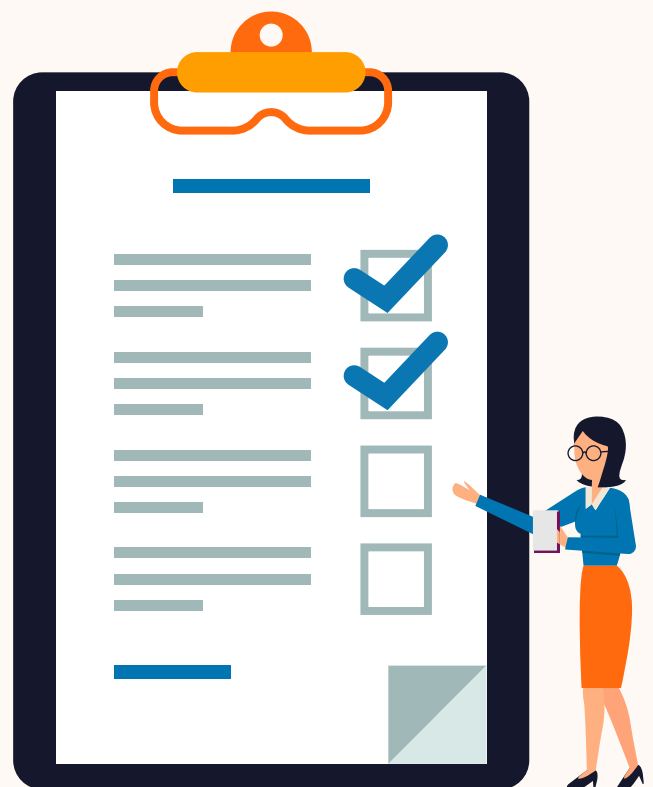


KPMG Survey and why it may be useful

Use our study to harness the experiences of leading insurers to accelerate your IFRS 17 journey. With less than a year to run before the date of the IFRS 17 opening balance sheet, the clock is ticking. The journey to implementation is not easy, and late starters face multiple jeopardies — more ground to cover and a smaller talent pool on which to draw. Those who delay also risk forgoing the opportunity to be strategic in how they operationalize the new standards and to achieve greater efficiency.

Even front runners don't have the luxury of much time to spare. And even among the largest and best resourced insurers some are finding they need to take decisive action to re-invigorate their implementation program and secure more resources to accelerate progress and reduce project risk.

Our study covered some of the largest insurers around the world, with significant resources and bandwidth. We list hallmarks that distinguished those that stand out from the pack and are tackling IFRS 17 with confidence, below,



Early analysis of data and disclosures: Front runners identify disclosure requirements rigorously at an early stage of their implementation program and use this to guide data requirements and design decisions, avoiding costly rework.

Effective use of working assumptions: Allows multiple tasks to proceed in parallel rather than sequentially, accelerating progress in a compressed time frame. Front runners define working assumptions, keep them under careful review and refine them as interpretations evolve, rather than back end loading critical decisions.

Staying in control: Front runners implement effective governance and oversight from the get go, allowing them to identify slippages and correct where needed. They understand the need to design and test controls throughout implementation as well as controls over new reporting processes, avoiding a scramble to back-fit controls close to the finish line.

Rigorous testing: Closely linked to controls, front runners understand the importance of testing; testing new data feeds, new systems, new processes and new reports and results. They plan for rigorous testing and know they need to allow the time for re-work and re-testing in order to face the new world of IFRS 17 in confidence.

Headquarters of participating insurers

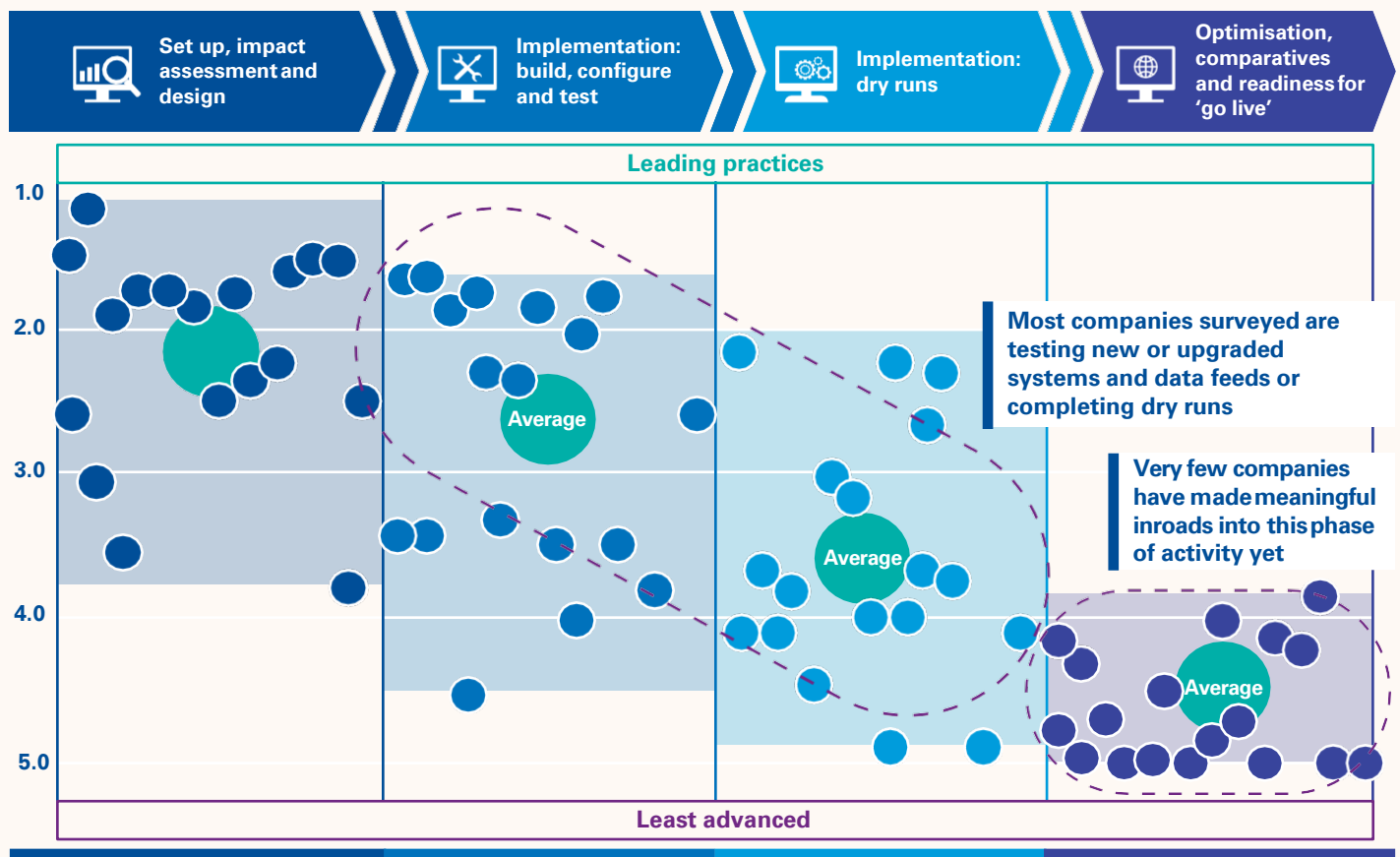


IFRS 17 implementation in four phases: overview

Two thirds of respondents have completed updating their target finance systems architecture and are deep into testing their preferred IFRS 17 solution. Twenty percent of companies in our survey have completed end to end dry runs across at least part of their business, although the majority are not there yet, completing builds and initial testing. Among the companies surveyed, trends by size and geography are not significant, although composites and life insurers generally appear further advanced than property casualty insurers.

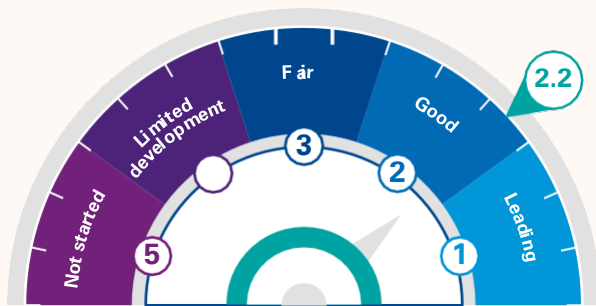


Twenty percent of companies in our survey have completed end to end dry runs across at least part of their business, although the majority are not there yet, completing builds and initial testing.

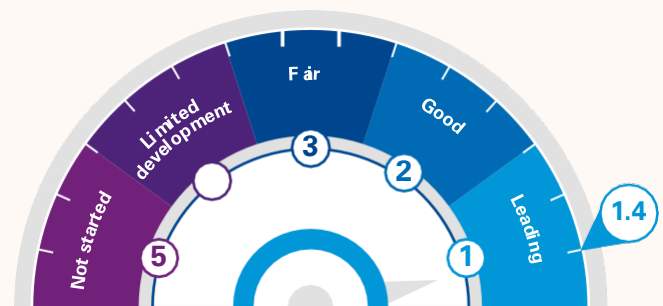


Source: IFRS 17 benchmarking survey, KPMG International, December 2020.

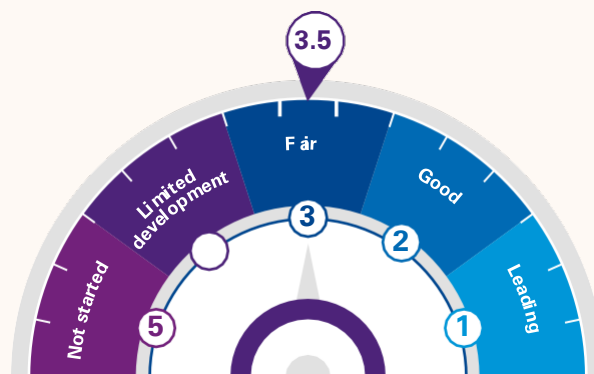
1. Set up, impact assessment and design



Average score across all respondents



Most advanced attribute:
Creating a broadly skilled
global implantation team



Least advanced attribute:
developing designs for updated
processes and controls

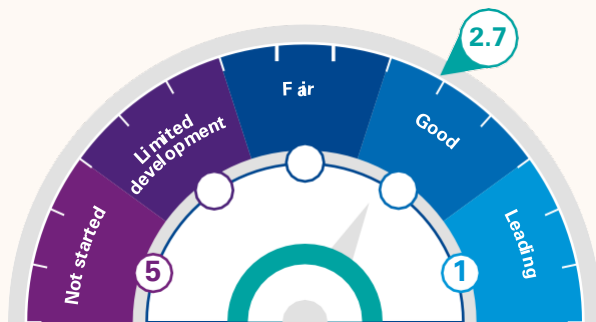
Where are the leaders?

All the companies in our survey have multi-year and multi-jurisdiction programs which have been in flight for several years. Two thirds have developed their target finance systems architecture and selected and designed relevant IT solutions and two thirds have developed a full suite of policy and methodology papers to guide design and implementation.

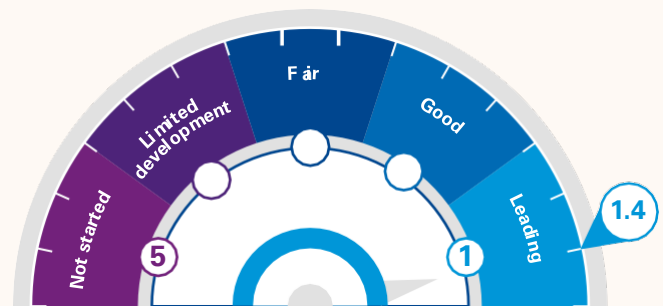
What could work better

- 80 percent of companies have refreshed their finance TOM but only a minority use it to guide design decisions.
- Two thirds of companies find it a challenge to deliver appropriate functional training to relevant staff at the right time.
- Even among leading companies developing designs for updated processes and controls is lagging — this is the least advanced of all tasks in this phase.

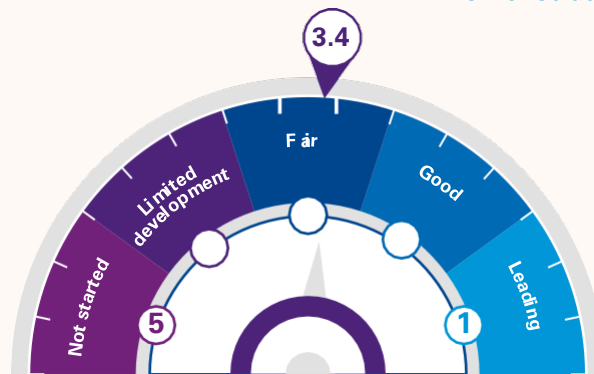
2. Implementation: build, configure and test



Average score across all respondents



Most advanced attribute:
Demonstrating governance & oversight
over implementation



Least advanced attribute:
Plans for restating opening balance
sheet

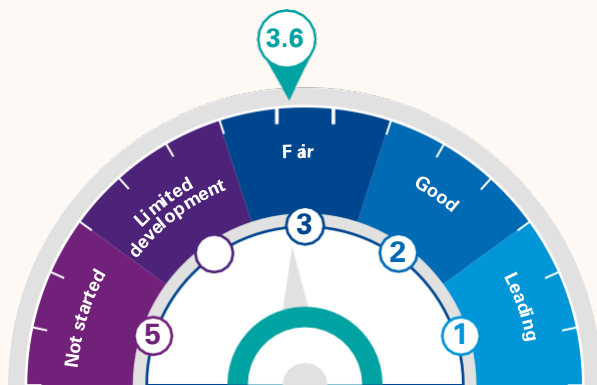
Where are the leaders?

Half of respondents have fully updated IT systems which have either been tested or are ready for testing and half have completed updating actuarial models and one third have updated new data feeds.

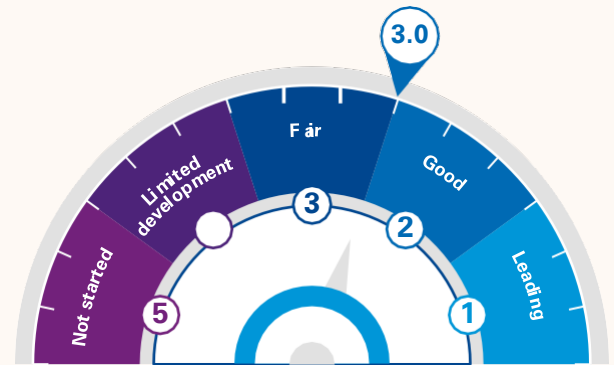
What could work better

- Only 10 percent have involved all three lines of defense in testing **updates to IT systems**
- Half do not yet have a reasonably complete draft of their updated financial statements and have not yet updated their chart of accounts and posting schemes — an important proof point to define data requirements with one third acknowledging there is still further work needed to identify **new data requirements and sources**.
- Nearly 80 percent are still developing their **approach to transition** and building their opening balance sheet.

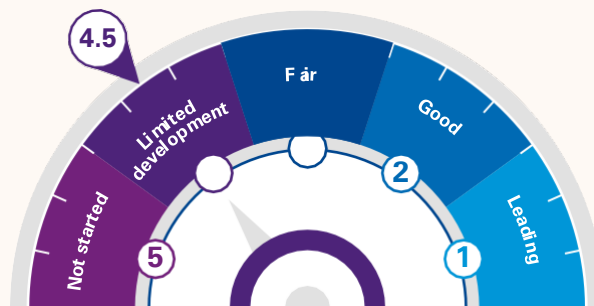
3. Implementation: dry runs



Average score across all respondents



Most advanced attribute:
Tracking open issues, simplifications
and workarounds



Least advanced attribute:
Updating planning & forecasting,
management reporting and KPIs

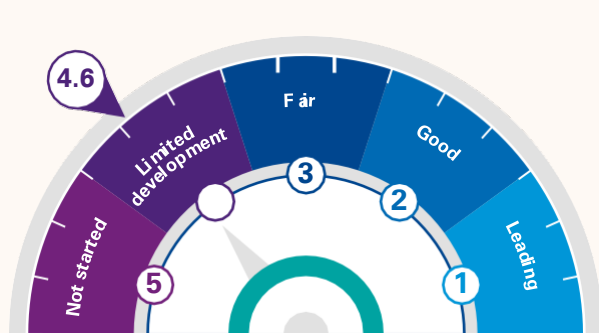
Where are the leaders?

Twenty percent of companies have completed end to end dry runs across at least part of their business. One third have developed plans to handle parallel running once their opening balance sheet has been developed, although only two companies have completed updating their consolidation systems and so several of those that have completed dry runs are using workarounds to collate the data.

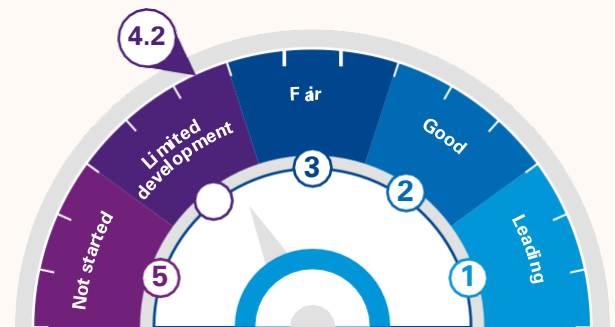
What could work better

- Forty percent of companies are not tracking and prioritizing open issues, workarounds and matters of interpretation creating **greater challenges in demonstrating governance and oversight** compared with earlier phases.
- Eighty five percent of companies have not yet designed quantitative IAS 8 disclosures (disclosure of the impact of forthcoming changes), an important public disclosure of the impact of these changes.
- Updating planning and forecasting, management reporting and key performance indicators is a major task for those where IFRS is the group's main basis of reporting.

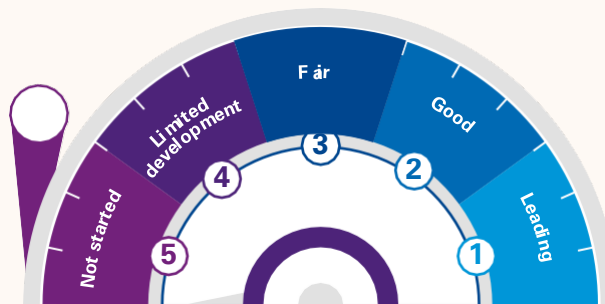
4. Optimization, comparatives and readiness for go live



Average score across all respondents



Most advanced attribute:
Testing interim reporting capability



Least advanced attribute:
Building comparatives

Where are the leaders?

Unsurprisingly, few companies have yet to develop detailed plans for this phase of activity. Of those that have developed plans to tackle transition and build comparatives, a quarter have developed plans to test their interim reporting capability separately from their full close — a subtlety often overlooked.

We will revisit and share progress over future months and years.

“

Forty percent of companies are not tracking and prioritizing open issues, workarounds and matters of interpretation creating challenges in demonstrating governance and oversight.

”

Sri Lankan Insurance **SECTOR REVIEW & OUTLOOK**



The pandemic added a tailwind to the life insurance industry while non-life is primed to grow from the post-pandemic economic revival

Sri Lanka's insurance industry which emerged stronger from the pandemic induced conditions in 2020 transcended its momentum into the first quarter in 2021 (1Q'21) with almost every key performance matrix improving, albeit some divergence was seen between how life and non-life insurance segments have fared.

For instance while the Gross Written Premiums (GWPs), profitability matrices, Risk Based Capital (RBC) and industry growth turned out strong, the pandemic and its aftermath rekindled future prospects, particularly for the life insurance segment as people who became more conscious of the risks to their lives, sought more life protection.

Meanwhile the increasing risk awareness, growing public confidence over insurance, innovative and varied product offerings and, more recently the growing use of digital platforms from everything from customer on-boarding to premium collection to claims handling, particularly at a time when the conventional agent driven model became disrupted due to the virus, have all contributed to the robust growth in the life segment.

Reflecting this phenomenon, the life insurance GWPs grew by 15.98% in 2020, the highest since 2017 before reaching an exponential 34.13% growth rate in the 1Q'21, while bringing the penetration level measured through GWPs as a percentage of the Gross Domestic Product (GDP) to 0.69% from 0.59% in 2019, with the total insurance penetration to 1.39% of GDP from 1.31% a year ago.

While the life insurance penetration still remains well below some of the Asian counterparts with relative high penetration levels such as Malaysia and Thailand with just under 3.5 percent of GDP⁽¹⁾, the recent data showed the pandemic in fact added a tailwind into an otherwise less impressive growth and woefully low penetration levels in Sri Lanka.

In fact, among the lines of insurance businesses, health and life insurance became the favourites to grow, globally with the heightened risks caused by the pandemic to one's health and related expenses, and the need for financial protection and independence after one's retirement. This behaviour is expected to have a similar impact on the local market too though there was a temporary setback in 1Q'21 as can be seen by the analysis below.

The pandemic induced demand for more life protection will receive further impetus from the envisaged growth in the Sri Lankan economy which is poised to grow from 2021 onwards which is estimated above 3.0% under the most conservative estimates, after a contraction in 2020.

There is a strong positive correlation between the life insurance GWPs and real GDP growth as the rising per-capita income drives life insurance penetration.

In a further sign of significance of life policies to people in Sri Lanka, the policy lapses measured by both the number of lapsed policies and lapsed policies as a percentage of total policies in force declined to their lowest in 2020, continuing the downward trajectory witnessed during the last 5 years.

Further the rising incidence of non-communicable diseases and related deaths which currently accounts for 83% of total deaths in Sri Lanka is also expected to provide further momentum for the people to sign up for health and life covers.⁽¹⁾

Non-life (General Insurance) landscape

Conversely, the non-life insurance business met with some setback as reflected in the fall in the GWPs, caused by the pandemic induced conditions which forced the authorities to put a lid on vehicle imports to conserve foreign exchange as motor insurance accounts for the biggest driver of general insurance business in Sri Lanka, accounting for about 60% of the total non-life GWPs.

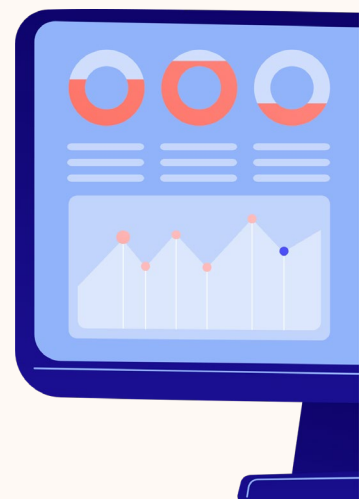
Paradoxically the sector delivered some robust profit growth in 2020, supported by the sharp fall in the claims, which logged at 26.88%, weighing down on the net claims ratio to its lowest in five years due to limited mobility and near absence of travel and leisure industries as such conditions immensely reduced the incidence for claims.

Besides, the timely intervention by the regulator also helped the broader industry to weather the pandemic induced challenges successfully as the Insurance Regulatory Commission of Sri Lanka (IRCSL) suspended dividend payments and discretionary payments by insurers in a bid to safeguard capital in the sector while at the same time they offered a three months moratorium on all insurance premiums from the onset of the pandemic last year to prevent potential policy lapses from occurring.

These actions, which together supported by the higher earnings helped the sector to even bolster and stay well above the minimum capitalisation levels measured by the RBC, providing them the capital heft required to withstand the unforeseen future shocks.

Meanwhile the expected increase in interest rates in the economy after the August 2021 policy rate hike is also expected to bode favourably for the sector as it will result in higher investment returns and thereby higher profits for the life insurers who hold well over third of their assets in government securities.

Besides, the rising interest rates would also result in potentially lower transfers to life insurance fund due to higher discount factor used to value the fund resulting in higher profits, as there has been a negative correlation established between the change in insurance contract liabilities and the 5-year average treasury bond rate.



(1) First Capital Research - Life Insurance sector report dated June 22, 2021

While the immediate future prospects of the non-life insurance business are largely contingent on how soon the import restrictions on vehicles are lifted and how soon the broader economy is unshackled from the virus induced restrictions, this segment is nevertheless primed to grow in the medium term in lockstep with the expected renaissance in the business and personnel incomes as higher incomes will prompt people to seek cover for their numerous assets from their factories to business establishments to homes and other assets and valuables to one's health from unforeseen events and adversities.

On a further positive note, given the confined ability to grow their motor insurance business in the near term, the general insurers could increasingly explore the options to grow their share of non-motor insurance businesses to either offset or at least to blunt the adverse impact coming from motor insurance.

Besides what was cited above, the limited fiscal headroom has for continuation of State pension schemes, under-funded retirement savings funds, vast gaps exist in social security needs due to a large majority of the workforce falling outside any type of social security net and emerging new life styles have offered a vast potential for the country's insurance fraternity to become more innovative and penetrate into the market in the period ahead.

In this backdrop, following section will look at how the insurance sector performed from 2020 through 1Q'21 through the lenses of key performance indicators as cited above.

1. Combined Gross Written Premiums improve the top line

The Gross Written Premiums (GWPs), the mostly watched gauge for the insurance industry's health continued its ascent at double digit levels during the first three months of 2021 over the corresponding period in 2020.

However, the behaviour between life and non-life segments went in the opposite directions, mirroring the industry conditions in the pandemic's aftermath which disproportionately favoured the long-term or life insurance business.

The broader insurance industry reported a combined GWP of Rs.57.42 billion in the three months to March (1Q'21), logging a 14.36% growth over the same period in 2020.

However almost entirety of growth was brought in by the life insurance segment of which the GWPs soared by an impressive 34.13% over the corresponding period last year to Rs.29.16 billion, reflecting the continued momentum in seeking life protections with the heightened risks brought about by the pandemic.

Life Insurance

While directly not comparable, the 1Q'21 growth came in at more than double the rate at which the life GWPs grew during 2020 which was 15.98% to Rs.102.97 billion.

In fact most notably the GWP growth during 2020 and 1Q'21 also reversed the decelerating trend observed in the life insurance business in the last few years, with the 2020 growth featuring as the second highest annual growth rate in the last five years.

1Q'21 performance also corresponded with the period which the economy returned to a brief near normalcy after the dissipation of the virus and the related restrictions where the people splurge on everything from staples to discretionary to high ticket value items.

And the exponential growth in the life premiums during 1Q'21 signals that life insurance continues to feature in people's shopping list reflecting that it is gradually becoming a necessity irrespective of the conditions of the economy or the direction of the virus after its initial outbreak ignited the need for serious life protection.



The rise in GWPs in this segment was also supported by the considerable rise in the Decreasing Term Assurance (DTA)/Mortgage Protection Policies which grew due to increased number of loans granted by the banks and financial institutions in response to descending interest rates.

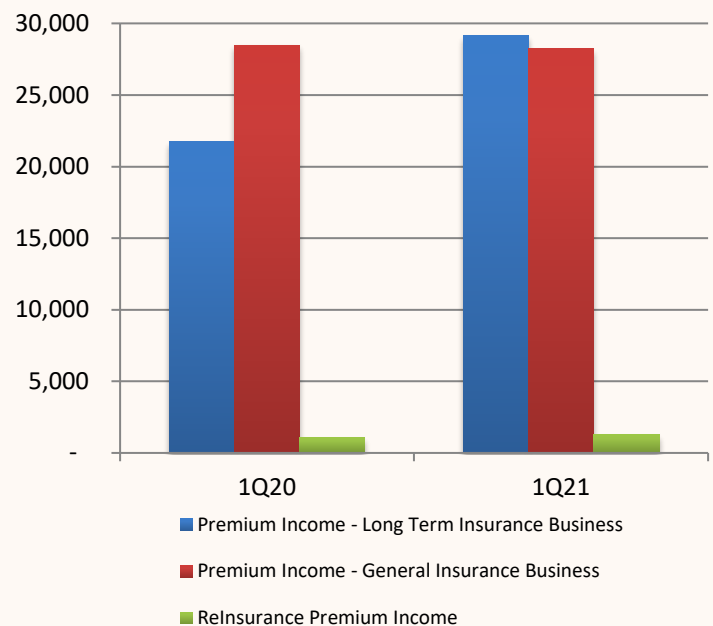
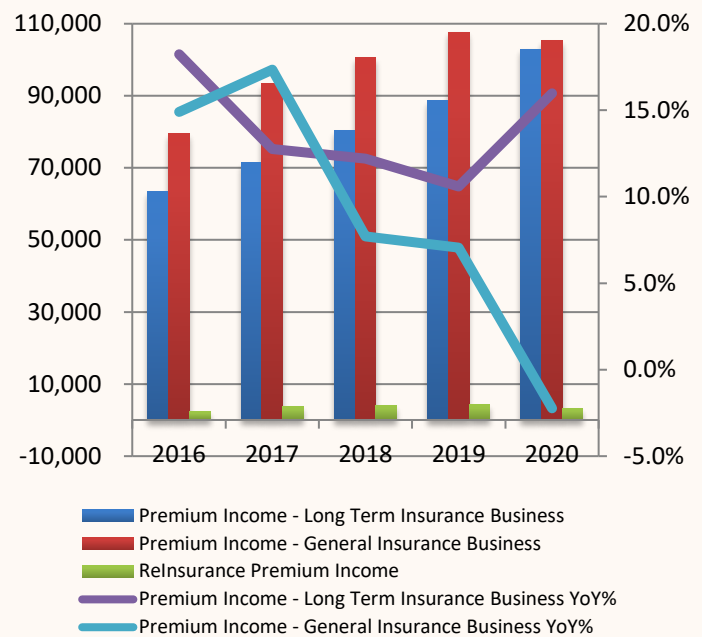
For instance, the sum insured under term insurance which captures mortgage protection policies and also provides a proxy for GWP growth showed a surge of 34.26% in 2020 to Rs.1,557.87 billion predominantly due to increasing DTA business under group DTA policies of one life insurer. Whereas, term insurance accounted for 30.93% of total sum insured under long term insurance, becoming the second largest category of policies, after policies referred to as, 'others'.

Sri Lanka's life insurance industry remains intensely competitive with 13 long term insurers, out of which 04 operate with collaborations with foreign insurers. Besides, there are 02 composite insurers who engage in both life and non-life insurance. They are the State owned Sri Lanka Insurance Corporation Limited and MBSL Insurance Company Limited.

Based on the company-wide data available only through 2020 end, Ceylinco Life Insurance Limited continued to dominate the industry based on GWPs with a 21.44% share, followed by Sri Lanka Insurance Corporation Limited with a 18.70% share of total industry GWPs.

The meteoric rise in the Softlogic Life Insurance PLC which consistently maintained a double digit growth in GWPs during the last five years brought them to the third spot in respect of market share with a share of 15.21%, displacing the third and fourth places held by AIA Insurance Lanka Limited and Union Assurance PLC respectively

Softlogic Life increased its GWPs by a robust 24.97% in 2020, surpassing the industry growth of 15.98%.



Premium income & growth rate of the insurance industry through 2020 & 1Q'21 (Rs million)

Source : IRCSL



General Insurance

As highlighted earlier, general insurance business fell casualty to the conditions created by the pandemic as lockdowns, restrictions on mobility, disruptions to broader businesses and the resulting erosion of business and personal incomes had a bearing on their affordability and thereby the segment GWPs.

The general insurance GWPs which declined by 2.24% during 2020 to Rs.105.28 billion, again slipped by a negligible 0.77% during the 1Q'21 compared to the same period in 2020 to Rs. 28.26 billion.

While the 2020 decline in general insurance premiums were predominantly caused by the motor insurance, the 1Q'21 premiums were weighed down by the sharp fall in the health insurance premiums, followed by the reduction in motor insurance premiums.

While it was abundantly clear for motor insurance premiums to falter due to the ban in place on the vehicle imports, slump in the health insurance premiums by as much as 24.42% between the two periods to Rs.3.57 billion in 1Q'21 defied the logic.

Health insurance sub-segment reported 12.70% growth in 2020, making perfect sense when the pandemic brought in novel risks to one's health and the escalating general healthcare costs. This growth helped the health insurance sub-segment to increase its share in the general insurance portfolio to 17.76% in 2020 from 15.41% in 2019, cementing its position as the second largest sub-segment.

Nevertheless the 2020 growth in the health insurance sub-segment came in at below the 2019 growth of 17.17% and, in 1Q'21 fire insurance segment displaced health insurance as the second largest insurance class..

Meanwhile the motor insurance sub-segment which accounts for 56.9% of the total general insurance market recorded a premium income of Rs.16.08 billion in 1Q'21, marking a slippage from Rs.16.22 billion in the year earlier period.

The narrower decline during 1Q'21 compared to the 3.91% contraction witnessed during FY2020 was a reflection of the travel and broader economic activities returning to a brief normalcy during the first three months of 2021. Despite the declines seen in health and motor insurance sub-classes, other insurance classes such as fire, marine and other categories reflected an increase in tandem with the recovery in general business and factory activities which operated with their full capacity.

For instance fire insurance premiums rose by a robust 15.90% to Rs.3.79 billion in the 1Q'21 compared to the same period last year.

General insurance segment is equally competitive with 12 players operating in the market with the 02 composite insurers. According to granular data available only up to 2020 on individual company performance on GWP, except for 3 insurers, all other general insurers had performed well on their GWPs notwithstanding the headwinds.

Based on such data Sri Lanka Insurance Corporation Limited clinched the top spot with a share of 18.40% from Ceylinco General Insurance Limited which had a share of 17.74%. Allianz Insurance Lanka Limited's share of the market fell to 13.16% in 2020, albeit retained its third spot, from a share of 16.80% in 2019 due to the loss of premium income from 'Suraksha' student insurance scheme of the government which they had in 2019 and the impact the pandemic had on its business.



2. Investment Income reflects hunt for yields amid falling G-Sec yields

Investment income which forms the second largest stream of income for insurers behind GWPs saw a mixed performance between life and non-life insurance segments similar to GWPs, albeit both segments saw them reallocating their investments into high yielding assets in search of higher returns when the interest rates descended to historical lows.

For instance while the bulk of the investments were continued to be held in government securities, both as a need to comply with the regulatory requirement and also to maintain liquidity while minimising risks in the market, there was a shift observed within the portfolio towards equities, corporate debt and particularly unit trusts to take advantage of the higher equities yields and to seek short term investments with better investment yields.

After logging an increase of 6.97% in investment incomes to Rs.46.94 billion in 2020, the life insurance segment expanded its investment incomes by an exponential 34.46% in 1Q'21 to Rs.11.98 billion from the same period in 2020 due to aforementioned reasons.

For instance investments in government securities continued to increase with the growing assets, which accounted for nearly 45% of the total investments or Rs.232.08 billion, as opposed to the regulatory mandated 30%, allocation to equities surged by 55.84% to Rs.35.05 billion from a year ago.

Further the life insurance industry had Rs.123.84 billion in investments in corporate debt, an increase of 16.75% from the same period last year and the investments in unit trusts more than doubled to Rs.14.13 billion in 1Q'21 from Rs. 6.59 billion a year ago, reflecting the said shift.

As a result of healthy growth in assets, during 1Q'21 total life insurance investments rose by a robust 15.97% to Rs.518.36 billion.

As a result the life insurance investments had yielded 10.13% return in 1Q'21, up from 9.99% a year ago.

Meanwhile the non-life investment incomes slipped to Rs.1.81 billion from Rs.1.83 billion a year ago, registering a decline of 1.09%. Its investment mix mirrored the life insurance investment portfolio reallocation, albeit the growth in the total portfolio came in at just 5.86% to Rs.134.55 billion due to deceleration in the segment asset growth between the two quarters due to aforementioned pandemic induced conditions.

The general insurance investments yielded a 7.47% return in 1Q'21, slipping from 8.77% a year ago.



3. Insurance assets allocation largely mirrored investment mix

Insurance assets allocation nearly mirrored the investment allocation in the insurance industry where the bulk of the assets were in government securities followed by corporate debt and bank deposits, albeit the growth in the latter decelerated somewhat in response to the fast decline seen in the deposit rates while unit trust assets and assets allocated to equities advanced as highlighted earlier.

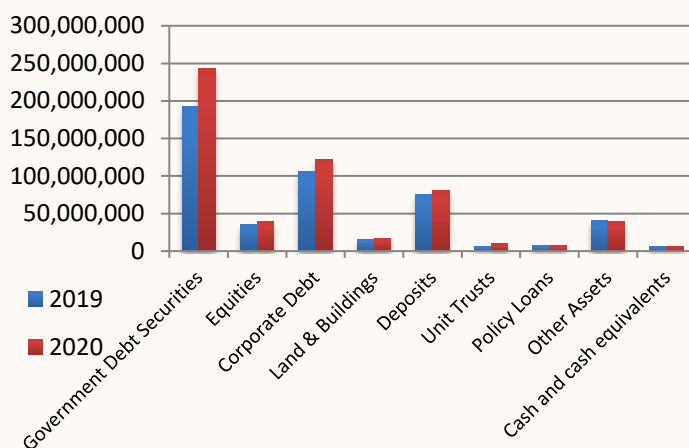
While the total insurance industry assets grew by 11.81% to Rs.798.09 billion by the end of 1Q'21 from a year earlier, the bulk of the growth was driven by the life insurance segment.

Continuing the momentum in 2020, the life insurance industry assets grew by a robust 15.03% year on year to Rs.585.51 billion by the end 1Q'21, out of which Rs.232.08 billion or 39.63% were in government securities. Such assets were up by 13.42% from a year ago.

Meanwhile there were Rs.123.84 billion in corporate debt, up 16.75% from a year ago while deposits held in banks were up by 5.71% to Rs.89.56 billion.

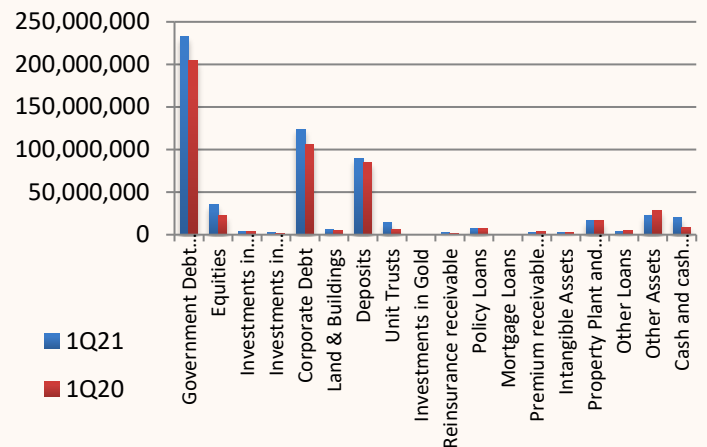
The trio together accounted for 76.08% of the total assets in the long-term insurance business by the end of 1Q'21.

Among the other assets, allocations into equities and unit trusts surged by proportions highlighted under the investments section above and besides, there was a notable increase in cash and cash equivalents to Rs.20.39 billion from Rs.9.20 billion a year earlier.



Long-term insurance asset allocation in 2020 & 1Q'21 YoY comparison (Rs Million)

Source : IRCSL

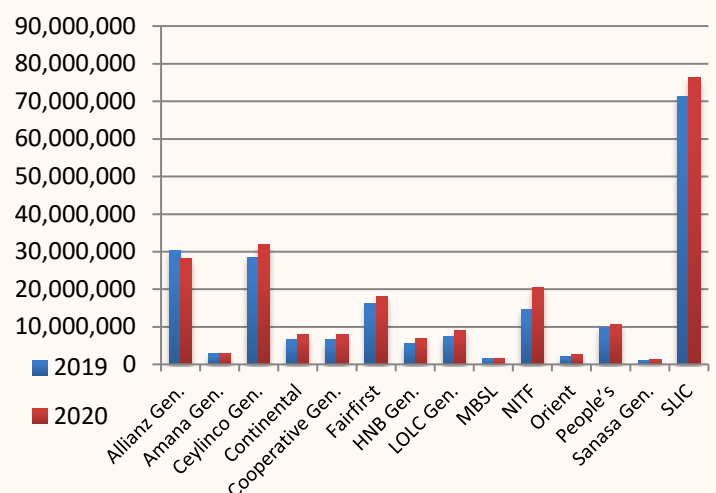


Long-term insurance asset allocation 1Q'21 YoY comparison

Meanwhile the general insurance assets rose by a modest 3.8% on year to Rs.212.6 billion through 1Q'21 reflecting the persistent subdued conditions prevailed for the non-life businesses since the onset of the pandemic.

While the government securities, bank deposits and corporate debt together accounted for 43.2% of general insurance assets, a notable Rs.27.6 billion or 13% of the assets continued to be premium receivables from policy holders and intermediaries, partly reflecting the relief that may have afforded to the policy holders affected by the pandemic.

Similar to long term insurance assets, allocations to unit trusts and equities under general insurance surged in search of optimising overall asset yields amid declining yields of other key financial assets such as government securities and bank deposits.



General insurance asset allocation during 2020 & 1Q'21 YoY comparison (Rs. Million)

Source : IRCSL

4. Claims and benefits paid in life and non-life insurance reflect a mixed outcome

Claims and benefits showed a mixed performance between life insurance and general insurance segments which became more evident due to the pandemic.

While life insurance claims continued to grow, the non-life insurance claims dropped sharply predominantly in response to the intermittent travel restrictions and below par business activity since the pandemic set off last year, resulting in less incidence for claims from motor vehicles and travel and tourism industries.

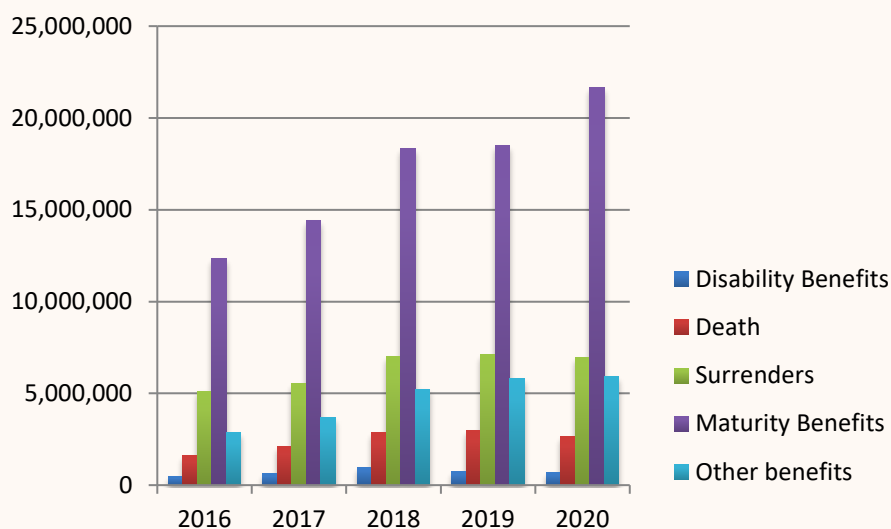
The life insurance claims and benefits which rose by 7.86% in 2020 to Rs.37.90 billion grew by a further 12.73% to Rs.9.83 billion in 1Q'21 from a year ago.

While the breakdown of 1Q'21 life insurance claims isn't available so far, the 2020 claims and benefits were mainly driven by maturity benefits which accounted for 57.17% of total claims that year, followed by surrenders which accounted for another 18.34%.

The claims incurred under the 'other category' consists of hospitalisation benefits, advance payments, interim payments, cash and loyalty bonus expenses, cancellations etc. The death benefits and disability benefits accounted for the balance claims and benefits.

An analysis of number of surrenders posted a sharp increase over 100% in 2020 due to DTA policies where customers rescheduled their loans taken from financial institutions in response to the fast decrease in interest rates. Therefore, people surrendered their existing DTA policies for new DTA policies which were taken for new loans.

Meanwhile the general insurance claims fell by 11.06% to Rs.10.5 billion in 1Q'21 from a year ago after registering a 26.88% plunge in such claims during 2020 to Rs.41.52 billion which brought down the overall general insurance net claims ratio to 49.16%, the lowest in five years, weighed down mainly by the slump in motor insurance claims., followed by health insurance.



Claims incurred by insurance companies - Long term insurance (Rs. Million)

Source : IRC SL



For instance motor insurance claims which accounts for the lion's share of claims under general insurance fell by 7.27% in 1Q'21 from a year ago, decelerating from last year's plunge due to the brief return of normalcy during the first three months of 2021 as mobility improved through the start of the new year holidays.

Further health insurance claims also took a dip by 15.12% to Rs.2.47 billion in 1Q'21 from the same period last year. Meanwhile there were slight improvements in fire and marine insurance sub-classes in 1Q'21, reversing the declines recorded in 2020.

5. Contrasting profitability outcome between life and non-life insurance

Profitability of the insurance business measured through Profit Before Tax (PBT) also took a mixed picture between long term and general insurance verticals during 1Q'21 which was opposite to how the two segments delivered profits during FY2020.

While the combined insurance business reported a robust 29.26% growth in PBT during 2020 to Rs.41.77 billion, the PBT of the long-term insurance business contracted by 17.89% to Rs.17.34 billion while the general insurance profits soared by 103.53% to Rs. 23.04 billion becoming the largest contributor to overall PBTs in 2020 for the first time.

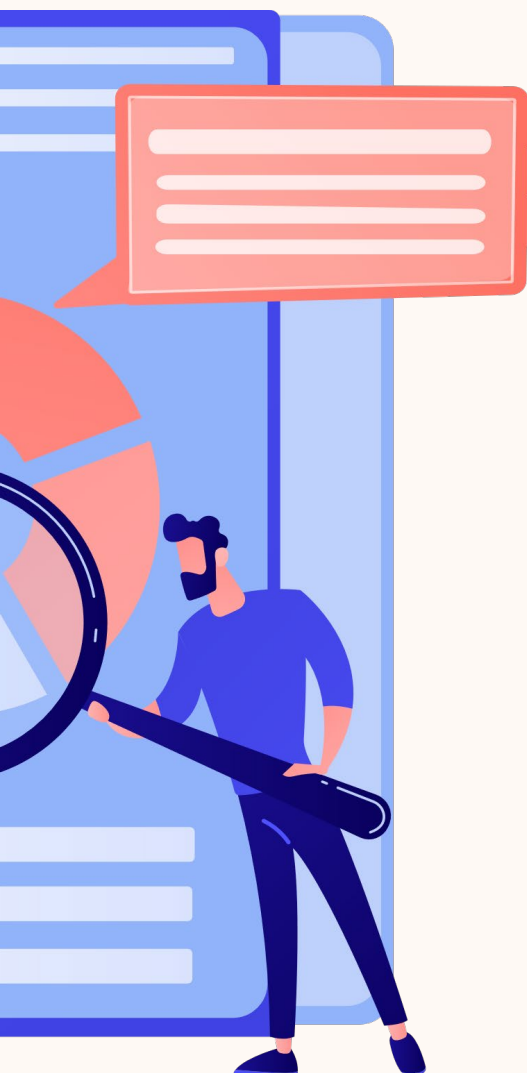
This divergence in PBT resulted from the decline in surplus transfers and higher claim provisions made by major long term insurers in the life insurance segment, while the higher profitability in general insurance was possible from the lower claims as highlighted earlier.

Conversely in 1Q'21, the life insurance PBT grew by 12.85% on year to Rs.4.04 billion while the general insurance PBT fell by 18.73% to Rs.3.21 billion from the same period a year ago.

Meanwhile the other profitability indices such as Return in Equity (ROE) and Return on Assets (ROA) demonstrated a better general insurance business at bottom line level than the life insurance business.

For instance ROE for general insurance business soared to 22.23% by end of 1Q'21 from 8.70% a year ago while the same for the life insurance business slipped to 13.62% from 16.28% a year earlier.

Meanwhile the ROA for general insurance surged to 10.48% in 1Q'21 from 4.01% a year ago while in the life insurance business it slipped to 2.97% from 3.64%.



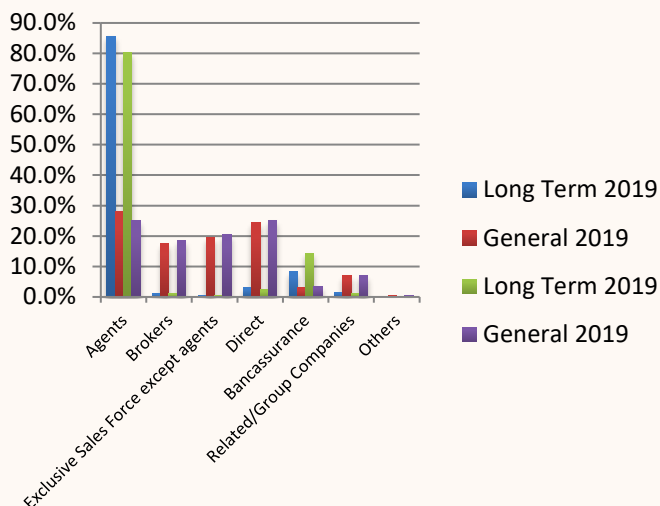
6. Pandemic adds a flywheel to digital adoption, driving expenses down

The profits of the insurance industry was also in recent years supported by the declining expenses which further received a tailwind from the pandemic induced acceleration of digital adaptation throughout the insurance value chain.

For instance the Management Expense Ratio which was declining from a peak of 53.5% in 2018 to 49.6% in 2019 further came down to 45.1% in 2020 (1).

By 1Q'21, this ratio further fell to 42.21% in life insurance from 45.72% a year ago in the life insurance business, mostly reflecting this ubiquitous use of digital platforms for on-boarding to customer servicing to premium servicing to claim handling since when the pandemic disrupted the conventional agency model.

There was a negligible increase in this ratio to 42.41% in general insurance segment from 41.21% a year ago due to the ease in premium incomes and investment incomes since last year.



Distribution channels of insurance companies

Source : IRCSL

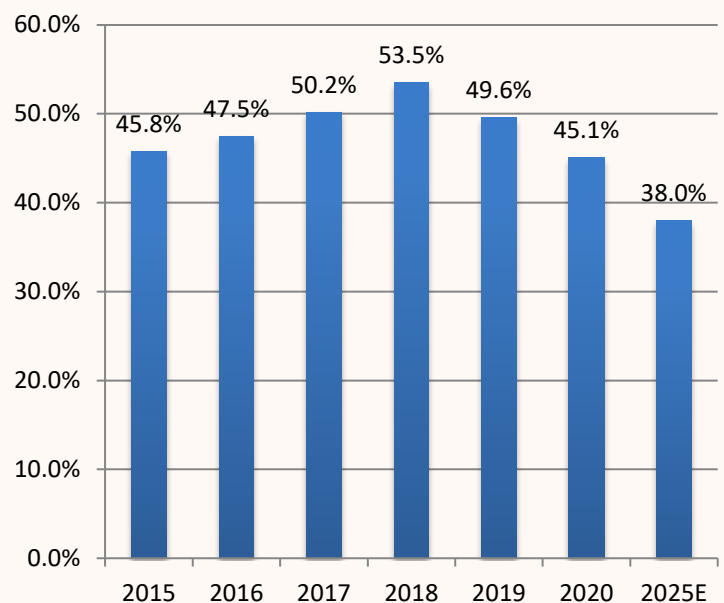
Even though these platforms will not completely replace the in-person agency model, digital platforms would form an integral part of courting new business as this will provide a viable option for those who prefers dealing remotely via online at the comfort of one's home or office and also serving the emerging new generation of clientele.

For instance agents' contribution to the overall GWPs generation in both life and non-life insurance segments have experienced declines during 2020, they continued to remain the dominant channels for generating GWPs, and this is particularly evident in the life insurance business. The share of GWPs generated by the agents population in the life insurance segment declined from 85.60% to 80.18% in 2020.

Further the investments in technology and information security by the companies would enable the staff to operate from a remote location, cementing a platform for most likely to be a hybrid work arrangement even after the pandemic wanes, taking further fat out from the companies' overheads.

Adoption of increasing amount of technology by the industry was not by choice but also a judicious approach since even prior to the pandemic to reduce costs in light of rising compliance cost and increased regulatory oversight on the sector. The pandemic did add a flywheel into their already embarked on journey towards digitising their sales force and exploration of the full potential of making the most of the technology in the company's operations.

The industry looks to have the potential to further bring down the ratio to 38% by 2025 as they consider the new normal powered mostly by technology which would become a potential game changer for the insurance industry in the post-pandemic era. ⁽¹⁾



Expense ratio

Past behavior in expenses ratio at life insurance business & future forecast

Courtesy : First Capital Research

(1) First Capital Research - Life Insurance sector report dated June 22, 2021

7. Insurance industry bolstered its capital levels further enhancing its solvency standing

Although the dour economic conditions set forth by the pandemic and its potential spill over effects on the insurance industry appeared to weaken its capitalisation levels, the industry in fact emerged with stronger capital buffers and thereby enhancing its solvency standing.

While the preemptive response by the regulator since the onset of the pandemic by way of suspending dividend distribution and other discretionary payments buttressed capital levels, the higher earnings of the sector further bolstered its capitalisation indices measured through Total Available Capital (TAC)* and Capital Adequacy Ratio (CAR)** stipulated under the Risk Based Capital (RBC) rules in place since January 01, 2016.

Meanwhile the regulatory mandated moratorium on premiums on all policy holders for three months also helped the industry to avoid potential policy lapses and fend off any undue pressure on the profitability and thereby the capitalisation of the industry.

Similar to BASEL III regulations in the banking sector which stipulate minimum capital adequacy ratios relative to their size in assets, the RBC attempts to ensure the insurers continuously maintain their capital relative to the risks inherent in their liabilities and the adequacy of their capital to withstand unforeseen shocks.

Under RBC framework for capital, the insurers are required to maintain their CAR above 120% level and a minimum TAC of Rs.500 million, the two barometers, both the industry and the individual companies are in achievement well in excess of their minimum levels by 1Q'21 as all life insurance companies and general insurance companies complied with minimum requirement a change from a year earlier where two life insurers didn't comply with the minimum requirement.

The life insurance industry as a whole reported its CAR at 342% by the end of 1Q'21, up significantly from 299% a year ago. It is largely expected that the growing life insurance profits supported by the new found interest for life insurance policies and increased penetration levels would support the life insurance companies to continuously stay well above the minimum CAR levels which provide them with the increased shock absorption capacity in case of future risks and unforeseen events.

Meanwhile the general insurance CAR rose from 214% to 249% between the two periods and by 2020 end all the general insurers had recorded a CAR above, in what is referred to as the, 'enforcement level' of 160 percent, likely referring to the elevated minimum requirement enforced by the IRCSL over and above the minimum stipulated level of 120%.

According to the statistics available up to December 2020, the TAC of the life insurance industry grew by 13.46% or Rs.29.66 billion in total to Rs.250.02 billion.

In general insurance, the industry TAC grew by 18.82% or Rs.10.30 billion to Rs.65.04 billion in 2020 but more granular level analysis of the individual companies showed, again except for one insurer all others achieved their TAC.



(1) First Capital Research - Life Insurance sector report dated June 22, 2021

* TAC is measured through the addition of Tier I and Tier II capital and subtracting the deductions mostly comprising of intangible and illiquid assets that are not generally available for covering losses.

** The cumulative of the capital required to address all relevant and material categories of risks such as credit risk, concentration risk, market risk, reinsurance risk, liability risk and operational risk.

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KPMG is one of the largest professional services firms in Sri Lanka and is also the oldest Chartered Accountancy firm in the country spanning over a century since inception in 1897.



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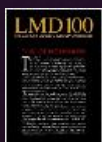
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2018 Oracle ERP Partner of the
Year 2018 Oracle SCM Partner
of the Year 2018

Our Impact Plan

Our Impact Plan clarifies our commitments and actions across four important categories: planet, people, prosperity and governance.

Planet

Decarbonization —

We are committed to achieving net-zero carbon emissions by 2030.

Carbon reduction Net carbon emissions per full-time equivalent Ahead of 2016-2020 target of a

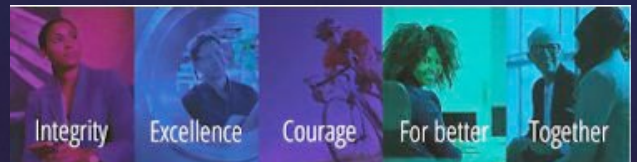
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2016–2019 13% 10% reduction

Renewable energy

2019 energy from renewable sources 57% On track to beat 2020 target of 60%

Governance

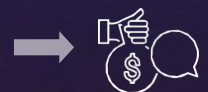
Our Values lie at the heart of the way we do things. To do the right thing, the right way, always.



Our commitments

Act lawfully, ethically and in the public interest.

Work against corruption in all its forms, including extortion and bribery.



As part of The World Economic Forum's International Business Council, KPMG has been part of a taskforce developing universal and material ESG metrics.

Prosperity

We passionately believe that the work we do for clients should also be good for our people, our communities and the world at large.

Community investment

KPMG is committed to supporting education and lifelong learning and is a founding members of UNESCO's Global Education Coalition to help scale up distance learning solutions to ensure no child is left behind.

*USD in millions

\$79 Cash contributions from KPMG firms, their partners
\$17 Volunteering activities
\$16 Other (including management costs)
\$12 Pro bono engagements

\$124
Total community investment value

Number of hours '000s

81 Pro bono engagements + 395 Volunteering activities = 476 Total community investment hours

Community investment data based on information received from KPMG firms with annual revenues over US\$100 million.

KPMG Service Offerings



Audit

High quality, independent financial statement audits are essential to maintaining investor confidence.

Our audit professionals are committed to the public interest. They seek to challenge assumptions and unlock valuable insights based on a thorough understanding of an organization's business and industry, and innovative audit methodologies and approaches.

Understanding the financial performance of any business must be placed in the context of strategic priorities, risk appetites and competitive positioning. Our technology-enabled audit approach applies extensive data analytics to provide the necessary evidence confirming that critical controls and disclosures uphold the highest level of integrity.

- Audits of financial statements
- Audit-related services
- Audit data & analytics
- Accounting Advisory

Management Consulting

Our high capability teams offer deep industry and technical knowledge, and market-leading tools to deliver solutions across every business and industrial sector.

Our consultants assist clients to make better decisions that may reduce costs, enhance organizational effectiveness and develop appropriate technology strategies.

- People & Change
- Customer & Analytics
- Financial Management
- Operations
- Strategy & Economic Advisory
- IT Advisory
- Supply Chain

Risk Consulting

Our risk consulting practice combines the knowledge and expertise of over 50 partners, directors and professionals. We help organizations transform risk and compliance efforts into competitive advantage by applying a risk lens to corporate strategy. This improves risk intelligence and decision making, protects financial and reputational assets, and enhances business value.

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- Business Process Management
- Accounting Advisory Services
- Internal Audit & Risk Compliance

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Our experienced investment professionals skilfully assess how opportunities to buy, sell, partner, fund or fix a company can add and preserve value. Our teams combine a global mind-set and local experience with deep sector knowledge and superior analytic tools to support clients. From assisting to plan and implement strategic change to measurably increasing portfolio value, we deliver tangible results.

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- Corporate Restructuring
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- Mergers, acquisitions and restructuring
- International tax services
- Transfer pricing
- Tax management consulting
- Global mobility services
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