Blockchain: from hype to reality

The potential of blockchain has been the subject of much debate in the reinsurance world, but it is about to bring concrete benefits to early adopters, says David Edwards of ChainThat.

Eight years ago, the writer Malcolm Gladwell described a tipping point as “the moment of critical mass, the threshold, the boiling point” when ideas or products take off and move from the periphery of one’s experience to become ubiquitous.

That moment is approaching for blockchain, as it moves from pilot phase to securing and streamlining reinsurance transactions and delivering savings and efficiency for the benefit of all.

The main challenge to innovation is not technology but governance and, particularly, securing the consent of the multiple parties to a reinsurance agreement. However, the logic of blockchain will persuade even slow adopters to embrace it.

It is widely recognised that the current means of transacting reinsurance are far too expensive, involving high frictional costs that are underpinned by poor quality data. Many brokers, insurers, reinsurers and managing general agents are using legacy IT systems resulting in data being duplicated multiple times across a number of different systems. The current methods means there is no single version of the truth or process upon which all parties in a transaction can rely.

Another consequence of this is that there can be lengthy delays in the reconciliation process leading to cashflow strains. As soon as a transaction is executed, a business should have a reasonable expectation of being paid, but with so many parties inputting information, it can take anything from 30 to 120 days for reconciliation and cash settlement.

The Blockchain Insurance Industry Initiative, aka B3i, has estimated that a move to block-chain—a single, secure distributed ledger platform accessible to all parties in a financial transaction—would take up to 30 percent of the frictional costs out of writing reinsurance business. Based on our discussions with market players, that number seems reasonable. Lloyd’s of London in 2017 posted a combined ratio of 114 percent and an aggregated market pretax loss of £2 billion

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($2.6 billion). We estimate that reinsurers using blockchain could save 30 percent in expenses and shave 10 to 12 percent off the combined ratio.

At a time of extremely challenging global market conditions, the substantial efficiencies and cost reductions which blockchain could deliver could mean the difference between reinsurance centres such as London being profitable or making a loss.

Earlier this year R3, a global leader in blockchain for financial services, and ChainThat produced a study which estimated that blockchain could deliver annual operational cost savings to the global reinsurance industry of 10 to 25 percent—or $20 billion to $50 billion.

Irresistible savings

In May, EY launched Insurwave, the first application of blockchain in insurance. Insurwave is supported by Willis Towers Watson, XL Catlin and MS Amlin and it will be used to manage the insurance of the Maersk fleet. It is expected that it will support more than half a million automated ledger transactions and help manage risk for more than 1,000 commercial vessels in the first year.

By connecting participants in a secure, private network with an accurate, immutable audit trail and services to execute processes, the platform establishes a first-of-its-kind digital insurance value chain.

Insurwave, like ChainThat products, uses the Corda platform which will ensure that different blockchains will be able to communicate with each other as the technology spreads.

The next proving ground for blockchain is likely to be reinsurance facilities. Facilities offer a perfect testing ground for blockchain because the current mode of operation includes a range of inefficiencies such as multiple sources of data and a range of interpretations of contracts.

These issues are compounded if we bring claims into the equation. If the customer has multiple geographical exposures, the parties must also consider tax calculations, which further complicates reconciliation.

ChainThat’s Facilities application supports the placement and negotiation of a facility contract and its terms between broker and a panel of re/insurers and then supports the placement of individual risks under the facility’s terms with that panel. This provides a comprehensive and flexible solution that supports the broker’s and the carriers’ needs for sharing and coordinating data within these facility-type arrangements.

The application is ready to be configured to individual facilities that will create a competitive advantage for early adopters. As facilities normally have a restricted number of parties, such as a broker and three carriers, it is much easier to organise the governance of a blockchain.

The cost is low and time to market is significantly fast. We hope that the successful operation of a facilities blockchain will show the immediate benefits to all the parties, and persuade more insurers that the greatest danger for them is missing out.

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