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COVID-19 pandemic shifts InsurTech investment priorities

Funding remains robust, but concentrated on those bolstering virtual customer engagement and operational efficiency

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Key messages

Despite the COVID-19 outbreak and the pandemic's economic fallout, total InsurTech investment through the first half of 2020 appears as robust as it was last year, when funds raised reached record levels.

However, investment was heavily concentrated in a relative handful of InsurTechs, while many may struggle to raise additional capital given ongoing disruption in the economy and shifts in the industry's needs and priorities.

The pandemic has prompted many insurers to accentuate their digital transformation efforts and seek InsurTechs that can help accelerate virtual interactions in sales and claims, as well as reduce expenses.

Attention is also expected to shift toward InsurTechs that can provide insurers with more comprehensive, holistic offerings rather than single-point solutions that need to be integrated by the end-user.

InsurTech funding nearly even with 2019's record pace, but bar being raised for funding

The amount of money invested in InsurTechs during the first half of 2020 remained remarkably robust at nearly $2.2 billion, despite the economic fallout and general uncertainty prompted by the COVID-19 outbreak, according to data collected by Venture Scanner and analyzed by the Deloitte Center for Financial Services.

However, while Venture Scanner's data indicates that the sector appears to be on track to generate at least the second-highest amount of money raised for any given year, the top 10 InsurTechs received the lion's share of available capital, leaving the rest of the InsurTech community to compete for about one-third of total funds invested.

In addition to all the trends we identified from Venture Scanner's database (which forms the basis for all our statistics and quantitative analyses in this report), in June and July we interviewed senior executives at venture capital (VC) and private equity (PE) firms, as well as accelerators specializing in this segment. The consensus from the interviews was that most InsurTechs may struggle to raise additional rounds of financing well into next year. Interviewees added that priority will likely be given to those addressing the most pressing digitization and operational efficiency challenges faced by insurers hurriedly adjusting to the post-pandemic world, both internally and externally.

In any case, speed would appear to be of the essence. "Insurers are looking to achieve in three months in digitization what they thought would take three years," said one London-based InsurTech investment firm executive we interviewed, citing the urgency created by the industry's nearly overnight transition to remote staffing, as well as the rapid virtualization of customer engagement in sales and claims.

There were a number of leaders inside insurance organizations that were resisting streamlining labor and automating systems and processes, observed one US-based VC firm executive, who added that "now there seems to be renewed vigor to really question the status quo and think about getting leaner and more efficient."

Pandemic shifts insurer, investor priorities

Given these extraordinary circumstances, InsurTechs with ready-to-use solutions to help overcome operational challenges and speed up digitization efforts were cited by those we interviewed as being much more likely to get funding in the short and medium term. "Insurers and investors are recognizing that process improvement may not be the most headline-grabbing form of innovation, but companies need that more now than something that might be transformative years from now," said another US-based VC firm interviewed. "While there is a hesitation to let go of long-term initiatives completely, in the near term it's going to be a capital allocation question."

Another VC executive said most insurers are "more eager to consume relevant InsurTech offerings that are ready for prime time now." Such offerings likely include those facilitating automated underwriting, online distribution via digital managing general agencies and direct sales, as well as virtual claims management.

Some of the uptick in investments that could be of more immediate help to insurers might not even be showing up on Venture Scanner's InsurTech dashboard, according to those interviewed. One example cited is the rising importance of healthtechs supporting telemedicine, which is helping bolster workers' compensation claims management, from diagnosis to treatment to status monitoring.

"Portfolio triage" underway as many investors tighten targets

Many VC firms are in the middle of what one interviewee characterized as "portfolio triage," determining which of their investments may be best positioned to help insurers adjust to the pandemic's impact sooner rather than later.

Many InsurTechs developing solutions outside the industry's newly emerged priorities will likely be operating in what one investor group called "survival mode," looking to manage cash reserves and "extend their runway" until crisis conditions ease up and insurers can return their attention to less immediate needs. Some may seek to sell to or merge with other InsurTechs to combine resources and eliminate duplication in the market.

Another major selling point for InsurTechs seeking investment and end-user interest going forward will likely be the ability to provide broad rather than narrowly focused support. "VCs are going to get tougher or change strategies to bridge together adjacent solutions to realize the entirety of a customer's needs, rather than leaving it to the insurer to integrate point solutions piece by piece," the London investment firm asserted.

This could also spur greater merger and acquisition activity, as InsurTechs combine to enable consolidation of individual point solutions into a more comprehensive suite of products. Meanwhile, legacy carriers may be on the lookout for acquisition candidates to import new capabilities and specialized talent from undercapitalized InsurTechs.

Pandemic upends on-site pitches

COVID-19 has also undermined the interpersonal interaction facilitating InsurTech financing. One accelerator we interviewed noted that the pandemic has cut down dramatically on live pitches for individual investors, while most in-person national and international conferences have either been postponed or gone virtual. These were among the opportunities for investors and startups to meet and become better acquainted, as well as negotiate financing deals face-to-face, that may no longer be available for the time being.

One online brokerage InsurTech told us that "building relationships remotely is tough, especially when you're asking someone to give you lots of money. I'm not sure anyone has a good solution for that right now, so it's likely future deals will just run a lot slower."

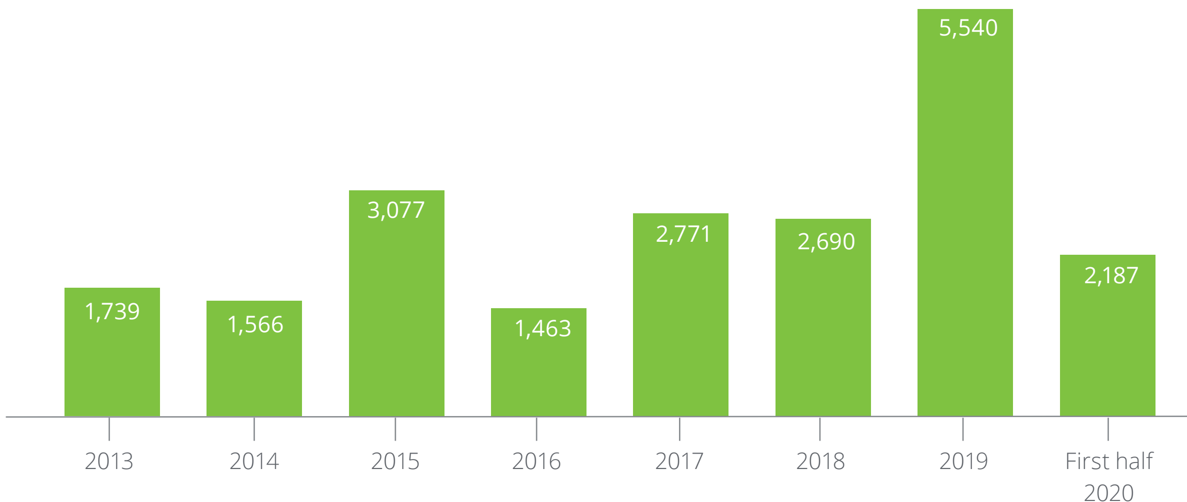
Yet others noted that deals can still get done, despite the loss of what was characterized by one accelerator as "often just innovation theater." The industry-wide adoption of collaboration software has enabled many InsurTechs to engage with potential investors despite the pandemic—including those who may not have had the time to travel to see everything being offered and everyone behind the many startups seeking capital.

InsurTech by the numbers

Concerns that the economic fallout of COVID-19 might prompt skittish investors to cut back on InsurTech financing in 2020 may be somewhat alleviated by first-half data collected and reported by Venture Scanner.

Despite a massive rise in unemployment, a flip to negative GDP, and volatile capital markets, InsurTech investments in the aggregate appear to be as robust as ever. Investment of nearly $2.2 billion recorded by Venture Scanner going to 67 InsurTechs during the first half puts the sector well on track to finish with at least the second highest amount ever, easily topping the $2.7-to-$3.0 billion full-year figures recorded for 2015, 2017, and 2018 and perhaps even approaching 2019's record of $5.54 billion. (See figure 1.)

Figure 1. First-half 2020 funding puts InsurTech on track for at least second-highest annual total

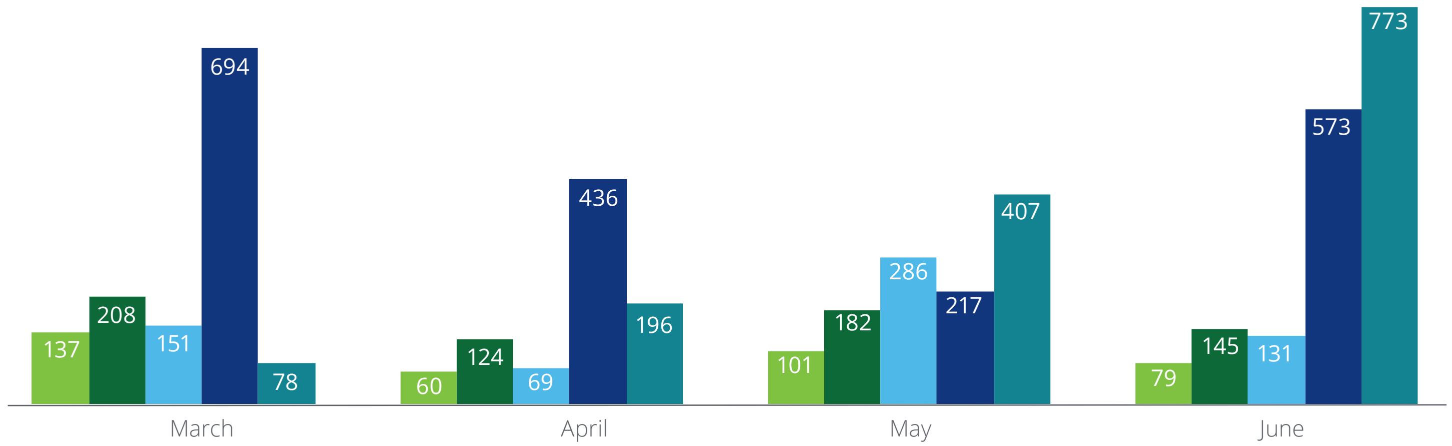


InsurTech funding in US$M (2013-2020)

Source: Venture Scanner data; analysis by Deloitte Center for Financial Services.

It was touch-and-go for a while. First-quarter investments were down slightly—mainly because of a precipitous decline in March, when the COVID-19 outbreak reached the United States, prompting lockdowns, business closings, and a nosedive in the US stock market. This is significant, because 75% of the funds raised in the first half, as recorded by Venture Scanner, were invested in US InsurTechs. Yet second-quarter investment was actually higher overall, Venture Scanner data showed, despite dropping more than 50% in April compared with the same month a year earlier. Investment bounced back strongly after that, nearly doubling May 2019's figure and climbing about 40% year-over-year in June to pull the first half about even with 2019 levels. (See figures 2 and 3.)

Figure 2. Global InsurTech investment plummets when pandemic hits the United States in March and April, but rebounds strongly in May and June

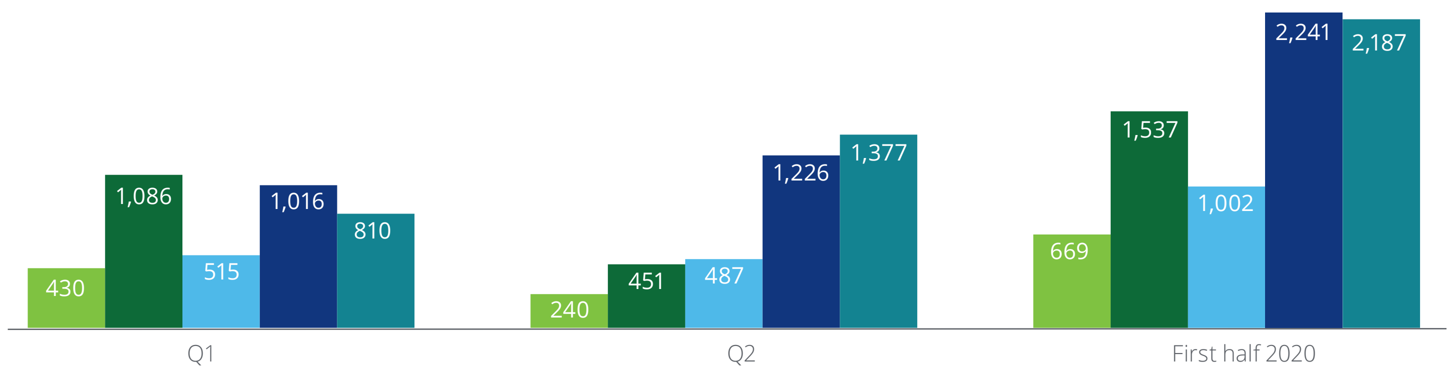


March to June - Funding in US$M

2016 2017 2018 2019 2020

Source: Venture Scanner data; analysis by Deloitte Center for Financial Services.

Figure 3. Higher capital raising in May and June drew first-half 2020 funding nearly even with 2019



Q1, Q2, and first-half funding in US$M

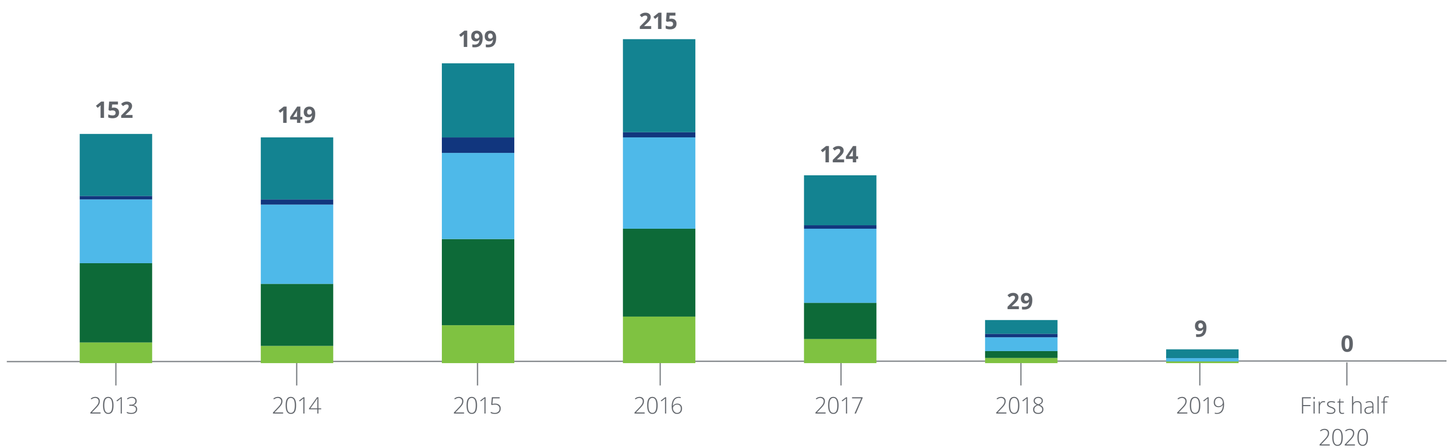
2016 2017 2018 2019 2020

Source: Venture Scanner data; analysis by Deloitte Center for Financial Services.

A deeper dive into the Venture Scanner data to see where all this money went, however, showed that most of the funding was concentrated among the top 10 InsurTechs, which accounted for nearly two-thirds of all dollars invested in the first half—with the top four dominating by drawing 44% of the total. Such concentration is not new (in the first half of 2019, the top 10 accounted for 53% of all funding), but it is accelerating, a phenomenon becoming more pronounced over the past few years, and described by more than one investor group we interviewed as evidence of an ongoing "flight to quality." In that context, all remaining InsurTechs were left to battle over essentially just one-third of the capital raised in the first half.

At least InsurTechs outside the top 10 did not have to compete for funding with brand-new startups, as no launches were recorded by Venture Scanner for the first half of 2020. Only 38 entities have been launched in the past three years following the hundreds of InsurTechs created prior to 2018, saturating the market with often duplicative prototypes. (See figure 4.)

Figure 4. New InsurTech launches fewer and farther between since 2017



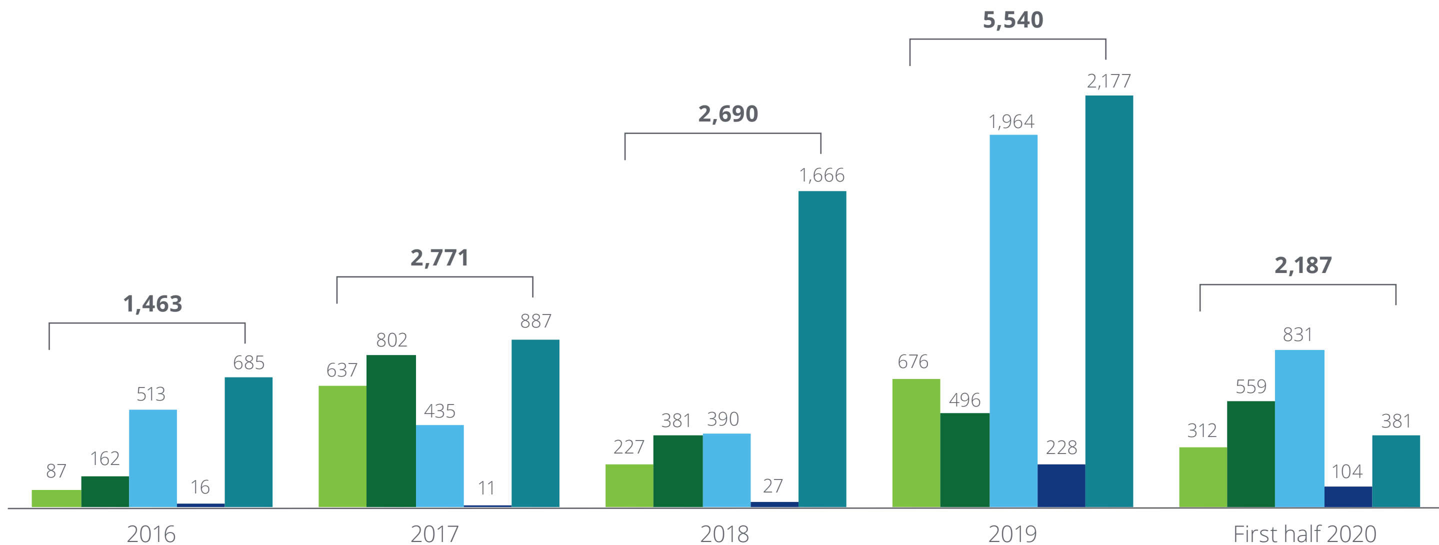
Launch by category (2013-2020)

Personal ins. | Ins. operations | Ins. customer aquisition | P2P ins. | Commercial ins.

Source: Venture Scanner data; analysis by Deloitte Center for Financial Services.

Indeed, the prevailing trend of investors and end-users focusing on InsurTechs that appear more likely to make a market impact sooner rather than later is likely being accentuated by rising demand for those ready to deploy and that meet recently emerging needs, particularly related to the pandemic.

Figure 5. Funding for InsurTechs in operations soars for second straight year, while customer acquisition already hits second highest total



Funding by category in US$M (2016-2020)

Commercial ins. | Ins. customer aquisition | Ins. operations | P2P ins. | Personal ins.

Source: Venture Scanner data; analysis by Deloitte Center for Financial Services.

InsurTech landscape changing with the evolving environment

In terms of funding by category (see figure 5), Venture Scanner data showed that investments in InsurTechs for operations led the way in the first half at $831 million, following 2019's full-year record total of $1.96 billion—which eclipsed the $1.39 billion invested in the prior three years combined. Insurer efforts to seek greater operational efficiency and cost controls are likely to remain high priorities given top-line growth challenges during the pandemic, with insurable exposures being undermined by the struggling economy while low interest rates hinder investment portfolio returns.

At the same time, Venture Scanner data showed that first-half investment in customer acquisition InsurTechs of $559 million is already higher than the $496 million invested for all of 2019. This likely indicates that insurers are keen to prioritize greater digital engagement with consumers, perhaps with the help of InsurTechs offering insurance comparison sites or support for direct-to-consumer sales. This at a time when face-to-face interaction between agents or brokers and their clients has been severely limited and may remain challenging for the pandemic's duration, and perhaps beyond, as buyer behavior changes.

Meanwhile, personal lines InsurTech investments recorded by Venture Scanner dropped substantially to $381 million for the first half—well below the levels seen over the past two full years. This is likely the result of saturation, as investors have poured nearly $4 billion into the segment to digitize and streamline auto and homeowners' insurance sales, distribution, and claims service.

Mergers and acquisitions could increase as capital tightens

InsurTech merger and acquisition (M&A) activity has thus far been in line with totals from the past few years, with eight deals identified by Venture Scanner in the first half of 2020 versus 18 for all of last year and 21 in 2018. However, with the industry's shift in priorities and greater urgency to provide integrated solutions, more InsurTechs may be seeking a safe harbor if they have trouble raising capital, either by combining with or selling to other InsurTechs, or perhaps legacy insurers.

"This couldn't be a better time for being forward-thinking and going on the offense," said one US-based VC. "While many InsurTechs may not get their follow-up round of financing, they might have a good team, solid customers, and strong intellectual property, and that's worth acquiring." A leading accelerator added that "the big will keep getting bigger" in InsurTech, with acquirers likely seeking smaller startups with good talent but not enough traction to draw additional funding on their own.

Consolidation may have been inevitable even if a pandemic hadn't disrupted the insurance market and economy, given the duplication of solutions competing in the market, according to a London investment executive interviewed—who wondered, for example, how many variations of chatbots the industry really needs.

Unique times create unique opportunities, which may explain why InsurTech M&A could play a critical role in post-pandemic business strategy for legacy insurers. Some will be more eager and better equipped than others to consider an InsurTech acquisition as carriers evolve their products, services, and capabilities to support significant systemic change across their customer base.

Most sectors and individual carriers may need to reinvent products and business models in order to thrive long term, and InsurTechs could help them do so, whether insurers serve as customers, investors, or acquirers. Insurers will likely need to explore a range of inorganic growth strategies, as well as de-risk their approach to M&A by broadening their activities to include partnerships with peers, co-investments, and cross-sector alliances based on fit. InsurTechs could play a very interesting role in filling gaps in market needs, as well as shoring up insurer operating models.

Yet even as their company's business model may be changing, insurance leaders should evaluate prospective InsurTech M&A deals based on their strategic fit, as opposed to bargain pricing. That fit should take into account the changes occurring within and across industries that have reframed strategic considerations in an insurance company's ability to pursue an M&A deal, whether doing so defensively or offensively. Insurers can deploy a revised set of strategic choice options and scenario-planning tools to help identify the new capabilities they require, prioritize the markets where they need to operate to safeguard their future and drive growth, and then identify which InsurTechs could possibly help achieve those goals.

Several InsurTech M&A patterns are likely to emerge over the next year or so, including the following:

- InsurTechs combining to eliminate duplication, scale costs, and bolster capital positions, as well as speed up development and implementation.
- InsurTechs looking to combine with those offering adjacent point solutions within or across portfolios so as to be more holistic and readily consumable by the industry.
- Legacy carriers acquiring InsurTechs to add capabilities and plug gaps in their organizations.

Where might InsurTechs, insurers, and investors go from here?

How innovative can insurers afford to be during the pandemic and subsequent economic uncertainty? It remains to be seen whether insurers will look to InsurTechs to help them do what they have always done, only faster and cheaper, rather than engage with them to rethink traditional operating and business models.

There is also concern that once the pandemic passes, insurers may simply default to the way they always have done business, rather than permanently transform how they operate and deal with customers for the long term.

One VC firm urged insurers to seize the opportunity presented by the pandemic-driven shifts in priorities and to "think bigger. Don't just digitize what you've always done and think you'll automatically be better off over the long term."

The challenge ahead is to reimagine how to engage with customers, generate additional revenue, control costs, launch new products and platforms, and deploy talent effectively in what promises to be an increasingly virtual, data-driven, and self-directed economy. InsurTechs will likely remain well positioned to help legacy carriers accomplish those goals, especially if internal innovation initiatives are sidelined as part of an insurer's expense management mandate in response to an uncertain economy.

Another VC firm noted that while some InsurTechs may not ultimately survive in this difficult environment, "at least we've still created a lot of digitally savvy people who want to transform the industry and are experienced in trying to do it. But insurers still need to figure out a way to attract such people, especially if they are entrepreneurs."

"Think bigger. Don't just digitize what you've always done and think you'll automatically be better off over the long term."

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