

Convergence of Banking and Insurance: Opportunities in Wholesale Financial Services

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Abstract

One of the most significant economic developments of the past decade has been the convergence of the previously separate segments of the financial services industry – particularly the banking and insurance sectors. Convergence has coincided with the increasing globalization of the financial services sector, and has been facilitated by the deregulation of financial markets. The development of dynamic financial markets for derivatives and other innovative securities as well as advances in computer, modeling, and telecommunications technologies also have accelerated convergence. An important factor driving convergence is the disappearance of traditional “safe-haven” markets and an increasing focus on shareholder value maximization by corporations worldwide. The resulting shift in focus towards enterprise-wide risk management solutions by both financial and non-financial corporations has created a growing demand for new risk management products. These developments provide opportunities for the traditional wholesalers of risk management products, particularly investment banks and reinsurers. The paper discusses the core competencies of banks and reinsurers and the factors needed for success in the evolving market. The discussion considers the merits of unbundling the traditional insurance value chain to create more responsive organizations and de-emphasize residual risk bearing by insurers and reinsurers. The paper also discusses innovative wholesale risk management products, including products that modify classic insurance and reinsurance product models but do not access broader capital markets and risk-linked securities that combine risks and investment features traditionally handled separately and access capital markets directly. The paper concludes that significant opportunities exist for investment banks to expand into insurance-linked securitization products and for reinsurers to expand into hedging risks not traditionally covered by insurance and reinsurance products.

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