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CAFII ALERTS WEEKLY DIGEST: August 16 – September 6, 2024

September 6, 2024

The CAFII Alerts Weekly Digest is intended to provide a curated compendium of news on insurance, regulatory, and industry/business/societal topics of relevance to CAFII Members – drawn from domestic and international industry trade press and mainstream media – to aid in Members' awareness of recently published media content in those areas.

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GOVERNMENT/LEGAL/REGULATORY/BUSINESS DEVELOPMENTS

Canada Needs An Action Plan To Combat Financial Scams Ahead Of Open Banking, Real-Time Payments

By Rita Trichur, The Globe and Mail, September 5, 2024

https://www.theglobeandmail.com/business/commentary/article-canada-needs-an-action-plan-to-combat-financial-scams-ahead-of-open/

Perhaps you've received a phishing e-mail from a purported Nigerian prince promising a big payout from his frozen account in exchange for a small fee and your banking information. Or maybe it was a text message urging you to click on a link because your debit card has been frozen or to accept a surprise e-transfer.

It seems fake fortune is smiling upon me, too. I recently received an e-mail alerting me to a deposit of $1,200 in my non-existent casino account and another offering me a lucrative investment opportunity.

"We are prepared to act as a silent partner, offering financial support while fully respecting your autonomy in managing the business," stated one e-mail. "Whether through an equity arrangement, joint venture, or loan, we are flexible in structuring the partnership to best suit your needs."

When it comes to financial fraud, we ain't seen nothing yet. Open banking and a new real-time payments network are coming to Canada, and they will provide criminals with new vectors for exploitation. That's why the banking industry is urging the federal government to combat financial fraud by implementing an anti-scam action plan that takes a multi-industry approach.

"This is a shared responsibility," the Canadian Bankers Association wrote in a recent submission to the House of Commons standing committee on finance. "Canadians, government, financial institutions, telecommunication companies, online platforms, technology companies, law enforcement, and the courts all have a significant role to play in this fight."

Sure, the CBA's recommendation is rooted in self-interest. But so what? The idea makes sense given what has already transpired in other countries.

"Australia's experience, for example, saw significant increases in scams following the launch of real time payments and consumer-driven banking, highlighting the need for proactive measures to mitigate these risks," the CBA stated in its submission.

Canadian fraud statistics are already staggering.

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Last year, there were 41,988 victims of fraud in Canada with total losses estimated at $569-million, according to the Canadian Anti-Fraud Centre. There have already been nearly 16,000 victims of fraud and $284-million in losses during the first half of 2024.

But that's likely the tip of the iceberg. The RCMP estimates that only 5 per cent to 10 per cent of frauds are reported by victims. As such, the CBA reasons that true losses could be as high as $11-billion annually.

The Department of Finance, which is consulting on various proposals to strengthen the financial sector, acknowledges that "everyone has a role to play in stopping fraud." But proposals outlined in its consultation paper are largely focused on banks.

Ottawa is mulling whether banks should be required to "prevent or delay transactions" that are suspected to be fraudulent and whether consumers should have the option of disabling the ability to conduct higher-risk transactions, such as wire transfers, on mobile apps or through online banking.

Sure, such changes ought to be examined. But the government must also think laterally because financial scams often involve other companies including tech platforms, wireless carriers and residential internet service providers.

Imagine what more could be accomplished if wireless carriers systematically alerted banks about phone numbers associated with known fraudsters?

Just think of all the text messages that consumers delete and voluntarily report as junk. Surely, that data could be put to better use.

To its credit, the government is examining how to increase transparency and accountability for financial fraud.

Canadians already benefit from some liability protections for unauthorized credit card and debit card transactions. But as the consultation document notes: "Bad actors continue to find new ways to perpetrate fraud to gain both unauthorized and authorized access to Canadians' money."

The government must think broadly about liability. Shouldn't tech companies, for instance, bear some of the responsibility for failing to protect consumers from financial frauds perpetrated over social-media networks, especially since some are also dabbling in peer-to-peer payments?

At least one banking chief executive argues they should.

"The majority of fraud starts online, specifically on social media, and it is high time that tech firms step up to protect people using their sites," wrote Robin Bulloch, CEO of Britain-based TSB, in an op-ed for The Independent earlier this year.

Ottawa is also considering introducing a maximum liability threshold for account holders who are victims of unauthorized transactions. But the idea is already proving controversial elsewhere.

British regulators, for one, walked back plans to force banks and other payment companies to refund fraud victims up to £415,000 ($738,000), The Financial Times reported this week. The maximum payout will likely be cut to £85,000, the

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newspaper reported, citing people familiar with matter. In addition to pushback from banks and fintechs, the story cited concerns that fraudsters would game the compensation system.

Canada must learn from the experiences of Australia and Britain. By all means, hold banks to account. But don't let other companies off the hook.

OSFI Asks For Feedback On Crypto Disclosures, Updates Operation Risk Guidance

Regulator Sets Out Some Of The Key Risks For Canadian Financial Institutions

By Steve Randall, Wealth Professional, August 26, 2024

https://www.wealthprofessional.ca/news/industry-news/osfi-asks-for-feedback-on-crypto-disclosures-updates-operation-risk-guidance/386810?hsmemberId=83982452&tu=&utm_campaign=&utm_medium=20240826&_hsenc=p2ANqtz-833RnhchAyYrPb-EXVAzylnUFyEqvLQEWtcaGRvSKMzh8caTnLrvgvv_QW97aYVoqTgXKHeHIKNgO5mySEPCRYLn6Daq&_hsmi=321691598&utm_content=&utm_source=

Canada's financial institutions regulator is seeking feedback on the regulatory framework of cryptocurrencies held by FIs and has published its final guideline on operational risk and resilience.

The Office of the Superintendent of Financial Institutions wants feedback from stakeholders on guidelines for federally regulated financial institutions to publicly disclose their exposures to crypto assets "to protect Canadians' savings and the security of our financial system."

It follows a consultation in November 2023 in parallel with the Basel Committee on Banking Supervision and new draft amendments to the Pillar 3 Disclosure Guidelines for domestic systemically important banks and small and medium-sized deposit-taking institutions for public consultation to incorporate the new BCBS disclosures standard.

OSFI has also published its final guidance E-21 on operation risk and resilience, revised with simplified language to make it clearer and better streamlined.

It follows on from OSFI's annual report highlighting the risks to FIs in May, which noted that the inflation target has not yet been reached and with current interest rates and market volatility continued higher borrowing costs, increased mortgage renewal/refinancing risk, decreased consumer spending and business investment can be expected.

OSFI states that today's financial institutions operate in a complex risk environment, with increasing risks to their operations from:

- internal control failures
- third-party disruptions
- infrastructure outages
- technology failures
- cyber and geopolitical incidents

- pandemics
- natural disasters

This requires robust risk management and resilience, the regulator states.

The new guideline:

- Enhances expectations for operational risk management.
- Sets new expectations for operational resilience, a vital component of OSFI's supervisory framework.
- Sets new expectations for business continuity risk management, crisis management, change management, and data risk management, which strengthen operational resilience.

While its annual report acknowledged opportunities ahead, such as the higher rate benefits for pension fund investment income and decreasing future liabilities, it also highlighted that "changing institution and consumer behaviour could have unexpected effects on actuarial experience, policy design, risk modelling, and other institutional decisions."

Household debt

Rising Canadian household debt was also noted in the annual report as a risk with mortgage payments taking a larger chunk of household income, and if the labour market weakens, "the effects on credit quality could be material, and the landscape could change dramatically."

With 76% of mortgages outstanding as of February 2024 due for renewal by the end of 2026, OSFI says Canadian homeowners could be in for a payment shock, especially if they took out their home loan when interest rates were lower between 2020 and 2022.

"We expect payment increases to lead to a higher incidence of residential mortgage loans falling into arrears or defaults," the report states.

FIs are also significantly exposed to wholesale credit risk especially from commercial real estate lending, but also from corporate and commercial debt. "Current interest rate levels have produced challenging refinancing conditions for some commercial and corporate borrowers and the conditions could negatively affect wholesale credit markets in the coming year," OSFI warns.

Also, liquidity and funding conditions "remain sensitive to an uncertain financial market landscape. The expected and actual path of global interest rates will influence the risk appetite of market participants."

Among other risks identified by the regulator are "threats to institutions' integrity and security ranging from fraud and money laundering to cyber security and foreign interference." This is exacerbated by technology, OSFI says, allowing for more sophisticated attacks on FIs.

The regulator will be closely monitoring how these risks and others could impact Canadian financial institutions in the months ahead.

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OSFI Releases Inaugural Quarterly Guidance

Industry Day Slated In September

By Terry Gangcuangco, Insurance Business, August 23, 2024

https://www.insurancebusinessmag.com/ca/news/breaking-news/osfi-releases-inaugural-quarterly-guidance-502685.aspx?hsmemberId=83982452&tu=&utm_campaign=&utm_medium=20240823&_hsenc=p2ANqtz-92NfBYfhdfsMejK5cHdJVUNO987imD9iaDmOa-uapL0wtLkSdZVspkF5w18ox8FdJ-KjECq1RmdraIvWq6XQKSHFWC8w&_hsmi=321409448&utm_content=&utm_source=

The Office of the Superintendent of Financial Institutions (OSFI) has released its first quarterly guidance. The new system, featuring four fixed release dates throughout the year, is intended to provide stakeholders with greater predictability.

Addressing several critical risks identified in OSFI's Annual Risk Outlook, the guidance includes the final Guideline E-21 on operational risk and resilience, updates to the LICAT (Life Insurance Capital Adequacy Test) guideline, and a consultation on the public disclosure of crypto-asset exposures.

Alongside these, OSFI has also published the 2024 Memorandum to the Appointed Actuary, which outlines the requirements for the appointed actuary report.

Meanwhile, OSFI is piloting its first virtual industry day, on September 5. The event will offer the industry the opportunity to learn more about the newly issued guidance and engage in a Q&A session. Stakeholders, who can choose which sessions to attend, are encouraged to register for the event.

The first session of the industry day in September will be a presentation on OSFI's policy review, followed by a discussion of the crypto-asset exposures, final Guideline E-21, and LICAT guideline.

Part of the new pilot approach to the way OSFI releases regulatory guidance, industry days will be held two weeks after each quarterly release. The next quarterly guidance release is scheduled for November 21, with another virtual industry day planned for December 5.

Superintendent of Financial Institutions Peter Routledge (pictured) noted: "By issuing policy releases on four set dates annually, we meet the request of regulated financial institutions that OSFI deliver more predictable and transparent releases of our regulatory guidance. Our measured, principles-based approach to regulatory guidance will remain responsive to OSFI's key risks."

OSFI publishes guidelines to regulate and supervise federally regulated financial institutions, aligning with the current and emerging risk landscape.

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OTHER CAFII MEMBER-RELEVANT NEWS

Engaging Millennials And Gen Z: The Life Insurance Conversation Advisors Must Start

Understanding Younger Generations' Unique Needs Can Unlock New Possibilities

By Co-operators, September 06, 2024

https://www.insurancebusinessmag.com/ca/news/life-insurance/engaging-millennials-and-gen-z-the-life-insurance-conversation-advisors-must-start-504148.aspx?hsmemberId=83982452&tu=&utm_campaign=&utm_medium=20240906&_hsenc=p2ANqtz--BI1p1eCkKRhIAPunY_NqN2pe5sz9Zp88q8mYKhaExtBhmJQqwrGBvXYHaTvEwlBlhNSKprVAKGqnWrQOVZtYn57Z-tg&_hsmi=323476472&utm_content=&utm_source=

The financial services landscape is rapidly evolving, and consumer behaviours are shifting. For life insurance advisors, this evolution underscores the importance of adapting to the distinct needs of Millennials and Generation Z.

Younger, digitally savvy generations prioritize flexibility, customization, and transparency in their financial decisions. However, despite their technological prowess and economic awareness, many Millennials and Gen Z individuals still overlook the crucial role of life insurance. Co-operators believes this presents a significant opportunity for advisors to connect with these cohorts and provide valuable advice.

To effectively bridge this generational gap, advisors must understand Millennials' and Gen Z's unique values and priorities and articulate how life insurance aligns with their broader financial goals. The lasting effects of the COVID-19 pandemic have profoundly influenced their approach to financial planning.

While the need for life insurance has surged across all demographics, Millennials and Gen Z stand out for having the highest unmet demand, even though their ownership rates are similar to those of Baby Boomers. Co-operators recognizes the generational "life insurance gap" as a pivotal opportunity for life insurance advisors to provide meaningful advice, tailored to the unique values of these younger cohorts.

The generational life insurance gap

This generational 'life insurance gap' is a critical opportunity for advisors. According to LIMRA, 44% of Gen Z and 34% of Millennials report needing or needing more life insurance coverage.

Co-operators believes the reasons for this gap are twofold.

- First, these younger generations are reaching key life milestones that act as trigger points for life insurance purchases—such as getting married, buying a home, or having children—much later than their predecessors.
- Second, the rising cost of living has forced them to prioritize other financial obligations, often at the expense of securing life insurance.

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Additionally, there needs to be more awareness about the cost of life insurance. A recent study found that over a third of Canadians estimate the cost of life insurance to be three times higher than it is. This overestimation is a significant barrier to purchasing life insurance, particularly for younger people juggling multiple financial priorities.

The essential role advisors play in closing the gap

Life insurance advisors have a unique opportunity to make a difference in the lives of Millennials and Gen Z. While these younger generations are often financially savvy, they frequently overlook the importance of life insurance—one of the most critical elements in a comprehensive financial plan.

Building trust is the foundation of an advisor-client relationship, especially when addressing something as personal as life insurance. Advisors can start by adopting a supportive and empathetic approach, taking the time to understand their specific concerns and financial goals. Many younger clients hold misconceptions about life insurance—such as its cost or relevance to their lives at this stage. By dispelling these myths, it'll help them see the value of starting early, not just to secure affordable coverage but to guarantee their insurability for the future.

Advisors also have an opportunity to guide Millennials and Gen Zs through the complexities of life insurance and help them understand its role in building a more secure financial future. Engaging Millennials and Gen Z in meaningful discussions about life insurance can be most effective when tied to significant life milestones, as they've traditionally acted as trigger points for purchasing coverage.

Tailored conversation starters

When addressing key life milestones with younger clients, advisors can consider the following conversation starters to guide their discussions:

Purchasing their first home

- "Congratulations on purchasing your new home! Now that you've made this significant investment, let's discuss how to protect it long-term."
- "I understand you might feel financially stretched after such a big purchase, but life insurance can be more affordable than you think. Let's explore your options."

Expecting their first child

- "As you prepare for this exciting new chapter, it's important to consider securing your child's future and ensuring your family's financial stability. This includes planning their education and setting up a safety net for the unexpected."
- "Term life insurance is a great option for new parents—offering coverage at a lower cost. With Co-operators' Versatile Term products recently dropping in price by 3% to 7%, now is the perfect time to secure coverage that fits your growing family's needs."
- Why start the conversation now?

Co-operators believes it's critical for advisors to start the conversation about life insurance with Millennials and Gen Z clients sooner rather than later. Not only does it help them secure better rates, but it also positions advisors as a trusted resource who care about their well-being. As the financial landscape continues to evolve, the role an advisor plays in guiding younger generations through financial decisions becomes increasingly valuable.

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Remember, while technology and robo-advisors have their place, they cannot replace the human elements of empathy, understanding, and personalized advice. By starting the conversation today, advisors can help build a secure financial future for the next generations.

Airport Lounge Access, Travel Companions And Insurance: Why Some Credit Card Benefits Are Not Worth The Hype

By Barry Choi, The Globe and Mail, September 6, 2024

https://www.theglobeandmail.com/investing/personal-finance/household-finances/article-airport-lounge-access-travel-companions-and-insurance-why-some-credit/

Many credit cards come with an annual fee – some as high as $799. If the benefits the card brings are worth it, that fee is easier to justify. But be warned: Some of the perks may be overrated.

Airport lounge access
With unlimited food, free drinks and comfortable seating, it's no wonder airport lounges are highly appealing for travellers. However, the allure fades quickly if you're flying from a major Canadian airport during peak hours, such as early in the morning or after work.

Food quality is inconsistent, and seating tends to be sparse. This assumes you can even get in since overcrowding has led to long lines and lounges will turn people away when they're at capacity.

Given that more than a dozen credit cards in Canada now offer airport lounge access, it's no surprise that lounges have become packed. Airlines and lounge providers are struggling to meet demand. To be fair, this isn't an isolated problem for Canadian airports. Any central hub – such as Los Angeles, London and Doha, to name a few – also struggles with crowds during peak travel times.

If you've signed up for a credit card believing that lounge access is worth more than the annual fee, you may want to rethink that decision. That said, when lounges have reasonable – or no – crowds, it is a great way to start your travels.

WestJet companion voucher
The WestJet RBC Mastercards have an annual companion voucher. It allows a passenger travelling with the primary cardholder to pay a reduced base fare of $119 for travel within Canada or the continental United States or $399 for the rest of the WestJet network, plus any taxes, fees and other ATC.

ATC—or air transportation charges—are standard in the airline industry and typically include airport fees, tourism taxes, facility charges, etc. However, when using the companion voucher, WestJet typically adds an "Other ATC" fee, which is not added when paying for a cash fare for the same route.

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Travellers have recently noticed that when using their companion voucher on select routes, an "Other ATC" fee of $20 is applied, which raises the question of whether the companion voucher should actually be advertised at $139 and $419, respectively.

When reached for comment, Julia Kaiser, media relations adviser at WestJet, wrote in an e-mail: "'Other ATC' is added to most WestJet fares, including fares booked with Companion Vouchers. ... 'Other ATC' was implemented more than 15 years ago and has fluctuated over time. 'Other ATC' is disclosed at all points in the guest booking journey."

However, current and former WestJet employees who are familiar with the fee and spoke with me confidentially say WestJet's revenue management team uses "Other ATC" as part of its pricing strategy to address high demand periods and increased fuel costs.

While it's true that "Other ATC" is disclosed when passengers book their flights, there's never a formal breakdown of what's included in that fee, so it's a bit deceiving. This additional $20 is clearly being added to those using a companion voucher, but it's never mentioned anywhere when people sign up for the credit card.

The value of the companion voucher is further debatable considering the voucher only applies to the base fare. In some scenarios, the base fare is lower than the cost of the voucher's co-pay, so there are no savings at all.

The WestJet Mastercards still offer value for travellers who enjoy flying WestJet, but the companion voucher's value is questionable upon further inspection.

Travel Insurance
Make no mistake, credit-card travel insurance is better than nothing, but the limitations can haunt you if you ever need to make a claim.

With credit card travel insurance, the underwriting is done at the time of the claim. For example, let's say you have a heart attack abroad and need to make a claim through your credit card insurance.

Your insurance provider will check your medical history, looking for a reason not to pay out. If they find that you had visited your doctor earlier and complained about chest pains, they could reasonably deny your claim, citing a pre-existing condition.

Now, compare that with an insurance policy purchased separately from a provider such as TuGo or Manulife. The underwriting is done at the time of purchase since you would answer a medical questionnaire. Any potential flags would be addressed immediately. Even if you have a previous medical condition, an included or optional stability clause would likely still give you coverage.

Additionally, certain conditions exist to qualify for your credit card travel insurance. You may need to pay for the entire cost of your flights and hotels with your credit card. Credit card travel insurance also only covers you for a set number of days. This can be problematic for those aged 65 and older as the standard coverage time is limited to three days.

If you're under 55, many credit card travel insurance policies are likely adequate. However, if you're older or have any health concerns, you're better off purchasing a separate policy where you know exactly what you're covered for in advance.

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Economic Uncertainty Fails To Dampen Canadian Life Insurers' Performance

By Alain Castonguay, September 3, 2024

https://insurance-portal.ca/life/economic-uncertainty-fails-to-dampen-canadian-life-insurers-performance/?utm_source=sendinblue&utm_campaign=daily_complete_202409-03&utm_medium=email

In a commentary published on August 29, Morningstar DBRS noted that despite the economic challenges posed by a sluggish real estate market and rising household debt, Canada's big four life insurance companies have shown resilience in the first half (H1) of 2024.

In the report entitled Canadian Life Insurers Perform Well in H1 2024, Brush Off Impact of Weaker Real Estate Market, Morningstar DBRS reviewed the performance of Manulife, Great-West Lifeco, Sun Life, and iA Financial Group.

According to Patrick Douville, Vice President of Global Insurance and Pension Ratings at Morningstar DBRS, these insurers have focused for several years on lower capital-intensive products. These products shift investment risk to policyholders and limit other types of guarantees. "This trend, in addition to a lower capital framework uncertainty now that the transition to IFRS 17 is complete, has allowed lifecos to focus more on capital redeployment and on optimizing ROE (return on equity)," said Douville.

Douville highlighted Manulife's move to raise its core ROE target to 18 percent or higher within the next three years. "This should raise the bar for all four lifecos and put pressure on them to deploy excess capital," he added.

The agency also observed solid performance in insurance revenues and new business across the four insurers. However, in the wealth management sector, Sun Life reported mixed results, with net outflows of $29.7 billion from segregated funds and third-party managed assets.

Commercial real estate exposure

The life insurers' real estate portfolios are well-diversified both geographically and in terms of property usage. "Weakness in the Canadian and global real estate sectors had some impact on results, mainly through the direct holdings of real estate properties, though this was limited and spread over multiple quarters, including throughout 2023," the agency stated.

"While lifecos still have significant exposure to office properties, many of those are own-use or leased to long-term tenants," the report added. Manulife and iA reported declines in revenues due to recent acquisitions and reinsurance impacts.

In terms of solvency, the four insurers maintained stable and robust ratios, allowing three of them to proceed with share buybacks. Manulife, Sun Life, and iA collectively spent hundreds of millions of dollars on these buybacks in the first half of the year. Great-West did not follow suit, likely due to a lower capital ratio (LICAT ratio of 130 percent in Q2 2024).

Morningstar DBRS predicts that life insurers will demonstrate greater boldness in managing their financial capacities. "The question of capital redeployment remains central to the medium-term strategic outlook of the four lifecos, with opportunities in the U.S. and Asia likely to be pursued."

Gen AI Moves From Potential To Reality For Insurers

By Michael Shashoua, Digital Insurance, August 21, 2024

https://www.dig-in.com/news/gen-ai-moves-from-potential-to-reality-for-insurers?utm_campaign=NL_DIG_Morning_Briefing_08222024&position=1&utm_source=newsletter&utm_medium=email&campaignname=NL_DIG_Morning_Briefing_08222024&oly_enc_id=1794I9343067F0V

Last fall, the insurance industry was looking at how to use Gen AI after the technology got a lot of hype.

Heading into this fall, the industry has advanced to targeting specific applications for Gen AI, such as operational security, risk management, underwriting, claims and applications for small and medium size enterprises.

The industry's spending on Gen AI capabilities is increasing and more insurers are adopting the technology, according to consultants' research.

Redhand Advisors' June survey of 998 risk management information systems (RMIS) professionals found that one in ten now use Gen AI, but nearly half of those surveyed expect to adopt Gen AI in the next three years.

In July, Boston Consulting Group research bore out the projected growth in Gen AI for insurers. A survey of 330 IT buyers at director level or higher, from various industries, found that their Gen AI investment on average would grow 30% over the next three years. The research also broke down adoption and plans by industry and found insurance to be a lagging industry, with at least 40% of its companies having done little or no adoption of Gen AI.

If insurance companies are as interested as these surveys indicate, there appears to be plenty of room for them to increase their use of Gen AI.

Rima Safari, a partner in the insurance practice at PWC, said commercial lines show potential for Gen AI applications. "When there are broker requests coming in, we're seeing a ton of value in data ingestion before you get into the underwriting process," she said. "We're seeing the same thing in group insurance, as opposed to personal lines, where there is a lot of data to ingest."

Jason Ralph, a partner at McKinsey & Co., speaking at the National Association of Insurance Commissioners (NAIC) summer conference on August 13, identified four ways Gen AI can create value for insurance companies:

- **Enabling customer journeys.** This relates to applying Gen AI in the form of chatbots to support customer service reps.
- **Summarizing complex information**, to generate insights and create reports, using data sets that were not otherwise being leveraged.
- **Providing context.** Creating new marketing material, going beyond just digesting and responding to information.

- **Developing technologies.** Using Gen AI to summarize text and code, and also to digest what code accomplishes in insurers' operations. This can reduce modernization of legacy systems that typically takes five years, and get it down to less than two years to complete.

However, Ralph cautioned, both technology itself and talent, as well as data management capabilities, can limit what insurers may achieve using Gen AI.

"We've seen a recalibration of expectations," he said. "When we first started talking about generative AI to our clients, a lot of the focus was on finding use cases where the sky's the limit. Something that fundamentally transforms the way that we do business and has limitless potential. The ability to fundamentally change the way that insurance is bought and sold. We've started to see very quickly that there are clear limits."

What Is Diversity, Equity, And Inclusion?

By McKinsey & Co., August 17, 2022

https://www.mckinsey.com/featured-insights/mckinsey-explainers/what-is-diversity-equity-and-inclusion?stcr=78BC983D06464AAA862C0DE9993B8B4B&cid=other-eml-alt-mip-mck&hlkid=a99638f915cd4c94bfe55f2feea2ff55&hctky=15382209&hdpid=e8824508-9acc-4596-9dda-16d0df66276a

Diversity, equity, and inclusion are three closely linked values held by many organizations that are working to be supportive of different groups of individuals, including people of different races, ethnicities, religions, abilities, genders, and sexual orientations.
Rainbow colored spheres hanging on stringsRainbow colored spheres hanging on strings

Variety, as they say, is the spice of life. If diversity is another word for variety, how can it enhance or flavor the world?

Diversity—through the lenses of race, ethnicity, ability, gender, sexual orientation, neurodiversity, and beyond—can help to strengthen organizations, as studies have shown time and again. Quite simply, diversity, equity, and inclusion (DEI) is used to describe three values that many organizations today strive to embody to help meet the needs of people from all walks of life. While concepts such as biodiversity are important offshoots of the core idea of diversity, this article focuses on diversity, equity, and inclusion in business and society rather than in other contexts.

Companies that are diverse, equitable, and inclusive are better able to respond to challenges, win top talent, and meet the needs of different customer bases. With DEI in mind, companies are considering how to better support employees. Over the past few years, many organizations have taken strides to build diversity, equity, and inclusion into their policies and hiring practices.

What are the differences between diversity, equity, and inclusion?
Diversity, equity, and inclusion are often grouped together because they are interconnected and it is only in combination that their true impact emerges. Some organizations include related concepts, such as belonging, in their DEI strategies. But all of these terms are also easily misunderstood. It’s important to grasp the individual meanings and implications of each of these terms:

Diversity refers to who is represented in the workforce. Some examples of diversity in workplaces include:

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- *Gender diversity:* What makes up the composition of men, women, and nonbinary people in a given population?
- *Age diversity:* Are people in a group from mostly one generation, or is there a mix of ages?
- *Ethnic diversity:* Do people in a group share common national or cultural traditions, or do they represent different backgrounds?
- *Physical ability and neurodiversity:* Are the perspectives of people with disabilities, whether apparent or not, accounted for? These are a few of the most common examples, but what is considered diverse can range widely. Nobel Prize winner Richard Thaler touches on this in an interview with McKinsey on debiasing the corporation. "There's lots of talk about diversity these days," says Thaler. "We tend to think about that in terms of things like racial diversity and gender diversity and ethnic diversity. Those things are all important. But it's also important to have diversity in how people think."
- *Equity* refers to fair treatment for all people, so that the norms, practices, and policies in place ensure identity is not predictive of opportunities or workplace outcomes. Equity differs from equality in a subtle but important way. While equality assumes that all people should be treated the same, equity takes into consideration a person's unique circumstances, adjusting treatment accordingly so that the end result is equal. In an episode of the McKinsey Talks Talent podcast on the inclusive workplace, McKinsey senior partner and talent expert Bill Schaninger offers a view on the implications of equity when sourcing talent: "There's a real difference between equal and equitable. Suppose we said, 'All interns are created equal. We pay them nothing.' The people who can afford an entire summer without getting paid are likely already coming from a position of privilege."
- *Inclusion* refers to how the workforce experiences the workplace and the degree to which organizations embrace all employees and enable them to make meaningful contributions. Companies that are intent on recruiting a diverse workforce must also strive to develop a sufficiently inclusive culture, such that all employees feel their voices will be heard—critical if organizations want to retain their talent and unlock the power of their diverse workforce. In an episode of the McKinsey Talks Talent podcast on the inclusive workplace, McKinsey partner and DEI expert Diana Ellsworth shared an example of how a lack of inclusion can manifest in workplace culture: "The LGBTQ+ community is underrepresented in the workplace, especially at more senior levels. As a result, many feel like an "only" at work and are more likely to experience microaggressions; they might feel unable to talk openly and comfortably about themselves, for example, or need constantly to correct assumptions about their personal lives."

Why is diversity in the workplace important?
A series of three McKinsey reports shows the impact of diverse workplaces: Why diversity matters (2015), Delivering through diversity (2018), and Diversity wins: How inclusion matters (2020). The latest findings draw from a data set that encompasses 15 countries and more than 1,000 large companies, as well as research on employee sentiment, and the results show a correlative relationship between business performance and diversity. It's worth noting that greater access to talent and increased employee engagement contribute to this performance effect. The business case for diversity is robust, and the relationship between diversity on executive teams and the likelihood of financial outperformance has gotten stronger over time. And the results have been replicated in further research, for instance, in Latin America and Central Europe.

Some of the key findings from the latest Diversity wins report include the following:

- Most employees support diversity, with overall sentiment on diversity 52 percent positive and 31 percent negative.
- There are clear correlations between diversity and business performance. Analysis of 2019 data shows that companies in the top quartile for gender diversity within executive teams were 25 percent more likely than

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companies in the fourth quartile to have above-average profitability (up from 21 percent in 2017 and 15 percent in 2014).

- The greater the representation of gender diversity, the higher the likelihood of outperformance. For instance, companies where more than 30 percent of the executives are women were more likely to outperform companies where this percentage ranged from only 10 to 30. The most gender-diverse companies see a substantial differential likelihood of outperformance—48 percent—over the least gender-diverse companies.
- The business case for ethnic and cultural diversity is also strong: in 2019, companies in the top quartile bested those in the fourth quartile by 36 percent in profitability. Notably, the likelihood of outperformance continues to be higher for diversity in ethnicity than in gender.
- Progress in building diverse workforces remains stubbornly slow.
- Despite employees' support of diversity, there are high levels of negative sentiment on inclusion—namely, equality, openness, and belonging—particularly around equality and fairness of opportunity.

Even during a crisis, when leaders might be tempted to shelve DEI efforts to ensure the company's financial survival, there is value to prioritizing diversity, equity, and inclusion. In the words of McKinsey's Bryan Hancock from McKinsey Talks Talent: "D&I is good business. It doesn't have to be at the expense of financial outcomes. . . . This isn't an issue where leaders can say, 'We can't do diversity right now, because we're under a lot of pressure.' Diversity is one of the things you've got to be mindful of in every context."

What other benefits can organizations realize from inclusion and diversity?

In addition to profitability, there are five key domains in which inclusion and diversity can significantly affect an organization's overall performance:

1. *Winning talent:* Organizations that monitor the demographic profile of their workforces are better able to retain top performers while making sure that diverse talent isn't lost.
2. *Improving the quality of decision making*: Diversity brings multiple perspectives to the table during times when enhanced problem-solving skills and vision are needed.
3. *Increasing customer insight and innovation:* Diverse teams are typically more innovative and better at anticipating shifts.
4. *Driving employee motivation and satisfaction:* Research in Latin America showed that companies that are committed to diversity are 75 percent more likely to report a pro-teamwork culture.
5. I*mproving a company's global image and license to operate:* Companies that can maintain or increase their focus on inclusion and diversity during crises are poised to avoid consequences such as struggling to attract talent or losing customers and government support.

How can organizations foster an inclusive workplace?

For companies looking to bolster inclusion and step up their DEI efforts more broadly, five areas of action stand out:

- Ensure that diverse talent is well represented.
- Strengthen leadership accountability and capabilities.
- Be fair and transparent, enabling equality of opportunity.
- Promote openness and tackle microaggressions, bias, and discrimination.
- Foster belonging through unequivocal support for all the ways diversity manifests.

A McKinsey survey about inclusion at work and how to address organizational barriers to it offers unique insight at a more granular level. The research finds that respondents of all backgrounds encounter barriers to feeling included—and that women, respondents who are ethnic and racial minorities, and those who identify as LGBTQ+ encounter additional challenges.

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A few key data points from the survey add nuance about the lived experiences of employees in workplaces, inclusive and otherwise:

- Employee engagement is strongly linked with a sense of inclusion. Those who feel very included are more likely than others to say they feel excited by and committed to their organizations.
- Nearly 40 percent of respondents say they have turned down or chosen not to pursue a job because of a perceived lack of inclusion at the organization.
- Over a third of respondents say their organizations don't put enough effort into creating a diverse, inclusive environment (while only 6 percent say too much is being done).
- A resounding 84 percent of respondents say they have experienced microaggressions at work. More than one in four say they have needed to correct others' assumptions about their personal lives, for example. High levels of respondents have experienced everyday slights rooted in bias, such as not receiving credit for their ideas, being asked to speak as a representative for a group of people like themselves, or being coached to communicate in a way that feels inauthentic.
- Looking only at LGBTQ+ respondents, 37 percent say they have had an uncomfortable experience coming out to colleagues in the preceding month.

Among respondents who identified as racial or ethnic minorities, 40 percent of those who indicated they have discussed identity-related issues at work in the preceding month say they have felt at least slightly uncomfortable in those situations.

To serve these workers better, organizations can pay attention to four main factors associated with employees' inclusion:

6. *Diverse, inclusive leadership:* The presence of diverse leaders at an organization, as well as an organization's focus on inclusive leadership, are correlated with individuals feeling more included.
7. *Meritocracy and initiatives to increase fairness in performance evaluations*: A meritocratic company culture is strongly associated with a sense of inclusion.
8. *Sponsorship:* Respondents who say colleagues at their organization have gone out of their way to create professional-advancement opportunities for them are also more likely than others to feel a strong sense of inclusion.
9. *Substantive access to senior leaders:* More than half of all respondents say that meaningful interactions with senior leaders have aided their career advancement.

What is intersectionality?

Intersectionality, a term coined by Professor Kimberlé Crenshaw in 1989, refers to the ways different parts of one's identity intersect or overlap with one another. For instance, gender is one aspect of a person's identity, but so are sexual orientation and race. A Black woman who is queer, or a White woman who has a disability, may take a perspective that acknowledges how those different aspects of their identity overlap or intersect. McKinsey's Women in the Workplace 2021 report, for instance, found that LGBTQ+ women, as well as women with disabilities, are much more likely than women overall to experience microaggressions on the job.

Acknowledging intersectional identities can strengthen companies and communities more broadly. "Everyone deserves to feel empowered across all aspects of who they are," says McKinsey senior partner Guangyu Li. "It shouldn't be left to any individual community to defend itself. It's in our collective interest to show up for each other with concrete action and to come together in solidarity."

Allyship is a concept that is closely related to intersectionality. An ally aligns with people in the minority to help foster equitable and inclusive opportunities for all. In corporate America, White women, for instance, may take allyship actions such as mentoring women of color, advocating for new opportunities for them, and actively confronting any discrimination they might face. However, there is a notable disconnect between the allyship actions that women of color say are most meaningful and the actions that White employees prioritize—suggesting opportunities for recentering efforts around the experience of women of color and other marginalized groups.

What issues are important to women in the workplace?
Women's representation in the corporate world has largely increased in recent years, but the pandemic has affected their participation in the workforce. It is worth noting that dynamics of gender in the workplace may be regionally specific. While much of McKinsey's work offers insight into women in corporate America, you can explore additional material on global gender equality, as well as gender diversity in Africa, Canada, Central Europe, France, Japan, the Middle East, and other regions.

The largest study of women in corporate America is Women in the Workplace, conducted by McKinsey in partnership with LeanIn.Org. The latest research, now in its seventh year, reflects information from 423 organizations that employ 12 million people, and includes responses from more than 65,000 people surveyed on their workplace experience, as well as in-depth interviews with women of diverse identities.

Findings from the Women in the Workplace 2021 report include the following:

- Women's representation in the corporate pipeline (that is, the journey an employee might take from starting as an entry-level worker to advancing to a spot in the C-suite) has increased since 2016. But women—and women of color in particular—remain significantly underrepresented in leadership.
- At every step in the career ladder, women of color lose ground to White women and men of color.
- The "broken rung" problem remains a challenge for women, particularly those seeking their first step up from entry level to manager. For every 100 men promoted to manager, only 86 women are promoted.
- Burnout, stress, and exhaustion continue to affect women more than men. In the past year, one in three women considered leaving the workforce or downshifting their career, a notable increase from levels seen early in the COVID-19 pandemic.
- Women leaders are doing considerable work to support DEI efforts and employee well-being more broadly, but they're not necessarily being recognized for it. For instance, employees with women managers are more likely than others to say that their manager has supported and helped them in the past year; women leaders also spend more time than men on DEI work that's outside their formal job responsibilities. Less than a quarter of companies, though, recognize this work in performance reviews, for example.

To support women in the workplace, companies need to invest deeply in all aspects of diversity, equity, and inclusion. Although there are no quick fixes, there are some steps companies should take to empower women at work:

- Companies should put more practices in place to ensure that promotions are equitable. Beyond reducing potential bias in the hiring process, companies need to extend similar rigor to performance reviews.
- Organizations need to track representation and hiring and promotion outcomes more fully. A company may track representation for women overall, but does it break those numbers down to look at representation for women on color in particular?
- Companies need to double their efforts when it comes to accountability. Only two-thirds of companies hold senior leaders accountable for progress on diversity goals, and less than half consider progress on diversity metrics in performance reviews.

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- To create a culture that embraces and leverages diversity, companies need to promote senior-level sponsorship, with top leaders fully and publicly supporting DEI efforts, modeling inclusive leadership, and actively participating in training and events.
- Spurring high employee engagement will also be crucial. Raising awareness of the barriers that many women face can help, and further training (on bias, antiracism, and allyship) can take employees from awareness to action.
- Burnout is on the rise, and investing in solutions to help address this problem will remain a crucial issue for many organizations. In addition to expanding on successful established policies and trying new approaches, companies can track symptoms and establish new norms to improve the everyday experience of employees.

What do we know about advancing racial equity for Black Americans in the US private sector and across society?
Black Americans in the workforce are at a disadvantage; the median annual wage for Black workers is approximately 30 percent, or $10,000, lower than that of White workers, with serious implications for economic security, consumption, and the ability to build generational wealth. They are underrepresented in higher-wage industries and executive roles, and they face lower odds for advancement. Clear racial patterns exist across the US labor force, with nearly half of Black workers concentrated in low-paying healthcare, retail, food services, and accommodations roles.

There are many benefits to righting historical wrongs and realizing the full potential of Black American talent: addressing wage disparities alone, for instance, could propel two million Black Americans into the middle class for the first time.

Doing so will take effort on many levels. Research from the McKinsey Institute for Black Economic Mobility suggests some jumping-off points:

- Consumer-facing companies that pursue broader racial-equity goals can better serve Black consumers.
- Harnessing the power of retail can drive demand for Black-owned brands.
- Addressing racial disparities in farming could generate billions in value for the agriculture industry.
- Increasing financial inclusion to broaden services for Black Americans could yield $2 billion in potential revenue, and changes in three key areas can help companies make more progress toward racial equity in financial services.
- Supporting historically Black colleges and universities can accelerate Black economic mobility.
- Understanding Black representation in film and TV could help drive greater diversity.
- Building supportive ecosystems for Black-owned business could add $290 billion in business equity.
- Emphasizing health equity can activate meaningful change or even help retain talent.

The stories of Black leaders' journeys can offer inspiration and hope for personal and professional development. Get insight from Jason Wright (president of the National Football League's Washington Commanders), Stephanie Hill (an executive vice president at Lockheed Martin), and Barry Lawson Williams (the founder of Williams Pacific Ventures).

What issues are important to Latinos in the workplace?
In the United States, Latinos make up 18.4 percent of the population and 17.3 percent of the labor force, and that share is projected to rise to more than 30 percent by 2060. This community faces challenges, and US- and foreign-born Latinos alike remain far from equal with non-Latino White Americans, with Latino Americans earning just 73 cents for every dollar earned by White Americans. They face discrimination in securing financing to start and scale businesses, and they face challenges accessing food, housing, and other essentials.

McKinsey research on the economic state of Latinos in America finds that they are underpaid, collectively, by $288 billion a year. At full parity, though, Latinos could spend an extra $660 billion annually, and Latino businesses could

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generate trillions in revenue and support millions of new jobs, while also creating new flows of generational wealth. Addressing barriers faced by Latinos in America could make the economy more robust for all.

How can we empower Asian Americans at work?
Asian Americans have contributed to the US economy since the 1800s, yet they have historically been overlooked. This group as a whole is often perceived as the "model minority," a term that diminishes the unique issues faced by their diverse community. Recently, given the rise in racially motivated attacks on Asian Americans during the COVID-19 pandemic, historically unaddressed challenges faced by this group are coming to light, offering a fresh reminder of the need to support and include Asian Americans at work.

In corporate America, Asian Americans are underrepresented in senior leadership roles (as are Black, Hispanic, and Latino Americans). What might help? Recognizing where in the corporate pipeline Asian Americans are underrepresented, mitigating implicit and unconscious bias during promotion and performance evaluations, fostering sponsorship for Asian American employees, and expanding workplace flexibility and support such as paid sick leave.

What does research show about the experiences of LGBTQ+ employees in the workplace?
For LGBTQ+ employees, many workplaces today fall short of full inclusion, even if there is visible corporate support for LGBTQ+ communities. For example, LGBTQ+ women are more underrepresented than women generally in America's largest corporations. Just four LGBTQ+ CEOs head these corporations—only one woman, and none identifies as transgender. An episode of the McKinsey Talks Talent podcast considers the latest research on the LGBTQ+ experience in the workplace and highlights practical steps for all employees to signal support and boost progress for this community.

Transgender employees face a unique set of challenges. They earn 32 percent less money than cisgender employees (cisgender refers to people whose gender identity aligns with the sex assigned to them at birth). More than half of transgender employees say they are not comfortable at work, and they report feeling less supported by managers. These strong feelings of exclusion have significant economic implications: greater transgender inclusion in the workforce through wage equity and increased employment could boost annual consumer spending by $12 billion a year. To help address the issues, companies can be intentional in recruiting (for example, by asking applicants what pronouns or names they prefer to use) or offer trans-affirming benefits, among other actions.

How do different industries approach diversity, equity, and inclusion?
Different industries may well need to take different approaches to diversity, equity, and inclusion, depending on the composition of their workforces. Several articles offer insight into those industry-specific dynamics, especially with regard to gender diversity:

- Companies can repair the broken rung on the career ladder for women in technical industries and roles.
- Organizations can work to close gender and race gaps in the US financial-services sector.
- Voices from the fashion industry on diversity offer insight on what actions might be most meaningful for creating more inclusive workplaces.
- Organizations can make traveling in cities safer and more comfortable for at-risk groups.
- The COVID-19 pandemic hit the education space hard; as the recovery continues, ensuring that education is equitable and inclusive will be vital.
- In the public and social sectors, women are increasingly represented, but they are also feeling burned out—a few actions can bend the curve.
- Consumers are expecting more from brands than ever before—here's what retailers can do to meet DEI needs.

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- Private equity can help catalyze DEI efforts to transform the global business community and improve returns.
- In media and entertainment, women remain locked out of top roles.
- While women in healthcare and life sciences have made progress, they remain underrepresented at senior levels.
- Research from the oil and gas industry suggests actions for the sector to consider to help attract and retain women.

Women are leaving the mining industry. Here's why—and what companies can do about it.

UPCOMING CAFII RELEVANT WEBINARS & EVENTS; AND RELATED EDUCATION CONTENT

2024 THIA Innovation Summit

https://www.thiaonline.com/cgi/page.cgi/_evtcal.html?evt=116

WHEN: September 26, 2024, 8:45 AM - 5:00 PM
WHERE: Manulife Conference space, Downtown Toronto.

Reserve your spot today for THIA's Innovation Summit, which returns this fall for a day of engagement and insights into the issues, solutions and trends affecting the travel health insurance industry.

This year's Summit will take place on Thursday, September 26th (the day after THIA's AGM) at Manulife's conference space in Downtown Toronto from 8:45 AM – 5:00 PM EST, cocktail reception to follow.* We are pleased to advise that this space is wheelchair accessible.

Space is limited and sure to fill up quickly, and Early Bird pricing is only available until August 9, 2024.

*Event information is subject to change.

This Year's Innovation Summit Highlights
Navigating Disruption: Travel Health Insurance in a Time of Change
At this one-day summit, we will be exploring the impact of emerging technologies, consumer expectations and a shifting global landscape on the travel health insurance industry, while meeting travel health insurance leaders and other industry experts.

The Summit will feature two keynote speakers, provocative panels, technology experts and information about emerging businesses that are helping transform our industry and adjacent industries.

A light breakfast, lunch and a networking cocktail reception at the end of the day are included in your purchase price.

Pricing

THIA Member pricing is valid for active THIA members and non-member colleagues at their company. Non-members must be registered by an active THIA member.

- THIA Members Early Bird ticket (through August 9, 2024): $250 per person
- THIA Members Standard ticket: $300 per person
- Non-Members ticket: $350 per person

Accommodation

THIA has reserved a limited number of hotel rooms for attendees of our AGM on September 25th and the Innovation Summit on the 26th. The rooms are at the Canopy by Hilton Toronto Yorkville (387 Bloor Street East, Toronto ON M4W 1H7), a short walk from the Innovation Summit venue. The price is $359 per night plus applicable taxes. To take advantage of this rate, you must reserve by August 9, 2024. Visit here to reserve your room.

We strongly encourage those attendees who are travelling to Toronto for the event to ensure they have appropriate travel insurance coverage.