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Industry Perspective

Four factors creating a perfect storm in the insurance industry

The storm is brewing

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In insurance, there's a tendency toward hyperbole that makes it seem like the industry is perpetually on the verge of revolution, disruption or upheaval. I started in the insurance industry back in the early '90s, when "the CRM revolution" was being discussed as a major point of inflection. And, you know, nothing really ended up changing. Most of the companies that were large and successful in insurance then, continue to be large and successful in insurance now. Right now, however, there are at least four major forces in play within the insurance sector — and this time, I believe we really are on the cusp of something very substantial and very fundamental. It will change the way the entire insurance industry looks and works, and may even change a lot of the players in the sector.

1. New entrants

Insurance companies have remained relatively constant. Most of them have been in business for a good hundred years. Recently, however, there has been a rise in the number of new entrants marketing, selling or servicing insurance products or providing new capital. A range of new companies is coming in, redefining how insurance is done, and reshaping the economics of the industry in the process.

Many of these new entrants are interesting organizations with great capabilities. Google, which entered the UK market in 2011 as an insurance aggregator, is perhaps the most formidable new entrant, from the perspective of a traditional insurer. The technology giant joined the emerging insurance aggregation market, significantly disrupting competitive market conditions and, by some accounts, subsequently helping lower insurance premiums by roughly 30% over the last 5 years.

Introducing that sort of intense price competition into an industry which is not overly profitable to begin with, has changed the dynamics of the market substantially. To compound the issue, other companies are entering the fray as well, including retailers and their strong brand names, and telecommunications companies boasting telematics capabilities. Even car manufacturers are starting to embed telematics capabilities into vehicles and, in some cases, to sell insurance directly.

2. Social and economic dynamics

We've moved into a very low interest rate period, and those low rates are putting a lot of pressure on the profitability of insurance companies. Insurance is an industry that, essentially, takes in money and invests that money before subsequently paying claims. So, with lower investment returns, there's less profit being generated by the insurance sector.

On the life side, wearable technology and analytics can combine to create compelling wellness programs for clients. These programs, in effect, are enabling insurers to manage the risks they are writing by rewarding good behavior and penalizing bad behavior.

And it's a sector that doesn't really generate a lot of profit to begin with. Over the last 30 years, many U.S.-based insurance companies have failed to return their cost of capital. On top of low interest conditions, there has also been a lot of volatility on those returns, especially since the financial crash of 2007 and 2008.

On the plus side, insurers have rebuilt their balance sheets. However, market volatility makes it much harder to run their business. It's much more difficult to find stable, growing assets to match against long-term liabilities, for example.

The most obvious societal shift, and one that is certainly impacting developed countries, is the retirement of baby boomers. As they retire, they are taking money out of their accumulation products to provide an ongoing source of income; trillions of dollars are going to flow out of these products over the next 5 to 10 years.

On the other hand, this growing section of the retired population has more wealth than people who retired previously, and they're also living longer. That means they're generating new and different insurance needs, necessitating different types of insurance products — particularly around payouts and long-term care.

Of course, there's also growth related to Generation Y, which is largely composed of consumers who are unlikely to buy insurance in the same way that their parents would have. They're unlikely to walk down to the local broker and sit down to have a discussion over a cup of coffee to buy what is, in essence, a commodity product. Instead, they want everything now, everything mobile, everything available by text.

Meanwhile, it's in developing countries that we clearly see most of the growth. There's a move to urbanization, which is creating a much larger and more affluent middle class. And clearly, where there are assets, there is also income. There are families emerging that have started to drive a lot of new insurance needs.

As a result, in the developing world, we're seeing a lot of demand for insurance products. This is driving growth for domestic companies, but it's also acting as a magnet for some of the global insurers. Examples like AXA, MAPFRE and Prudential UK have all moved aggressively into the Asian and the Latin American markets.

3. The data revolution

Insurance companies have always made use of substantial amounts of data, but how they leverage data is changing in significant ways. It used to be that, if an insurer had an efficient operation and a large volume of risk data, it could find success by comparing, pooling and underwriting similar risks. Now, data is everywhere. It's pervasive, and it's immediately available. The whole concept of pooling risks may end up disappearing because, in effect, the data revolution will actually enable insurers to underwrite down to the individual level.

Historically, insurance has been about pricing a risk. Going forward though, the industry might be moving into a new realm that places more value on managing a risk. For example, telematics can be leveraged to give people driving scores — getting them to drive more slowly, brake more effectively, corner less aggressively, leave more distance between the car in front of them. On the life side, wearable technology and analytics can combine to create compelling wellness programs for clients. These programs are, in effect, enabling insurers to manage the risks they are writing — by rewarding good behavior and penalizing bad behavior.

A partner with deep industry expertise and knowledge of back-office systems can help guide the move to a service-enabled environment, which brings new capabilities while significantly lowering costs.

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4. The digital mandate

The convenience and efficiency of online and mobile channels, coupled with the commoditization of the core insurance product, has led insurance customers to seek a new experience.

The digital insurance trend, then, is really about the way consumers will choose to interact with an insurance company, as opposed to the way today's insurance companies try to dictate interactions with consumers. Going forward, insurers will need to focus far more on the consumer as an individual. In this environment, an effective omnichannel strategy will be key, as will an insurer's capabilities around self-service.

The Case for Transformation

Together, these four factors combine to create a compelling case for digital insurance transformation. If traditional insurers expect to remain competitive, they must become more:

- Agile, as they respond to new and increasing competitive threats
- Efficient, as they address profitability challenges
- Customer-centric, as they respond to social changes and increasing consumer expectations
- Even more advanced in terms of data and analytics, as the industry moves from just pricing and pooling risks to truly managing individual risks

Addressing these four business imperatives is a complex effort that will require insurers to both transform their legacy operations and build out new operations. As insurers consider their next move, they'll need to ask themselves: How do we reduce our "run and maintain" costs in order to build the kinds of new capabilities necessary to stay competitive? How do we enable or evolve our legacy systems to support today's digital imperatives? How do we accept new sources of data and analyze that data properly? And, perhaps most importantly, how do we do it all simultaneously?

At DXC, we feel strongly that these challenges are best met through a technologyagnostic approach supported by strong partnerships. A partner with deep industry expertise and knowledge of back-office systems can help guide the move to a service-enabled environment, which brings new capabilities while significantly lowering costs. With these updates, insurers can invest more heavily in building for the future, while paying special attention to evolving cybersecurity and regulatory compliance requirements, as well as big data and analytics opportunities, and capitalizing on new and emerging channels.

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