BUSINESS CHALLENGES THAT INSURERS SHOULD ADDRESS

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Insurance companies face many challenges, but none are more pressing than historically low interest rate levels, the speed and advancement of technology and changing customer expectations. Outlined below are several specific business challenges that insurance companies face and what some industry participants are doing to counteract those challenges.

	Business Risk	Sector	What Are Some Insurers Doing?
	Low Interest Rate Environment		
a.	Low Yield: Low-level interest rates appear to be the new normal, at least for the foreseeable future. This can depress interest income and adversely affect key performance ratios, *e.g.*, yield ratios analyzed by rating agencies during the external rating evaluation process. In addition, the inability to reinvest proceeds from maturing fixed-income securities in highly rated investments with adequate returns only exacerbates the issue, potentially creating an unfavorable mismatch between actual and expected return embedded in product pricing.	L&H/ P&C	Many insurers are expanding relationships beyond internal capabilities and existing outside asset manager relationships to obtain diverse perspectives and inform investment strategies. Making riskier investments, however, will require insurance companies to shore up risk management capabilities to manage the purchase of higher-yielding but riskier investments, such as real estate, equities, private placements, limited partnerships, lower-quality corporate bonds, etc.
b.	Pricing Risks: A prolonged period of low interest rates has narrowed the spread between actual investment return and guaranteed minimum crediting interest rate on interest-sensitive life insurance products, such as annuities. In addition, the low interest rate environment affects the interest earning assumption factored into the pricing of permanent life insurance products. As a result, life insurers face the daunting challenge of growing market share profitably, and many have scaled back on the sale of life insurance products that are now less attractive in the current low interest rate environment.	L&H/ P&C	Many insurers are re-evaluating underwriting and pricing models, using advanced analytics to redesign products and amending fee structures and terms to make products more transparent and attractive.
c.	Valuation Risk: In the pursuit of higher yield, insurers run the risk of introducing valuation risk into the investment portfolio by investing in potentially below-investment-grade financial instruments.	L&H/ P&C	In addition to the approach many are taking mentioned in a., insurers need to help ensure there's a clear segregation of duties in the decision-making process over the purchase of investments to avoid the lure of pursuing yield in potentially risky investment products. In addition, changes to investment allocation strategy should be made in a transparent manner and receive necessary buy-in and approvals from those charged with governance, *e.g.*, the board of directors' investment committee.

	Business Risk	Sector	What Are Some Insurers Doing?
	Technological Advancements		
a.	Big Data: It's been said that data are like crude oil—extremely valuable but unusable if unrefined. While many insurance companies have updated policy administration and claim systems, most still lack the technological infrastructure to take advantage of structured and unstructured data to meaningfully affect the underwriting process at a more granular segmentation level. Insurers that cannot mine insights from big data will be at a competitive disadvantage.	L&H/ P&C	Insurance companies collect a lot of structured and unstructured data from a variety of sources on their customers, as well as potential customers who may have entered the sales channel but decided not to finalize the purchase. To take advantage of big data, there first must be buy-in from key stakeholders that big data can be harnessed to provide actionable insights into product innovation, development and risk mitigation. Second, senior leaders need to take the lead in defining the company's short-, medium- and long-term strategy for gathering data and providing compelling use cases to monetize a data-driven strategy. That vision should be anchored in a customer centricity model (see a. and b. in Changing Customer Expectations). The remaining steps could include building capabilities, testing, scaling, etc.
b.	Loss Prevention Technologies: While insurance companies view themselves primarily as loss protection product providers, many large insurers are taking a keen interest in loss prevention technologies such as connected sensors, telematics, smart cameras, wearables, etc., as tools to limit the severity and frequency of claims to improve underwriting results, generate additional revenue sources and enhance the overall customer experience. Small to midsize insurers are likely behind in leveraging these technologies and therefore run the risk of losing market share and becoming irrelevant.	L&H/ P&C	Insurance companies are known for being low touch, *e.g.*, occurring primarily during the policy issuance, claim or benefit payment processes. To truly become a forward-thinking, customer-centric organization, insurance companies should consider tearing down their industry silos and begin to view themselves as part of a broader ecosystem (platform) in which they aren't just providing loss protection products but also are providing or facilitating loss prevention services. This could dramatically increase the overall number of touches with policyholders, provide cross-selling opportunities and increase retention. For example, property and casualty insurers that partner with security monitoring entities can consider offering bundled policies that include options for security systems and monitoring, weather alert text notifications, relevant loss prevention checklists, etc., which can be facilitated with technology. Life insurers can make policies that reward healthy behaviors more widely available by including options to purchase wearables that provide redeemable points, discounts for healthy habits, etc.
c.	Efficiency-Driven Technologies: Many large insurance companies have either undergone or are in the middle of major system modernization initiatives to enhance business processes, increase collaboration, improve customer experience and reduce cost. Many of these initiatives include using software tools, such as robotics process automation (RPA), to drive efficiency. Insurers that aren't actively taking steps to modernize their system to streamline their noncustomer-facing functions and drive efficiency will be at a competitive disadvantage.	L&H/ P&C	While it's important to leverage technology to monetize the wealth of data that insurance companies accumulate, it's also important to leverage technology to streamline nonrevenue-generating business processes to drive down cost and improve profitability, particularly in the current low interest rate environment. Insurance companies, both large and small, that intend to be relevant and profitable need a digital transformation strategy that's tailored to their long-term business objective. A key component of that plan should include efficiency-generating technologies such as RPA and intelligence process automation to systematize manual and repetitive tasks and activities.

	Business Risk	Sector	What Are Some Insurers Doing?
	Changing Customer Expectations		
a.	The Amazon Effect: Amazon has 100 million U.S. customers (for context, the adult population in the U.S. is estimated at 330 million) who tend to benchmark their experience with other products and service providers against their interaction with Amazon and other customer-centric organizations, such as Uber, Starbucks, Nordstrom, etc. As a result, customers are curious about what others are saying about the product or service they're purchasing, want a pleasant and enjoyable experience and often want to easily compare prices before finalizing a purchase. Insurers that fail to address these subtle but real changes in expectations are likely to face diminished market share and retention-related issues.	L&H/ P&C	The insurance industry isn't immune from the pervasive effect of changing customer expectations. While in times past, insurance companies solely competed against each other based on products and prices, they're now competing against industry and nonindustry participants on the basis of customer expectation and experience. As a result, insurers that create a business model and culture that puts the customer at the center of everything they do will thrive in the Fourth Industrial Revolution.
b.	Frictionless Experience: With close to 80 percent of Americans owning a smartphone, the U.S. is fast becoming a mobile-first society. As a result, insurers now interact with prospective policyholders who are more likely to initiate the purchasing process and make a purchase online if the experience is frictionless and provides a comfort level that they're getting the best value.	L&H/ P&C	Building on a. above, customers want their buying experience to be a straightforward process that provides perceived value for money. Take for example an insurance company that failed to create a seamless online buying experience for customers by requiring the same demographic information to be filled out on two different webpages and then verbally communicated back to the customer service representative on a phone call. The online and offline buying experience should be seamless, transparent and pleasant. It should use advanced algorithms to require less information from the potential customer while shortening the sales cycle and making effective pricing decisions.
c.	Product Innovation: As life expectancy increases due to advancements in medical technology, nutrition, etc., policyholders of life and health insurers worry less about dying prematurely and worry more about longevity risk, *e.g.*, depleting their nest eggs and maintaining their lifestyle after retirement. Property and casualty insurers aren't immune either. Products that truly reward policyholders with good habits, such as maintaining a claims-free record or taking effective precautionary measures during an impending storm, will become the products of choice. Insurers that fail to innovate and think around the corner or outside the box run the risk of irrelevancy.	L&H/ P&C	The insurance industry is known for being slow to embrace change and innovation. Therefore, insurance companies of all sectors and sizes must adopt a creative and innovative culture to remain relevant and competitive. A research and development unit could be warranted or partnering with an innovative service provider under certain circumstances. In addition, the ideation process for new products shouldn't just include product designers and pricing actuaries (the usual contributors) but can be cross-functional, including others (agents, back-office personnel, etc.) from within the company who aren't typically a part of the product development process.