














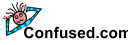




INNOVATION IN INSURANCE

In this brief article we look at four questions:

1. Why does innovation matter?
2. How strong is the insurance sector when it comes innovation?
3. In the insurance sector, what are and/or have been the barriers to innovation?
4. Going forward, where is innovation likely to add most value?

1 Why does innovation matter? Because it is one of the few ways in which an enterprise can build its capabilities, stay fresh, and become a market leader.

2 How strong is the insurance sector when it comes innovation? Overall, not bad. The table below is based on a customer's perspective of 'financial services'. Banks sell insurance, and insurance companies sell savings and investment products so we've ignored the silos (e.g. general insurance, health insurance, life insurance, protection, savings, investments, at-retirement, or pensions) to which industry insiders attach importance.

1966 	1967 The first ATM	1985 	1985 Critical Illness Cover to UK	1987 
1989 	1990 	1990 	1993 Admiral launches	1993 
1997 	1998 	2000 Maestro Prepaid Card launched	2001 	2001 
2002 	2004 	2005 	2010 	2010 










Perhaps we should challenge the conventional wisdom that consumers are not engaged with financial services: it is Protection and Pensions that seems to punch below their weight.

A 2011 paper by Cass Business School and the CII, *Innovation: Mapping the Role of the Corporate Leader*, made a number of important points:

- At Board level there is general agreement that 'Innovation is Important' because it is one of the few ways of developing sustainable competitive advantage – no organisation cost-cuts its way to a leadership position.
- At Board level there is a perception that insurance companies are not as good at innovating as they could or should be.
- There is an over-focus on product innovation and insufficient attention paid to other types of innovation that have a better track record when cost, risk and pay-off are taken in to account.
- Insurers do not seem to be as curious as other companies.

3 In the insurance sector, what are and/or have been the barriers to innovation? It would seem that a four part answer takes us some of the way to answering this.

- i. **Market conditions.** Innovation thrives when there is a lot of competition and/or when there are new entrants to a market. Neither condition really applies to insurance.
- ii. **Regulation.** In the Life & Pensions sector in particular, regulation and compliance dominate the business agenda and seem to have become substitutes for strategy. They also suck in a lot of scarce resources and affect the appetite for projects that actually make a difference.
- iii. **Corporate Cultures.** Innovation is most likely to add value when it is viewed as a corporate competence; when it as an integral part of the culture; and when senior people are measured on it. (Few Annual Reports by insurance companies refer to Innovation and its importance).
- iv. **Group think.** Every industry sector has its ‘group think’ – what Peter Drucker called, ‘The Theory of the Business’. Markets and consumers benefit when this is regularly challenged. For the reasons given previously, group think in insurance – particularly in the Protection sector – has not been strongly challenged. One aspect of this is the over-focus on product innovation mentioned earlier, so below we outline some other approaches to innovation that should be considered.

Type of Innovation	Description	Examples		
Customer-focused	Provides a new experience that customers perceive as valuable.			
Market - focused	A new business model that changes the dynamics of a market. (e.g. air travel, advertising, car insurance)			
Process / value chain	Changes to different parts of the value chain and its associated processes.			 Just in Time

4 Going forward, where is innovation likely to add most value to insurance companies?

- i. Applying insights from the ‘new’ discipline of **behavioural finance** to propositions and services.
- ii. Smarter use of information based on **actual consumer behaviour** rather than static proxies such as postcode, chronological age, or gender. (Consider Tesco offers to Club Card members, or Amazon’s use of predictive algorithms; the health-related data that the likes of Toumaz technologies collect; or location based services).
- iii. **Partnering** with organisations that have complementary perspectives such as the charities (higher EQ), or mobile phone companies (strong in m-commerce).
- iv. The growth of **unmet needs** based on changing consumer behaviour and demographics – more single parents, more complicated family structures, more singletons, more elective surgery.

The Bottom Line

The good news is that we now know quite a lot about innovation and how to combine it with process. Once the insurance sector attaches as much importance to imagination as it does to experience; and once it actually measures itself on innovation; we’ll see changes for the better.

POST SCRIPT

Several insurance folk who, between them, have more than a hundred years experience of the sector, were kind enough to provide a considerable amount of feedback regarding this article. Rather than revise the original I thought it would be helpful if I summarised what they had to say as a postscript.

There were ten key points which I have put in alphabetical order: you will have your own view of their relative importance.

1. Actuaries' influence
2. Branding
3. Complex distribution
4. Customer engagement
5. Execution
6. Fast follower
7. Knowing vs Doing
8. Mixed messages
9. Performance measurement
10. Pricing

1. **Actuaries' influence.** Only a numpty could claim that we could have an insurance industry without actuarial science at its heart. But do actuaries dominate the industry to its detriment? Does the profession's particular 'group think' stifle non-analytic thinking? Perhaps the actuarial exams should encourage different ways of looking at the same issue in much the same way as the Accountancy training involves current cost, historic cost and replacement cost accounting?
2. **Branding.** Organisations with strong brands seem to tune in intuitively to emotional intelligence, the value of intangible assets, and business renewal (updating the core brand proposition in response to changing market conditions). In the insurance sector branding is weak and too often confused with name recognition. This 'marketing-naive' mindset will inevitably see innovation as a low business priority.
3. **Complex distribution.** Ignore how we got here – but the fact is that today our distribution models are so complex that they discourage innovation because of the perceived free-rider risk.
4. **Customer engagement.** Once upon a time the market capitalisations of Unilever and Procter & Gamble comfortably exceeded those of the supermarkets. Not anymore. Retailers are bathed daily in large amounts of data that are transformed, with varying degrees of success, into information and insight. Retailers are plugged in to their consumers' behaviour and they've the service cultures to match. That is valuable. Insurers have nothing like this degree of engagement with their consumers. This, in turn, encourages slow learning and discourages innovation because it can't be done fast enough or confidently enough.
5. **Execution.** We can view innovation as **Insight + Execution**. Not only does the insurance sector underperform when it comes to the Insight element, but the Execution skills may be seen as a handicap also, because in the insurance sector execution is focused on compliance and getting it right first time, whereas retailers, for example, can execute quickly and 'well enough' and act on the results.
6. **Fast follower.** This strategy has a respectable history in the insurance sector and is not career threatening. Being innovative, on the other hand, can easily be seen as sticking-one's-neck-out and asking for trouble.

7. **Knowing vs Doing.** There's an irony here. The industry (along with Government) is assigning a good deal of time and resource to making consumers more financially capable in the belief that there is a big gap between what consumers actually know about finance and what we need to know. In fact the important gap is not between not-knowing and knowing; it is between knowing and doing. And the same is true when it comes to innovation in the insurance sector. The industry knows what to do. It knows that shareholders, customers, employees and the wider community would benefit if it became more innovative. But it chooses not to. There are higher priorities. There are habits to change. The costs and pain are immediate. The benefits are deferred.
8. **Mixed messages.** There are mixed messages not only between the industry and its customers but also within the industry itself. We sell promises. With some products the consumer can be confident that he or she can collect on that promise pretty much a hundred percent of the time. But not with all products. Mixed message number 1. In financial services, we implicitly criticise consumers for being financially feckless yet at the same time put more effort in to selling products that promote fecklessness (e.g. credit cards, loans, overdrafts) and less effort in to those that reward the behaviours we say are 'good' (e.g. savings, pensions, or protection). Mixed message number 2. This lack of clarity doesn't encourage innovation.
9. **Performance measurement.** You wake up tomorrow to find that you are the CEO of an insurance company. Consider what you will find in your in tray. Consider your corporate business agenda and priorities. Consider your corporate culture. Consider the **performance measures** that will drive the company regarding business-as-usual items such as advertising, capital adequacy, claims management, compliance, customer service, employee engagement, improved Governance, investor relations, and reducing operational risk. Where is innovation going to add most value? How confident can you be that the benefits of developing innovation as a corporate competence will outweigh the direct costs, opportunity costs, and risks?
10. **Pricing.** In our marketing we over focus on price and then complain when consumers do. We complain too about commoditisation when aggregators and our promotion campaigns encourage it. We also seem to feel that our industry is significantly different to other industries and that (a) what applies to them does not apply to us and that (b) innovation is an example of this. But who are we kidding?
 - Consider cars. Do BMW sell on price? No. They focus on brand, image, and perceived quality. Toyota sells on reliability. Skoda has repositioned itself and sells on value and quality.
 - Property? Location, location, location.
 - Clothing? Consider luxury brands (e.g. Boss, Givenchy), mid-market quality brands (GAP, M&S), and popular, low-price-good-value brands (Primark, TK Max).
 - Technology? Apple doesn't sell on price; nor do Blackberry, Dell, HP or Microsoft.
 - Air travel? Even the budget airlines pay attention to other aspects of the customer experience that build value – sophisticated online booking, developing the frequent-flyer habit, choice based on 'you get what you pay for.' The pricing is tactical rather than strategic.
 - Supermarkets? One might think that commoditisation would reign supreme, particularly with online shopping, but there's a good deal of innovation here around branding, customer information, competitor analysis, tie-ins to TV programmes and weather forecasts, and green issues.

Bottom line? Pricing is important, but perceived value is even more important. And we've been singularly unimaginative and 'innovation lite' in this part of the business.

End of postscript



Alan Newman spent most of his early years in Kuwait before coming to England and a military secondary school. After graduating with a degree in Psychology from University College London, he spent three years in Kenya on VSO as a science teacher. He then worked in the software sector before joining Digital where he worked in the Middle East and the UK. Between 1985 and 1987 he attended the International Advanced Management Programme at INSEAD and became a freelance consultant in 1992. Clients with whom he's worked include Aviva, AXA, Capita Registrars, Computershare, CSFB, Gulf Air, Hannover Re, Liverpool Victoria, the MoD, Shell, and Swiss Re. He has written for FT Finance and for The Journal of Brand Management.

References and recommended reading:

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