WORLD INSURANCE REPORT 2012

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TABLE OF CONTENTS

Preface

Capgemini and Efma are pleased to present the fifth edition of the *World Insurance Report* (WIR). Insurance companies around the globe are working hard to grow their businesses, despite today's challenging environment, in which costs are rising, and uncertainty persists about the financial contribution from investment income. The *WIR 2012* looks at how insurers are focusing their efforts on operational efficiency and effectiveness to protect and grow margins, even when demand is slow to increase.

The report specifically offers insights into how leading institutions are refocusing their efforts to reduce both cost per policy and total cost of ownership, and acting to improve the operational efficiency of their business processes.

The report builds on Capgemini's use of a proprietary Business Agility Maturity Model (introduced in the *WIR 2011*) to assess the functional maturity and leading practices of insurers across regions. This report also investigates the cost drivers for insurance companies across regions, and the increasing focus among insurers on transformation in the 'Policy Administration and Underwriting' Function.

The findings of the *WIR 2012* draw on research insights from 19 markets: Australia, Austria, Belgium, Brazil, Canada, Denmark, France, Germany, Hong Kong, India, Italy, Netherlands, Philippines, Singapore, Spain, Switzerland, the U.K., the U.S., and Vietnam. Among these countries are 13 of the world's top 20 insurance markets in terms of premiums. Included in the research were in-depth focus interviews with 71 insurance executives.

We are pleased to present you with this year's *World Insurance Report*, and hope our findings offer insight into the challenges and opportunities now facing the global insurance industry.

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Costs and Efficiencies Are the Critical Levers of Performance for Non-Life Insurers Today

CHAPTER 1

INTRODUCTION

Non-life insurers around the globe have been quick to respond to the effects of the global financial and economic crisis witnessed in 2008 and 2009. Many turned their focus in 2010 to the core drivers of underwriting performance, pursuing more cost-effective and efficient ways to acquire business and manage expenses and claims.

The reality is that even though premium volumes are rising in some markets, few insurers are in a competitive position to raise rates, few can expect any great contribution from investment income in the near-term at least, and few expect any major decline in claims. Many non-life insurers, and especially those in highly developed markets, also face a difficult task growing the top line, because insurance penetration (premiums as a percentage of GDP) and density (premiums per capita) are high, products are increasingly commoditized, and customers focus heavily on price.

As a result, for non-life insurers to achieve sustained performance in coming years, they will need to optimize client-acquisition and retention strategies, become more sophisticated in pricing risk, increase the efficiency of claims management, and undertake transformative initiatives in other key operational areas, such as policy administration (see Chapter 3).

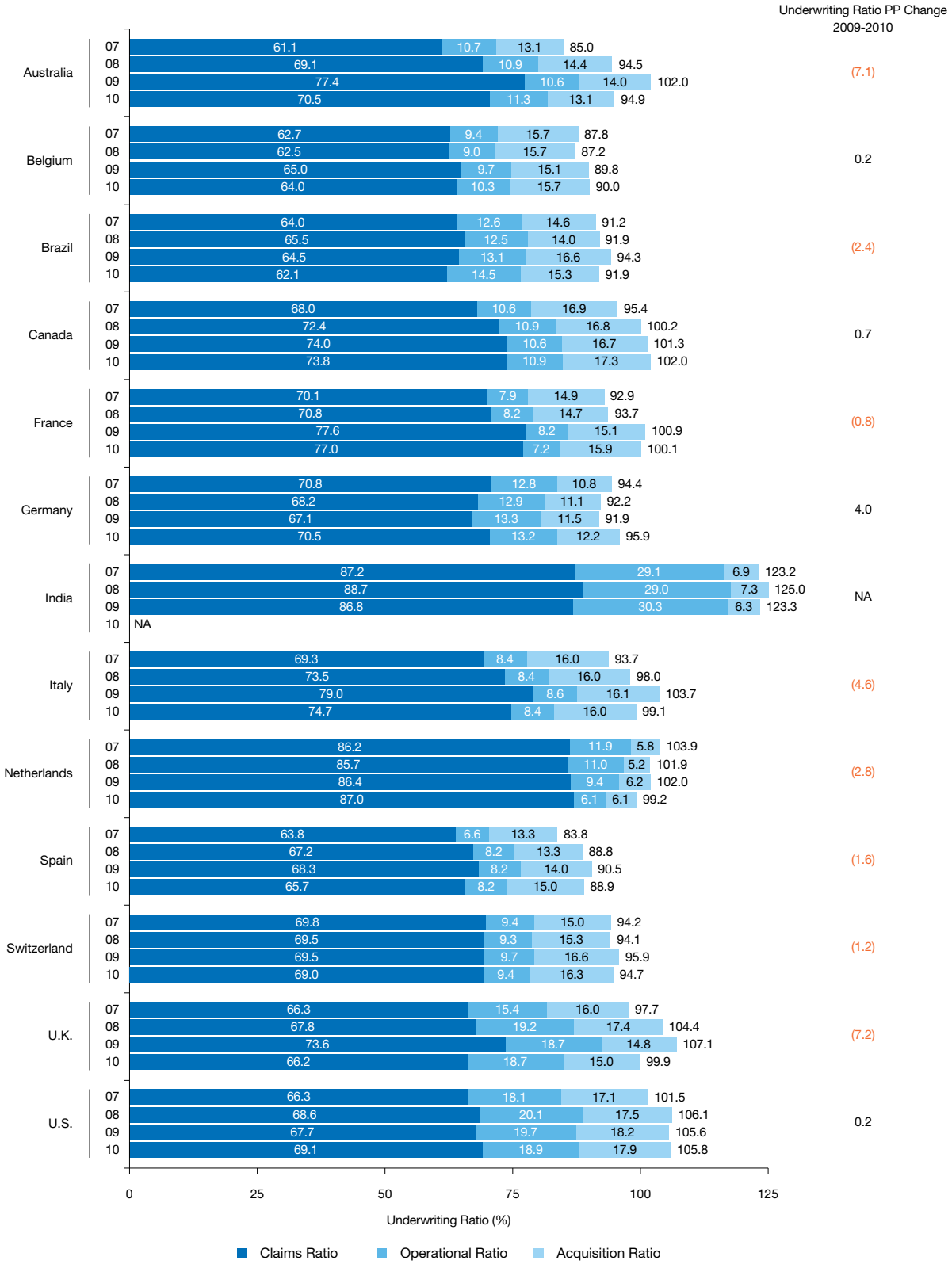
These conclusions are based on our study of the non-life segments in thirteen countries: Australia, Belgium, Brazil, Canada, France, Germany, India, Italy, Netherlands, Spain, Switzerland, the U.K., and the U.S. These countries together account for approximately 72%[1] of the global non-life insurance market.[2] For these countries, we used an Efficiency Model to calculate efficiency ratios (expense and profit metrics against gross written premiums (GWP)) for major players in each market, and to analyze broad industry performance trends by market accordingly.[3]

[1] Based on non-life premium volume for 2010 for the analyzed countries, and data from "World Insurance in 2010," Swiss Re Sigma Report, 2011

[2] See Methodology

[3] Since efficiency ratios depend on a variety of external factors, including general economic conditions, government regulation, business type, consumer preferences, etc., it is rarely relevant to compare ratios directly across regions. It is more germane to compare trends over time within regions, and perhaps within business types or insurance segments

Figure 1.1 Non-Life Insurance Expenses as a Percentage of GWP in Select Countries (%), 2007-2010



Note: The ratios are valid only for non-life insurance. The ratios reflect non-life data as reported by the countries themselves, and hence include health insurance for Belgium, India, Italy, Spain, Switzerland, and the Netherlands. At the time of analysis, no 2010 data was available for India, where the financial year ends March 31st. Ratios for prior years may have changed from those previously reported due to the restatement of results by some companies. PP refers to percentage points

Source: Capgemini analysis, 2011

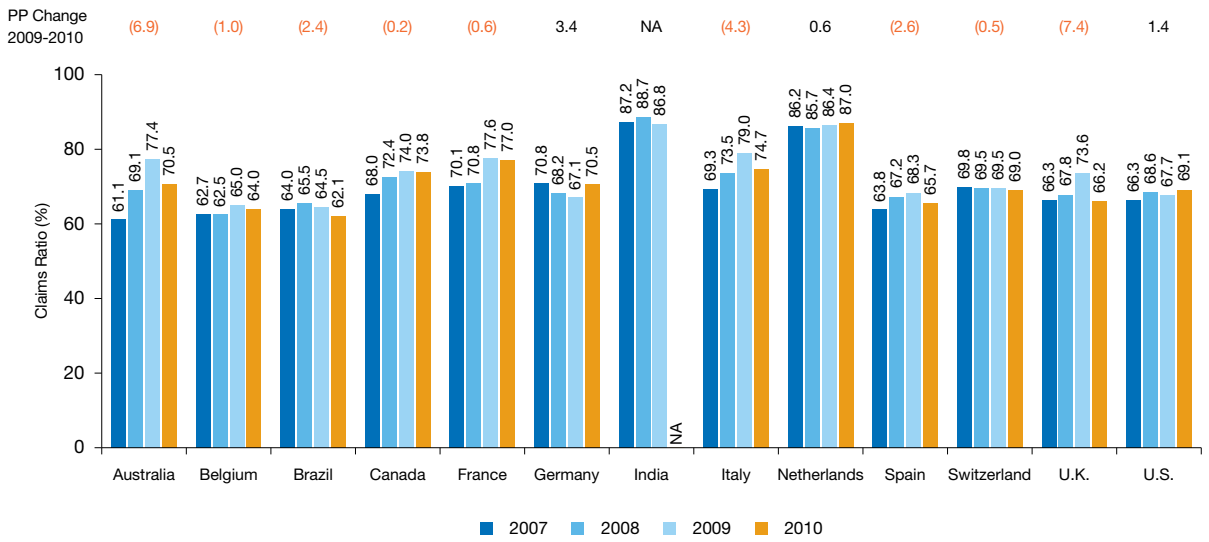
EFFICIENCY MODEL SHOWS CORE OPERATIONS ARE CRITICAL TO PERFORMANCE

Since profit margins declined in 2008 due to the effects of the global financial crisis, non-life insurers across the globe have been trying to reduce expenses across claims, operations, and distribution. There was an increased focus on underwriting performance in 2010, and an improvement was witnessed in many markets.

While many insurers have already enhanced operational ratios, their success varies enormously, especially given the distinct conditions in each market (detailed by country later in this chapter). However, the following general trends were evident from our analysis of non-life performance in 2010:[4]

- **Underwriting performance improved in many countries in 2010**, with declines in the underwriting ratio (claims ratio + acquisition ratio + operational ratio) showing that a smaller percentage of premium revenues was spent in claims and expenses in 2010 than in 2009 (see Figure 1.1).
  - A decline in the claims ratio (total claims and benefits disbursed/GWP) was the primary driver of better underwriting performance in Italy, Spain, and the U.K., as well as in Australia and Brazil, where the acquisition ratio (total commission and fees paid/GWP) also declined tangibly.
  - The underwriting ratio rose, however, in Belgium, Canada, Germany, and the U.S., due to higher claims and/or operational ratios (total operating expenses/GWP).
  - The underwriting ratio in India remained the highest across all the countries analyzed, as the industry there experienced both a high claims ratio and a high operational ratio.
- **The claims ratio declined in 2010 in most analyzed countries** (see Figure 1.2) as premium volumes grew, and fewer natural disasters occurred overall. These dynamics produced an especially strong improvement in the claims ratio in the U.K.

Figure 1.2 Claims Ratio for Non-Life Insurance in Select Countries (%), 2007-2010



Note: The ratios are valid only for non-life insurance. The ratios reflect non-life data as reported by the countries themselves, and hence include health insurance for Belgium, India, Italy, Spain, Switzerland, and the Netherlands. At the time of analysis, no 2010 data was available for India, where the financial year ends March 31st. Ratios for prior years may have changed from those previously reported due to the restatement of results by some companies. PP refers to percentage points

Source: Capgemini analysis, 2011

[4] Data for India refers to fiscal 2009, which ended March 31st, 2010

Still, claims ratios continued to reflect country-specific conditions, including the prevalence of catastrophic events, variations in premiums written, and changing regulations.

- The claims ratios of India and the Netherlands remained the highest among the analyzed countries. Dutch insurers continued to shoulder increased health-insurance claims after a new insurance act was introduced in 2006. The industry in India suffered from both inefficient underwriting practices and strong price competition.
- The claims ratio for the U.S. non-life insurance industry deteriorated in 2010, due to a significant rise in catastrophe-related expenses, and the continued weak underwriting performance of commercial insurance.
- The German non-life industry also had a higher claims ratio in 2010, as natural calamities and adverse weather conditions boosted claims expenditures across auto and property business lines.

- **The operational ratio remained relatively stable in many countries**, but the ratio was higher in India, the U.K., and U.S. than in other countries analyzed. The operational ratio of India's non-life industry remained the highest of all the countries analyzed, as both new and existing players have spent heavily to scale up their operations and/or capabilities. Brazil has also seen a rise in its operational ratio due to the scaling-up of operations, but major players there are expected to benefit from economies of scale after consolidation activity in the past few years. By contrast, the Dutch ratio dropped significantly in 2010, as insurers looked to become more efficient in a highly competitive environment. The ratio also remained low in France, as large players captured cost savings from initiatives undertaken in prior years.

- **A range of alternative distribution channels has emerged in recent years** and investment in technology has increased as insurers seek to generate cost efficiencies from their distribution networks. In some markets, this has helped to contain acquisition ratios, but the cost of acquiring new business remains high, especially when new business is generated by commission-based channels. In France and Spain, for instance, the acquisition ratio has increased, because agents and brokers remain the major distributors for non-life insurance products. The same dynamic is evident in German auto insurance. Still, non-life insurers across the globe are likely to continue experimenting with a range of alternative channels to generate growth and reduce expenses.
  - Brazil has witnessed an innovative example of alternative distribution, for example. Intermediaries are entrenched in the non-life insurance market there, but insurers have started to leverage the reach of widespread outlets, such as garages, petrol stations, pharmacies, department stores, supermarkets, and utility companies, to provide affordable and accessible insurance for the lower-income population of the country.

- **Investment incomes remain lower than before the global financial crisis of 2008 in most markets**. In 2010, the returns on non-life insurers' investment assets generally extended the recovery begun in 2009, but income is still lower in almost all markets than in the pre-crisis years. The Indian non-life industry continued to have one of the highest investment ratios globally as a result of significant exposure to rising equity markets, and prevailing high interest rates in the country. In general, though, the contribution of investment income to insurers' profitability is likely to remain far more limited than in the pre-crisis, because most insurers have adopted more conservative allocations (e.g., reduced exposure to volatile equity markets), either by choice or to comply with systemic risk and solvency regulations. Investment income could also suffer further if the global economy keeps slowing.

- **The profit margins for non-life insurers improved globally in 2010**, in line with rebounding investment returns, but they nevertheless remained sharply below pre-crisis highs (witnessed before 2008) in most markets. Many insurers also bolstered profits in 2010 by improving underwriting performance, though the U.S. managed to improve its profit margin despite a rising underwriting ratio. The profit margin declined tangibly in Germany, Italy, and Spain: In Germany, higher claims expenses wiped out profits; in Italy, regulation has especially driven up underwriting expenditure in auto insurance; in Spain, insurers have been unable to raise rates, because weak economic conditions have made customers more price-sensitive.

INSURERS IN MOST MARKETS SHARE A FOCUS ON COST AND OPERATIONAL EFFICIENCIES

With the decline in investment income, which once provided a constant profit stream for the non-life industry, insurers have been forced to concentrate on improving the building blocks of underwriting performance: claims, and operational and acquisition ratios. In many markets, the economics of risk pricing call for an increase in premium rates, but insurers face such competitive pressure that they have refrained from any significant rise in rates for fear of customer defections. As a result, the non-life insurance industry is looking to improve the process efficiencies in claims, operations, and distribution functions to lower their costs and enhance profitability.

In studying the non-life industries in thirteen countries (presented here alphabetically), we looked specifically at how insurers are performing with respect to the different components of underwriting performance. The study shows all non-life insurers are focused on reducing operational costs and raising effectiveness, but the options open to different players depend very much on market conditions.

AUSTRALIA

The Australian non-life industry is dominated by large-scale players after a decade of consolidation has resulted in there being just three major groups (Suncorp, Insurance Australia Group, and QBE Insurance Group). The three control more than two-thirds of total GWP.

The claims ratio of Australia's non-life insurers improved during 2010 as claims payouts declined and premium rates rose. Claims expenses had risen sharply in 2009, due to claims related to various weather events (including a higher-than-average number of home losses in bushfires), and inadequate pricing of compulsory third-party (CTP) motor insurance.

The performance of both personal and commercial lines improved in 2010, and the decline in the claims ratio for domestic lines was especially steep, as premium rates for personal lines rose for a second straight year: by 8% in 2010, after an 8% increase in 2009. Commercial-line coverage is more competitive, so insurers have been slower to push those rates up. Rates for commercial lines rose only 4% in 2009 and fell 1% in 2010.

Nevertheless, Australia's non-life market is relatively concentrated, compared to highly competitive markets like the U.S. and Germany, so insurers are likely to continue pushing up premiums to cover costs. Those rate increases could help to cover claims-related costs, and thus reduce the claims ratio, though 2011 has already seen numerous adverse natural events that are likely to increase claims payouts for the year.

Competition is also likely to increase in the Australian market, including entry and expansion by foreign players, so a price war could still ensue, making it more difficult for incumbent insurers to use price increases to cover costs. Still, insurers have also been improving underwriting results by focusing on better risk pricing, and improving reserve estimation for adverse natural events.

The operational ratio of Australia's non-life industry has been stable over the last few years, and is lower than many of the countries analyzed, because most incumbents have successfully leveraged their significant scale. Scale has also helped to keep the acquisition ratio in check. The ratio improved in 2010, declining by 0.9 percentage point to 13.1%, after edging down 0.4 percentage point in 2009. However, those improvements came after a significant jump in 2008, at the height of the financial crisis.

BELGIUM

The Belgian non-life insurance market has a higher level of market penetration than some of the larger markets in Europe, including France and the U.K.

The claims ratio for the Belgian non-life insurance industry improved marginally in 2010, declining 1.0 percentage point to 64.0%, after a 2.5-percentage-point increase in 2009, when the claims ratio had increased across all lines of business. Despite the slight improvement in 2010, the claims ratio could rise in the future, potentially forcing insurers to increase premium rates in coming years. The claims ratio for auto coverage is under particular pressure, due to intense industry competition, the increasing frequency and severity of accidents, and the surging cost of repairs and medical care.

The operational ratio for the non-life industry has also risen in the last two years, after declining from 2006 to 2008. This has left insurers little choice but to invest in operational efficiencies going forward.

The industry's acquisition ratio also increased marginally in 2010, as a rise in premium volumes increased commissions paid. The acquisition ratio in Belgium remains higher than in most European countries, even though the industry continues to explore alternative, lower-cost channels.

Direct distribution had been rising steadily (accounting for 20.9% in 2007, up from 15.2% in 1998), but has stagnated more recently, and accounted for 20.1% in 2009. Bancassurance has grown at a fast pace over the last decade, but still accounted for just 6.9% of the non-life market in 2009, though that share is higher for personal lines such as home insurance (18.2%). The expansion in direct and alternative distribution is likely to continue in coming years nevertheless.

BRAZIL

The Brazilian non-life insurance market remains the largest in Latin America, and has witnessed one of the fastest growth rates in the world in terms of non-life GWP in last few years. However, market penetration is still low compared to that in a few of the smaller countries in the region. Brazil's insurance regulators continue to push the adoption of international best practices, which should strengthen the system's controls and health, and provide insurers with a firmer base from which to expand their operations.

The claims ratio of Brazil's non-life industry dropped 2.4 percentage points to 62.1% in 2010, after a percentage-point drop in 2009, mainly due to decreased claims expenditures in auto lines. Auto insurance accounts for more than half of all non-life premiums in Brazil, and insurers have raised premium prices, by 14% across non-life, and improved loss controls in the auto segment. Also, the Brazilian reinsurance market has become increasingly competitive since deregulation in April 2008, and reinsurers are likely to push for improvements in the underwriting and risk management capabilities of non-life insurance players, which could help insurers to reduce claims costs.

Notably, Brazil's insurers have effectively managed their claims expenditures, even in a high-growth environment. Non-life premium volumes jumped 13.3% in 2010,[5] and the robust rate of growth in this emerging-market economy could drive further business expansion in coming years. This is likely to push insurers to increase infrastructure spending, and perhaps increase scale through consolidation, to capture efficiencies and ensure sustained profitability.

The industry's operational ratio has increased in the last two years, as insurers invested to expand their business. Consolidation and scale efficiencies could reduce that ratio in the future, although insurers will need to continue spending to capture improvements.

The industry's acquisition ratio dropped a little in 2010 as the economy helped to boost business, but Brazil's insurance products are still distributed mainly through intermediaries, and direct-sales channels have faced resistance. Convention and the legal system heavily favor brokers, which are strongly unionized, and politically influential. However, insurers have developed a new low-cost alternative channel leveraging widespread outlets, such as garages, petrol stations, pharmacies, department stores, supermarkets, and utility companies, and this has helped them to reach the lower-income population at low distribution cost.

CANADA

Canada is one of the world's top ten non-life insurance markets in terms of GWP, but the market is highly fragmented, populated by both global and local players.

An elevated claims ratio continues to result in underwriting losses for the Canadian non-life insurance industry. Adverse weather conditions have prevailed in the last three years, including tornadoes and hailstorms in 2010. The claims ratio dipped marginally to 73.8% in 2010 from 74.0% in 2009, but the severe weather and water-damage claims have helped to make personal-lines business

[5] Based on non-life premium volume for 2009 and 2010 in local currency (Brazilian Real), and data from "World Insurance in 2010," Swiss Re Sigma Report, 2011

unprofitable. The claims ratio has been especially high in auto insurance, but Ontario reforms announced in September 2010 could help drive cost savings by providing insurers with more flexibility to customize risk pricing and improve risk selection. Such actions could reduce the claims ratio.

The industry's operational ratio has largely held steady in recent years, and local Canadian insurers have tended to fare less well than large global players, which have more scale to drive efficiency in key elements of the business, including capital, research, and advertising. Still, the non-life industry has suffered an underwriting ratio of more than 100% for three straight years, so most insurers will need to make additional investments to improve operational efficiency. Consolidation may also occur among smaller players.

The acquisition ratio has also been high in Canadian insurance, and increased 0.6 percentage point to 17.3% in 2010, as agent commissions grew with the increase in premium volumes. The Internet is gaining traction as a low-cost alternative, though, and customers are keen to shop around for the best prices. As a result, insurers with Internet offerings could capture significant cost savings and potentially increase market share going forward.

FRANCE

France is the third-largest non-life insurance market in Europe, and the fifth largest in the world.

The claims ratio of the French non-life industry improved in 2010, but has been high in last two years, mainly due to natural catastrophes, most notably in 2010 from the impact of storm Xynthia and flooding from storm Var, and in 2009 from the effects of storms Klaus and Quinten. As a result, French non-life players will need to leverage best practices in weather-related underwriting to control claims costs going forward. Separately, motor insurance continues to be underpriced due to the high level of competition, creating even more cost pressure for insurers operating in that segment. Insurers exposed heavily to small businesses have also seen disproportionately high claims in their commercial lines, as small and medium-sized enterprises have experienced considerable volatility in earnings during the economic slowdown in recent years.

The operational expense ratio of France's non-life industry was better than in most of the other analyzed countries in 2010, largely because premium volumes increased while non-life insurers continued to pursue efficiencies. Large global non-life insurance players tended to have better operational ratios than smaller players, due to economies of scale. Also, a few of the large French insurance firms had invested heavily in process optimization before 2007, which has translated into reduced operational ratios since 2007. More recently, many major non-life players have announced new cost-savings initiatives for 2011 and 2012, as they seek to offset underwriting losses. As a result, the non-life industry's operational ratio is likely to improve further over the next few years in France.

The non-life acquisition ratio increased marginally in 2010, with agents and brokers still forming the major distribution network in the French non-life market. Nevertheless, insurers are keen to improve their cost efficiencies, and are looking to reduce acquisition ratios by developing low-cost channels, restructuring traditional channels (and existing agent models), and focusing on multi-channel strategies. Bancassurance has expanded as an alternative channel, although the growth has slowed in recent years, and many insurers are now focused on the cost-saving potential of the Internet as a channel.

In 2010, the industry's profit margin improved slightly, mainly due to an increase in investment income and a decline in the underwriting ratio. Still, commoditization in insurance products, and price transparency and customer awareness in this mature market, have prevented prices from keeping pace with the increasing cost of claims in the past two years.

GERMANY

Germany is the second-largest non-life insurance market in the world, and the largest in Europe. In Germany, insurance is mandatory for everyone, fueling the segment's growth. Most of the major non-life players are German, though a few pan-European giants also have a tangible presence.

The claims ratio of German non-life insurers deteriorated significantly in 2010, rising by 3.4 percentage points to 70.5%, mainly due to increased motor and property claims after storm Xynthia early in the year, and flooding from the Spree and Neisse rivers in the summer. The claims ratio is expected to improve in 2011, however, as the number of weather-related claims events appears to be lower than in 2010.

The operational ratio of the German non-life industry rose marginally in 2010, after a similar rise in 2009 but a slight year-on-year decline in 2006-08. The larger global non-life insurance players have had lower operational ratios, as they have the scale to shoulder the hefty capital, research, and advertising expenses required for non-life. However, most insurers operating in Germany are local and are smaller than these global players, and they continued to suffer from high operational ratios. As a result, the industry as a whole is expected to make investments in efficiency initiatives going forward.

The acquisition ratio of the German non-life insurance industry has increased marginally over the past few years, as the industry continued to distribute heavily through intermediaries, such as agents and brokers. Motor insurance is the largest single line of business, and its main distribution channel is the agent network. (Tied agents are in the majority, and account for more than half of market share.) The role of bancassurance remains limited in Germany, largely because the prevalence of small and regional banks impedes widespread distribution of standardized products throughout the country. Going forward, the German non-life insurance industry has an opportunity to reduce the acquisition ratio by developing and utilizing low-cost direct-sales channels.

Investment income for German non-life insurers dipped slightly overall in 2010, but a new ordinance on the Investment of Restricted Assets of Insurance Undertaking (AnIV) took effect in July 2010, and allows insurers to make new types of investments, including certain closed-ended real-estate funds, shareholder loans to real estate companies (which could produce interest income), and commodities. This new regulation could prompt German non-life insurers to increase their investments in alternative vehicles, such as real estate and private equity, potentially changing the contribution of investment income.

The profit margin for the German non-life insurance industry has seen significant erosion in the last couple of years, and the decline in 2010 was fueled by a rise in claims expenses, a drop in investment returns, and the lack of any significant increase in prices due to significant competitive pressure. If these dynamics endure, it could lead to consolidation among German insurers, especially as this highly developed market offers little room for significant additional expansion.

INDIA

India's non-life insurance industry is in a nascent stage compared to the other analyzed countries. Insurance penetration is very low, except for compulsory third-party motor insurance. However, privately held insurers are increasingly looking to penetrate health insurance.

The claims ratio of the Indian non-life industry remained high in 2009 (the most recent year for which results are available), even though no major covered catastrophes have occurred since 2005, except for the 2008 Mumbai terror attack. The claims ratio is largely driven by inefficient underwriting practices and price competition, and claims have been especially high in health and fire insurance. The claims ratio in health insurance was 111.1% in 2009, showing that GWPs remain far less than the claims and benefits disbursed on that coverage, especially given escalating medical costs. By contrast, the claims ratio for motor and marine insurance has improved, and this has especially helped public-sector (government-owned) insurers, for which the claims ratio dropped to 88.3% in 2009 from 91.3% in 2008. Private-sector insurers are more efficient overall, however, and have a lower claims ratio than the public-sector firms.

The operational expense ratio of India's non-life industry has been high for the last four years, as new and existing players invest in building capabilities and/or scaling up their operations. These dynamics are expected to last for some time, pushing up operating expenses for the industry as a whole. In 2009, the operating expenses of non-life insurance companies were up 13.9% from 2008, and the industry's operating ratio rose 1.3 percentage points to 30.2%. These ratios are likely to remain high as new private and international players continue to enter Indian insurance market.

The non-life industry's acquisition ratio declined slightly overall in 2009, but mostly because of the private-sector players, which are increasingly looking to tap cheaper distribution channels, such as the Internet, and introduce exclusive products for these alternative channels to reduce commission costs. Public-sector players, by contrast, continue to have large distribution forces, adding to their acquisition expenses. Overall, the total commission expenses for India's non-life insurance industry rose by only 6.3% in 2009, despite a 14.0% increase in GWP,[6] but consistent losses on underwriting are likely to push insurers to explore a variety of alternative channels, including online distribution, bancassurance, and non-banking financial companies (NBFCs).

Investment income rose significantly in 2009, largely because equity markets rose. The Indian industry's investment ratio was the highest among the analyzed countries due to equity exposure (though returns remain below pre-crisis levels), and this helped to compensate for poor underwriting results.

ITALY

Italy is one of the largest non-life insurance markets in Europe, but market penetration is low, with individuals typically resorting to minimal and compulsory coverage. There are a few large international insurances companies, but most insurers are Italian, and only a few of those players, such as Generali, have a strong presence globally.

The claims ratio for Italy's non-life insurance industry improved significantly in 2010, dropping by 4.3 percentage points to 74.7%, helped by a decline in car theft and auto accidents, as well as lower liability claims from injury cases. The ratio's decline followed a jump of 5.5 percentage points in 2009, which was partly driven by reforms in auto insurance, which accounts for more than 50% of non-life premiums in Italy. The Bersani Law enacted in 2008 increased competition in auto-insurance pricing and distribution, and a Milan court decision in 2009 on bodily-injury claims required insurers to increase reserves for such indemnities. Both initiatives have further increased claims costs for non-life insurers.

Italian non-life insurers also continue to suffer from higher-than-average fraud rates, especially in the auto sector, where fraudulent claims are estimated to represent nearly 10% of all claims, the highest rate in Europe. The burden of fraud is expected to push Italian non-life insurers to allocate more investments to claims management systems so as to enhance fraud-detection capabilities.

The investment in claims systems and other technology might add to operational ratios in the short-term, though the ratio for Italy's non-life industry has held fairly steady in recent years, and industry consolidation has generally allowed players to capture scale efficiencies and contain costs.

The industry's acquisition ratio has also remained stable, though it is relatively high compared with other European markets, as distribution is dominated by agents, which account for more than 80% market share in non-life insurance. Going forward, the industry will need to diversify its distribution strategies, find ways to reduce the cost of commissions being paid to agents, and develop alternative and lower-cost channels. To date, for example, brokers and direct sales contribute very little market share, and bancassurance still accounts for less than 5%.

Profits have eroded in the Italian non-life insurance market over the last three years, and have failed to recover since the height of the global financial crisis to the same degree as many other insurance markets. Non-life players are now looking to diversify and grow other products lines to improve their profitability, as the dominant auto sector remains under pressure, and the government is resisting increases in auto premiums.

[6] Based on non-life premium volume for 2009 and 2010 in local currency (Indian Rupees), and data from "Annual report 2009-10," IRDA, 2011

NETHERLANDS

The non-life insurance market in the Netherlands is mature, and is one of the top ten largest in the world in terms of GWP.

The claims ratio of the Dutch non-life industry remains among the highest globally, mainly due to the surge in health-insurance claims following the introduction of compulsory coverage in 2006. Since the 2006 mandate, health-insurance providers have competed largely on premium rates, despite being unfamiliar with risk pricing in the segment. As insurers garner more experience of actual consumption patterns and claims rates in health coverage, they should be able to manage the claims ratio more effectively, and improve price estimation. Beyond health insurance, non-life players also had to manage a substantial number of claims related to severe weather in almost every season of 2010, and this added to the industry's aggregate claims ratio.

The industry's operational ratio improved in 2010, however, as non-life insurers moved proactively to cut expenses and become more efficient in this highly competitive market. The ratio dropped 3.3 percentage points to just 6.1% in 2010, after falling 1.6 percentage points in 2009 to 9.4%. Notably, the workforce of the entire insurance sector shrank by 2.5% in 2010, cutting salary costs significantly.

The Dutch industry's acquisition ratio remained stable, and relatively low, with competition heating up from low-cost alternatives. Internet-only providers, for example, are moving aggressively into non-life products, primarily car insurance, which continues to drive down premiums. The Internet is also proving popular with customers, who like to compare products and prices online, and are quick to switch providers.

These trends are especially challenging to the position of established players, whose market share is being attacked. Regulation is also adding to the competitive pressure, with regulators halting the practice of automatic policy renewals, and thereby creating another opportunity for providers to vie for the business of other firms.

SPAIN

Non-life insurance penetration in Spain remains low compared to other major European markets such as Germany, Italy, the Netherlands, Switzerland, and the U.K., suggesting the market has greater growth potential and further room for improvement than those markets. Competition is significant in all insurance lines of business, however, because while there are a large number of insurers, the market is concentrated. Fifteen companies, for instance, account for 72% of all non-life GWPs. The pressure of market competition, combined with the price-sensitivity of customers and the capital requirements from Solvency II, could drive further concentration in the Spanish insurance industry, forcing some companies to merge.

The claims ratio of the Spanish non-life insurance industry dropped 2.6 percentage points to 65.7% in 2010, but remains above 2007 levels. The operational ratio has been stable since 2008 at around 8.2%, and remains at the lower end of the range among European peers. Spain's non-life industry is mature and competitive, so insurers have long had to focus on growing their customer base while controlling costs. In 2008, investments in efficiency initiatives caused a jump in the operational ratio of 1.6 percentage points, from 6.6% in 2007 to 8.2%, as those investments occurred at a time when premium volumes were growing only marginally. Given the stagnation in premium volumes since, and the already low operating ratio, new investment in efficiencies might be limited in the coming few years.

Premium volumes have fallen in the last two years, by 3.5% in 2010 and by 2.2% in 2009,[7] due to a decline in industrial activity, a drop in vehicle sales, and a shifting customer preference toward lower coverage. (Health insurance premiums have been rising, however, and volumes gained 5.5% in 2010.[8]) This decline in premium volumes has created stiff price competition, which is also intensifying due to the rise of new low-cost direct insurance providers. However, the first half of 2011 witnessed a small improvement in the profit ratio, as the claims ratio edged lower due to growth in premiums volumes in some lines of business, such as health, and a decline in the frequency of claims in auto insurance.

[7] Based on non-life premium volume for 2009 and 2010 in local currency (Euro), and data from "The Spanish Insurance Market in 2010" and "The Spanish Insurance Market in 2009," INESE, 2010, 2011

[8] Based on health insurance premium volume for 2009 and 2010 in local currency (Euro), and data from "The Spanish Insurance Market in 2010," INESE, 2011

Still, insurers have been slow to raise premium rates, and many have reduced premium prices, because customers in Spain are very sensitive to price hikes. At the same time, insurers have had to spend to attract customers, putting upward pressure on acquisition costs. That pressure has been compounded because commission payouts per-policy to brokers and agents have not declined as prices have dropped.

Brokers and agents together account for the majority of non-life insurance premiums in Spain, although the agent share has fallen steadily from 45.0% in 2001 to 39.5% in 2009, while the broker share has grown from 23.0% to 26.5%. While agents and brokers dominate, bancassurance has emerged as a fast-growing distribution channel in Spain, as it has in many European markets, and the non-life industry is expected to see increasing competition from low-cost direct insurers, which will put even more pressure on insurers to reduce premium prices. The push into bancassurance is being driven by the restructuring of the Spanish financial system, the concentration of savings banks, and the need for Tier 1 capital requirements imposed by Basel III regulation. These dynamics are causing financial institutions to focus on the life segment, and sell their non-life insurance businesses, while retaining joint ventures with insurance companies to distribute non-life products. However, bancassurance is not the only channel that is growing. To be more competitive, insurers are increasingly investing in new direct brands or entities (e.g., telephone or Internet) for distribution and service provision, especially in the auto-insurance segment.

The investment ratio of Spain's insurance industry grew in 2010, as compared to the financial crisis period of 2008-2009. Nevertheless, this ratio will remain linked to the performance of the stock market (which has generally under-performed in 2011), and the resolution of the European debt crisis. Spain's insurance players have traditionally been conservative in the allocation of their investment portfolios, keeping a high proportion in fixed-income securities, generally of good quality. Nevertheless, with stock-market values generally in decline, the DGSFP (Dirección General de Seguros y Fondos de Pensiones) is considering softening regulation to enable insurers to include in regulatory capital calculations some assets with lower ratings (certain assets with BB and B ratings).

In general, given prevailing market dynamics, Spain's insurers will have to focus on a combination of cost reduction strategies (for long-term sustainability), and growth strategies with limited investments. These investments could be allocated to product innovation, or to expand product portfolios through joint ventures/M&A, implement new channels (mainly Internet and bancassurance), or explore opportunities in emerging markets (mainly in Latin America). Such moves could minimize insurers' dependence on a limited range of products, distribution channels and geographies. This would require flexible platforms (policy administration, claims and billing) to complement business strategies.

SWITZERLAND

Switzerland's non-life insurance industry has one of the highest penetration rates in the world, higher even than in the U.K. or U.S.

The claims ratio improved slightly for Switzerland's non-life insurance industry in 2010, declining 0.5 percentage point to 69.0%. The claims ratio has held fairly steady over the last five years, but 2010 saw fewer covered claims from weather events, such as the hail storms that had increased motor claims in 2009. Also, in August 2010, the Swiss Federal Court revised compensation for whiplash injuries, reducing the claims for motor vehicle liability insurers.

Switzerland's non-life insurance players continue to derive substantial profitability from the core business of underwriting. Recent improvements in risk-underwriting measurement, for example, have contributed to a decline in credit/surety claims. The operational ratio of the non-life industry also improved marginally in 2010, but has varied only slightly in recent years, and operational efficiency has and will be a critical focus for insurers.

The Swiss acquisition ratio decreased marginally in 2010, after trending upward from 2006 to 2009, amid increased competition in this already saturated non-life market. Alternative distribution networks, such as bancassurance and the Internet, have not been significant in the Swiss non-life market to date, but may offer cost-saving potential in future.

The Swiss insurance market operates in a very tight regulatory framework, with stringent limits on investment portfolio allocations creating a very conservative investment approach. Indeed, over 40% of non-life insurers' investments are allocated to fixed-income instruments, and exposure to equities is minimal.

U.K.

The U.K. is the fourth-largest non-life insurance market in the world, and the second-largest in Europe. The non-life market is saturated, with most households having some form of insurance.

The claims ratio of the U.K. non-life insurance industry slid 7.4 percentage points to 66.2% in 2010, largely due to increased premiums, and a decline in adverse natural calamities. Personal-line premium rates rose significantly, mainly in motor insurance, which has suffered significant claims losses in the past several years. Commercial premiums rose in early-2010, but the rate of increase abated later in the year, as insurers sought to protect potentially defecting business. Overall, the claims ratio also benefited from the absence of any major natural disasters or major events like the floods of 2007 and 2008. As the U.K. non-life sector continues to focus on improving its underwriting ratio, premiums could continue to rise in the medium-term.

The operational expense ratio of U.K. non-life insurers remained at the high end of the range at 18.7% in 2010, but it is a similar ratio to that of the U.S. Going forward, the increasing pressure from operational expenses is likely to force U.K. insurers to streamline operational and administrative processes, and invest in long-term efficiencies in this highly competitive market.

The changing distribution pattern for non-life insurance products has helped to drive a decline in the U.K. acquisition ratio over the last two years. Brokers still account for the largest single share of insurance sales (37% in 2009), but that share has been declining over the last decade or so (from 52% in 1999). More recently, the use of new and lower-cost alternatives has been growing. For example, the share of sales through banks and building societies was 13% in 2009, up from just 5% a decade earlier. The Internet has also emerged as a fast-growing medium of direct sales, and the share of insurance products sold via the Internet is certainly higher in the U.K. than in other European countries. The use of non-broker alternatives is also likely to increase further in coming years.

The profit margin for the U.K. industry increased in 2010, as insurers raised premiums despite the highly competitive conditions. However, profit margins remain well below 2006 levels, and U.K. non-life insurers still need to cut their underwriting losses, and look to make core business more profitable, in order to thrive in the longer-term.

U.S.

The U.S. is the world's largest non-life insurance market. The majority of households has one or more types of insurance, and the market is highly competitive, with many specialty and general insurance providers, which provide the bulk of products. Motor insurance is mandatory, and accounts for the largest single segment of non-life coverage.

The claims ratio for the U.S. non-life insurance industry deteriorated from 67.7% in 2009 to 69.1% in 2010, as hefty weather-related personal lines claims and weakness in commercial line insurance undermined underwriting performance. The homeowners market, in particular, experienced more claims, especially as inland losses increased from winter storms, tornadoes, and hail storms. Commercial lines of business were pressured by a decline in premium rates, due to competitive pressure, and the ongoing tendency for insureds to opt for lower coverage amounts amid the weak economic conditions.

The rate of decline in commercial rates slowed in 2010 and early-2011, however, and there was even a slight increase in premium rates for some commercial property and worker compensation products. The auto-insurance business has also been affected by the economic recession, and premium volumes fell in 2010, due to a decline in new-vehicle sales, and a preference for lower coverage amounts among policyholders. Notably, though, the decline in claims and claims-related expenses was proportionally less than the decline in premium volumes, so the claims ratio still rose.

The operational expense ratio of U.S. non-life insurers overall declined marginally in 2010 as premium volumes increased. Large players also captured cost efficiencies from economies of scale, and leveraged prior investments in enhanced technologies. (The operational ratios for small and medium-sized insurers were higher, however.) U.S. non-life insurers are expected to increase their IT investments further in order to improve operational efficiency and reduce costs, focusing in particular on claims-processing and policy-administration technologies.

The acquisition ratio fell slightly for the U.S. non-life insurance industry in 2010, as premium volumes increased overall. However, this followed three years (2007, 2008, 2009) in which the acquisition ratio had increased, because premium volumes declined while insurers spent on developing alternative distribution channels. Moreover, the U.S. non-life acquisition ratio is one of the highest in the world, because the market is highly developed and competitive, so insurers invest in a wide variety of distribution strategies to try and capture and expand their market share. More recently, though, insurers have increasingly invested in Internet and mobile distribution channels to expand their reach and deliver better and faster customer service. These channels could ultimately result in reduced acquisition costs.

CONCLUSION

Many of the world's non-life insurers have experienced gains in profitability in the last two years, as investment income recovered from the lows posted at the height of the financial crisis in 2008. However, the ongoing effects of the economic recession are palpable, and remind insurers that they cannot rely on investment income to shore up performance.

Rather, insurers need to focus on the key components of underwriting performance, and must look for ways to minimize their claims, acquisition, and other operational costs, while growing their business. Smaller players may need to consolidate to gain critical mass and achieve enough scale to diversify, but all insurers will need to dissect their businesses to decide which initiatives will deliver advantage in whatever competitive and operating environment they face.

Some progress was made in 2010, but the focus on improving underwriting efficiency is likely to continue in coming years, especially given ongoing economic weakness across the globe in 2011, and particularly in Europe, which may lead to further declines and volatility in investment income. Core operational functions, such as policy administration, offer one of the few remaining areas in which transformation can deliver both cost savings and customer benefits.


30

Business Agility Survey Shows Investment in Several Policy Administration Sub-Functions Is Paying Dividends

CHAPTER 2

INTRODUCTION

Business agility measures the speed with which insurers understand and respond to changes in the external and internal operating environment to remain competitive. As such, business agility is very important to insurers today, as they face continually evolving social, market, regulatory, and technology trends. Among those trends are: fast-changing customer needs and buying behaviors, driven by changes in demographics; market forces of consolidation, convergence, and globalization; increased commoditization and competition; innovation and integration in distribution patterns; more stringent regulations; and evolving technology.

The analysis of business agility for WIR 2012 focuses on performance in Policy Administration and Underwriting, and shows the insurance industry has, on average, progressed farthest in achieving agility in certain core policy administration (PA) back-office levers: Confirmation of Coverage and Policy Issuance; Policy and Contract Maintenance; Billing and Premium Invoicing; and Premium Reminders and Renewals. Agility is higher in these areas than in other PA sub-functions, and it is notable that these are areas in which insurers have been investing in recent years to enhance cost efficiency and effectiveness.

The agility of insurers is now likely to improve noticeably in the near-to-medium term in other areas, especially Rate-and-Quote capabilities, and Underwriting and Risk Analysis. This is largely because there has been an increasing focus on offering online rate modification capabilities to all channels, and greater use of advanced analytics tools to support the underwriting process.

The degree of agility is also progressing steadily in Product Set-up and Compliance, due to specific demands in those areas: Market competition and changing customer preferences are driving insurers to increase their speed to market for products, and the global focus on regulatory stringency is requiring all insurers to put rigorous processes in place to manage changing requirements and standards.

Agility in PA and Underwriting is not consistent across insurers or regions, however. Of surveyed insurers, larger firms tended to exhibit higher maturity on most agility levers than smaller ones, especially on levers that are generally centralized and core to business. Medium and small insurers typically scored higher on levers focused on business acquisition and retention than on other levers. U.S. and European firms tended to be more agile than those in many emerging Asia-Pacific and Latin American markets, largely due to their more extensive investments in, and use of, advanced technologies and analytics.

PA AND UNDERWRITING AGILITY HINGES ON EIGHT KEY PERFORMANCE LEVERS

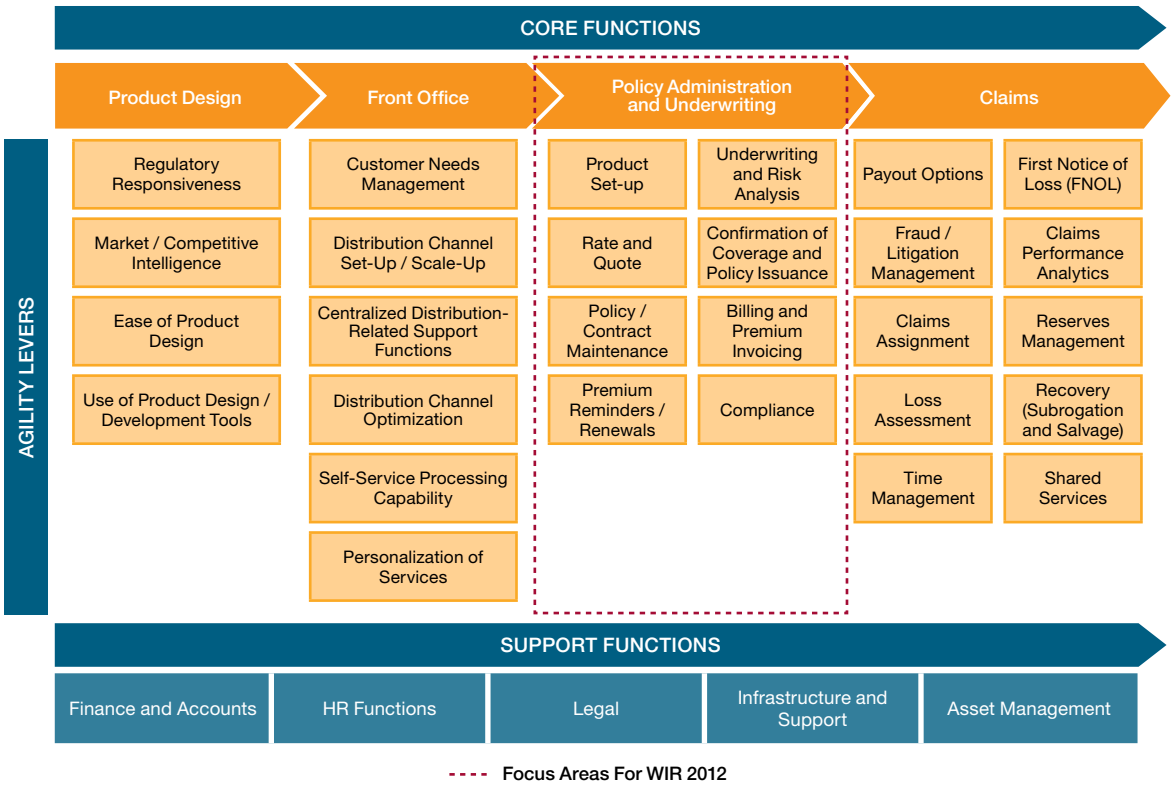
Capgemini's Insurance Business Agility Maturity Framework divides the insurance value chain into four core insurance functions: Product Design; Front Office; PA and Underwriting; and Claims. The model further divides each of these insurance functions into sub-functions called levers, and identifies five maturity levels for agility in each lever (see Figure 2.1 and methodology for more detail).

The 2012 WIR focuses on business agility in the PA and Underwriting function of the insurance value chain. In short, the greater the agility in PA and Underwriting, the more efficient insurers are likely to be in policy issuance and servicing, and the more effective they can be in reducing operational costs. (WIR 2011 was focused on agility in the Front Office and Claims segments of the insurance value chain.)

The following are the eight levers of agility in PA and Underwriting, and some examples of the maturity spectrum (see Figure 2.2 for more detail on the five distinct levels of maturity):

1. **Product Set-up.** How flexible insurers are in setting up or modifying products, and making them available to marketing/sales. Maturity ranges from manual set-up of new products/enhancements (maturity Level 1) to integration with enterprise-level analytics, documents, and content management systems (Level 5).
2. **Underwriting and Risk Analysis.** The degree to which insurers use underwriting tools, such as automated workflow management and rules engines, to help underwriters focus on their core job of assessing risk and controlling the quality of risks being underwritten. The most basic level of agility relies on manual/semi-automated processing of all submissions, while the most mature leverages advanced analytics, such as predictive models, to make underwriting decisions.
3. **Rate and Quote.** How able insurers are to provide accurate rates, and quote to their customers in real-time. Capabilities range from semi-automated rates/quotes for simple to complex risks to advanced analytics, including predictive models, for risk rating.
4. **Confirmation of Coverage and Policy Issuance.** How efficiently insurers can deliver confirmation of coverage and policy/contract documents to

Figure 2.1 Capgemini Insurance Business Agility Maturity Model's Framework



Source: Capgemini analysis, 2011

customers. The most basic approach involves manual processing and issuance of confirmation of coverage and policy/contract documents, while the most agile insurers integrate confirmation of coverage/issuance into external entities so as to support the self-service needs of customers/channels/partners.

5. **Policy/Contract Maintenance.** How swiftly insurers can process policy-change requests, lapses, and reinstatements, and endorsements (in-sequence and out-of sequence). Capabilities again range from piecemeal and manual to fully integrated.
6. **Billing and Premium Invoicing.** How efficiently insurers process the billing and premiums invoicing activity for new as well as renewal business. The least agile insurers still use traditional billing via 'snail mail' and do not integrate with policy generation, rollout, or tracking mechanisms. The most agile use billing and collection data for analytics and risk profiling.
7. **Premium Reminders/Renewals.** How sophisticated and efficient insurers are in processing premium reminders/renewals. Only the most agile use automated and integrated systems.
8. **Compliance.** How quickly insurers can make the required regulatory-driven changes, and comply with any new regulations across the PA function. The least agile undertake ad-hoc analysis of regulatory directives for compliance, and manually extract regulatory reports and compliance needs. The most mature integrate compliance with enterprise-level analytics systems to ensure enterprise-level compliance even with systemic frameworks such as Solvency II.

Figure 2.2 Five Levels of Maturity in Business Agility for Each Lever in the 'Policy Administration and Underwriting' Function

AGILITY LEVERS	LEVELS OF MATURITY				
	Level 1	Level 2	Level 3	Level 4	Level 5
Product Set-up	Manual set-up of new products / enhancements	Automated set-up for new products / enhancements for simple to medium complexity products	Automated set-up for new products / enhancements for complex products with business rules / process automation	Reuse of templates and editable forms for design and rollout of products / enhancements	Integration with enterprise-level analytics, documents, and content management system
Underwriting and Risk Analysis	Semi-automated processing of all submissions	Automated underwriting of all simple to medium complexity submissions	Automated underwriting of all submissions, including high-complexity submissions, with exception processing	Leveraging analytics for underwriting decisions	Leveraging advanced analytics, like predictive models, for underwriting decisions
Rate and Quote	Semi-automated rate and quote for simple to complex risks	Automated rate and quote for major lines of business	Access to rate and quote capability for external entities, like channels / partners	On-line rate modifications and changes	Leveraging advanced analytics, including predictive models, for rating
Confirmation of Coverage and Policy Issuance	Manual processing and issuance of confirmation of coverage and policy / contract documents	Automated processing and issuance of confirmation of coverage and policy / contract documents	Issuance of confirmation of coverage and policy / contract documents in electronic format, including e-mail and web	Outsourcing the confirmation of coverage and policy / contract issuance function	Integration with external entities to support self-service needs of customers / channels / partners
Policy / Contract Maintenance	Manual processing of policy / contract servicing request	Automated processing of non-financial policy / contract servicing request	Automated processing of simple to medium complexity financial servicing requests	Outsourcing of policy / contract servicing and maintenance function	Integration with external entities to support self-service needs of customers / channels / partners
Billing and Premium Invoicing	Traditional billing with snail mail capability, not integrated with policy generation and rollout; and without tracking mechanism	Automated billing with limited payment options. Billing and collections integrated with policy generation and maintenance	Flexible billing with multiple payment options, integrated with email and Internet	Account-level billing and tracking, channel-focused billing to support co-branding and custom-made insurance product	Use of billing and collection data for analytics and risk profiling
Premium Reminders / Renewals	Manual processing of premium reminders / renewals	Automated renewal notice / premium reminder processing	Automated generation of renewal notice / premium reminders with request for pending information	Automatic renewals / premium collections with usage of policy history data and support for co-branding and custom-made insurance products	Integration with external and internal systems, as well as enterprise analytics platform
Compliance	Ad-hoc analysis of regulatory directives for compliance, manual extract of regulatory reports and compliance needs	Dedicated compliance team for analysis, implementation, and tracking of compliance	Enterprise-level compliance team that governs the compliance norms across all functions, including policy administration	Robust archiving and retrieval mechanism for policy / contract / endorsement records, with audit trail	Integration with enterprise-level analytics system for enterprise-level compliance requirements, such as Solvency II

Note: Each level of maturity is incremental in improvement over the preceding one
Source: Capgemini analysis, 2011

PROACTIVE INVESTMENT HAS IMPROVED AGILITY IN CORE BACK-OFFICE PA LEVERS

Many insurers have been proactive in upgrading core back-office levers of PA systems, and the analysis shows these investments are paying off in terms of agility. This is especially the case in the areas of Confirmation of Coverage and Policy Issuance, Policy/Contract Maintenance, Billing and Premium Invoicing, and Premium Reminders and Renewals (see Figure 2.3).

However, insurers' agility in other PA levers is likely to increase in the near-to-medium term, as insurers keep investing in PA transformation initiatives to capture potential gains in process effectiveness and cost efficiency. For example, more insurers are developing automated rate and quote capabilities, and intend to offer online rate-modification capabilities to traditional as well as non-traditional channels. As a result, their maturity level on the Rate and Quote lever should improve in the near-term. And with the increasing trend toward leveraging advanced analytics to support underwriting processes, insurers are also likely to move up the maturity scale on the Underwriting and Risk Analysis lever.

This type of progress is not equally evident across all types of firms, however. Maturity levels heavily depend, on aggregate, on the size of the firm in terms of premiums written. For instance, large insurers displayed relatively higher maturity on most agility levers, driven largely by their ability to invest more heavily in advanced IT systems and analytics platforms. Larger firms were also far more mature on levers that are usually centralized and core to business, such as Underwriting and Risk Analysis, Billing and Premium Invoicing, and Premium Reminders/Renewals.

Medium and small firms, by contrast, displayed relatively higher maturity on customer touch-point levers, such as Rate and Quote, Confirmation of Coverage and Policy Issuance and Policy/Contract Maintenance, which all have a direct impact on customer service levels.

Non-life firms displayed higher maturity levels as compared to life firms on most levers, in particular the Underwriting and Risk Analysis, Rate and Quote, and Premium Reminder/Renewal levers. In fact, more than 47% of surveyed non-life insurance firms said they leveraged analytics for Underwriting and Risk Analysis and Rate and Quote, compared with just 27% of life insurers. Also, 23% of non-life firms used advanced analytics vs. 11% of life firms. Most large and medium-sized non-life firms have PA systems that are integrated in real-time with external and internal systems, as well as with analytics platforms. This contributed to non-life firms displaying higher agility than life insurers on Confirmation of Coverage and Policy Issuance, and Premium Reminder/Renewal parameters.

Life firms were generally more agile, however, in providing services around Policy/Contract Maintenance and Billing and Premium invoicing levers. Since life insurance policies are much longer-term contracts than non-life policies (which usually expire in a year), life firms are generally more focused on improving their agility around policy maintenance and premium invoicing levers.

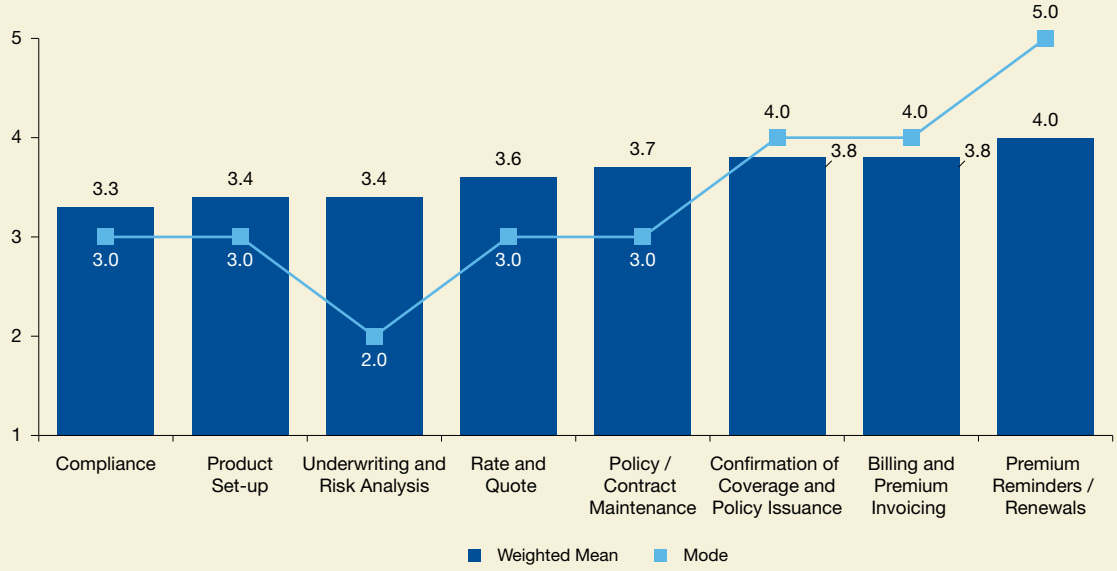
U.S. and European insurance firms displayed very similar agility levels on most parameters, reflecting their comparable approaches to, adoption of, and expenditure on, advanced technology. European insurers displayed higher maturity levels on the Compliance category amid their drive to meet new Solvency II norms. U.S. firms were relatively more agile on Underwriting and Risk Analysis, and Billing and Premium accounting levers, reflecting their widespread use of analytics, including predictive modeling, to support underwriting decisions, and the extensive use of billing and collection data for business intelligence. Insurers in many Asia-Pacific and Latin American insurance markets were generally less mature on most of these parameters, which is consistent with the still-emerging state of those markets.

SURVEY SHOWS AGILITY IN DIFFERENT PA SUB-LEVERS VARIED BY BUSINESS LINE, REGION, AND SIZE

Product Set-Up

Non-life insurers were more likely to have achieved higher agility levels in Product Set-up, mostly because their products are less complex than life products, such as annuities, universal life, and unit-linked products. In fact, one in four non-life firms surveyed is already integrating PA systems with other enterprise-level systems (that is, they have achieved the highest level of maturity in terms of agility on Product Set-up parameters, see Figure 2.4).

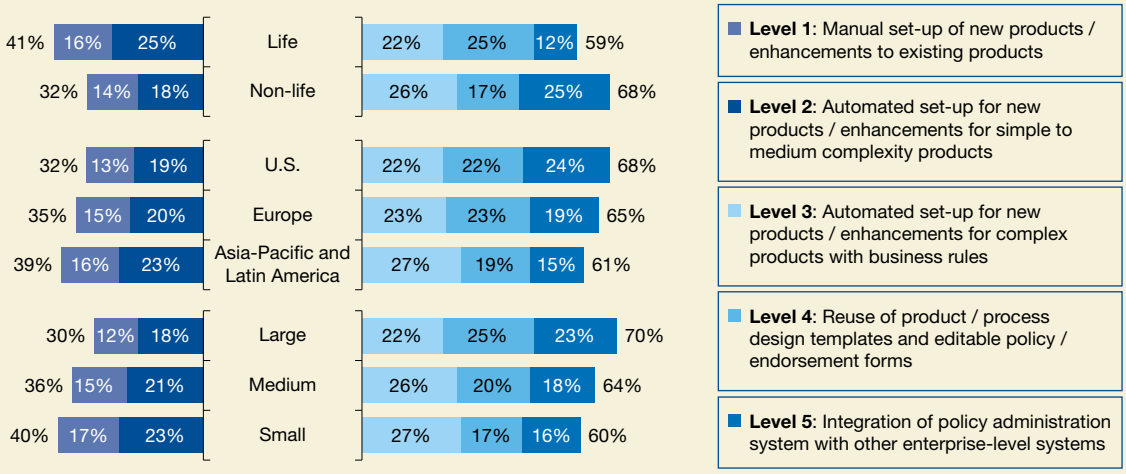
Figure 2.3 Relative Maturity of Insurers on Levers of Policy Administration and Underwriting, 2011



Note: Weighted Mean of any given lever reflects the weighted average score of all firms interviewed, based on the premiums of each firm and country. The Mode is the maturity level of the majority of insurers interviewed.

Source: Capgemini analysis, 2011; Executive interviews conducted for World Insurance Report 2012

Figure 2.4 Breakdown of Insurers' Business Agility Maturity Levels for Product Set-up, 2011



Note: Each level of maturity is incremental in improvement over the preceding one
Source: Capgemini analysis, 2011; Executive interviews conducted for World Insurance Report 2012

Many life insurers are also making significant progress, though, with more than 35% already at least at Level 4, reusing product/process design templates and editable policy/endorsement forms to enhance efficiency and effectiveness. Further progress is likely among life insurers, which continue to invest in improving their PA systems, but the investment component of life products, especially annuities, market-linked, and endowment products, is most in need of improved integration (especially with asset management systems) to enable greater agility.

As more insurers move to higher maturity levels on the Product Set-up lever, their speed to market for products is likely to improve, as they make products available to marketing/sales teams more quickly.

Underwriting and Risk Analysis

Overall, 83% of insurers have at least adopted automated tools for simple-to-medium complexity submissions in the underwriting process (i.e., they are at Level 2 on the maturity scale). However, just 17% is at Level 5, leveraging advanced analytics, such as predictive models, to support the underwriting process/decisions.

Non-life insurers appear to be more mature on this lever (23% are already at Level 5 and 24% at Level 4, see Figure 2.5). One leading U.S. non-life insurer, for example, uses automated underwriting tools that help with workflow management, and rules engines and underwriting workbenches to process even highly complex submissions. This insurer is also leveraging advanced analytics tools, including predictive modeling, to support the underwriting process/ decisions for personal auto as well as commercial lines.

It is relatively difficult, by contrast, to automate the underwriting of life insurance, because it often requires substantial external data, for instance from the medical clinics and pathology labs that do policy screening tests. Analysis of complex medical and financial information typically requires manual evaluation.

Many U.S. insurers surveyed are already quite mature in terms of Underwriting and Risk Analysis, with 25% leveraging at least standard analytics to support underwriting decisions (Level 4) and another 25% using advanced analytics, such as predictive models (Level 5). The maturity of European insurers is not far behind, and this progress reflects the significant investments in advanced technology, and greater use of analytics in these markets. By contrast, analytics are used by fewer insurers in the emerging markets of Asia-Pacific and Latin America, but are more common among the subsidiaries of large multinational insurers, which seek to leverage their best practices globally.

As insurers generally move to ever higher levels of agility in Underwriting and Risk Analysis, the chance of adverse risk selection is likely to decline, as underwriters will be able to spend more quality time and focus more on their core job of risk assessment.

Rate and Quote

The majority of insurers (75% of non-life firms and 58% of life firms) have automated their Rate and Quote functionality for most lines of business (that is reached at least a Level 3 on the maturity scale, see Figure 2.6). As such, these insurers have externalized their Rate and Quote capabilities for traditional distribution channels and customers, typically through business process management (BPM) or business process re-engineering (BRE), and many have done so to non-traditional channels as well.

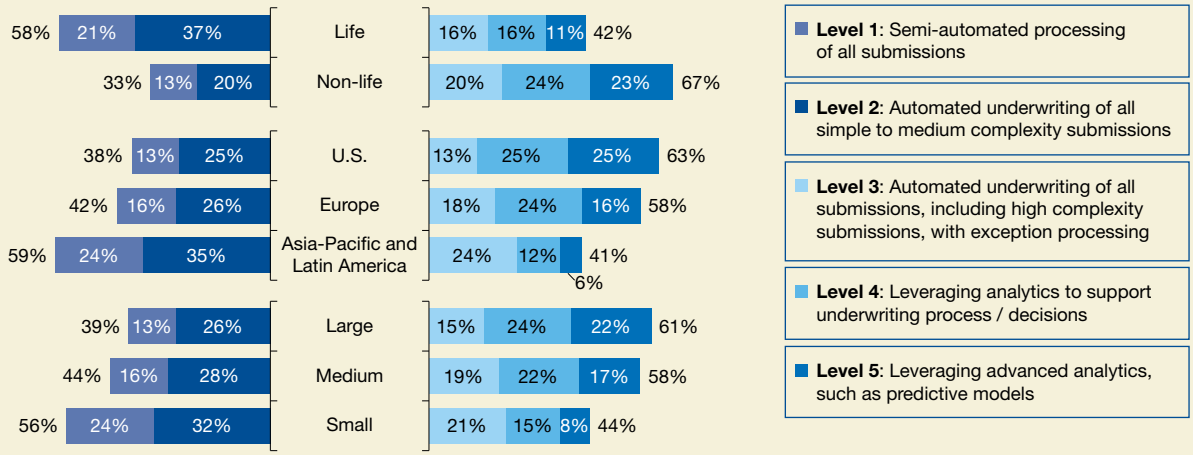
These capabilities are especially evident in the personal lines of non-life business, where policies are less complex than the tailored products in some lines such as commercial insurance. Nevertheless, life insurers also appear among the most mature on these parameters, amid the increasing drive by all firms to offer a range of self-service capabilities.

Only 18% of all surveyed insurers (but 23% of non-life insurers) have reached the highest level of maturity, leveraging advanced analytics, including predictive modeling, to enhance their Rate and Quote capabilities. For one major insurance company in Italy, this has meant: extending automated rate and quote capabilities to all external entities, including banks, points of sale, and other channels and partners; allowing online rate modifications and changes for simple-to-medium complexity risks; and, for car insurance, using an advanced analytics tool based on multivariate prediction to facilitate risk-profile evaluations.

Again, U.S. and Western European firms are most agile, while Asia-Pacific and Latin America insurers are more likely to depend on conventional rating approaches.

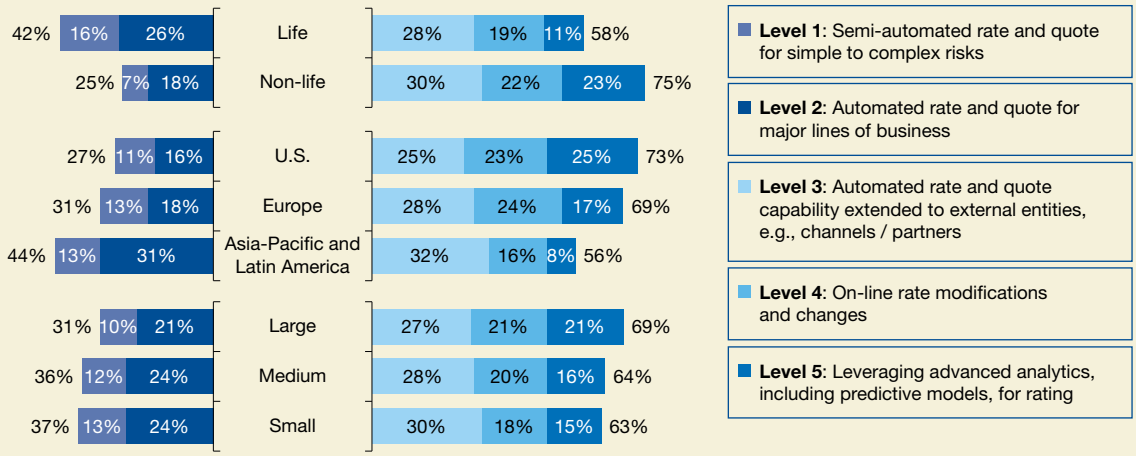
Higher levels of agility in this lever enhance the ability of insurers to provide accurate real-time rates and quotes to their customers, and the need for online quotes and rate modifications will only grow as more customers embrace the online channel. As a result, more insurers are likely to invest in this area in the near-to-medium term.

Figure 2.5 Breakdown of Insurers' Business Agility Maturity Levels for Underwriting and Risk Analysis, 2011



Note: Each level of maturity is incremental in improvement over the preceding one
Source: Capgemini analysis, 2011; Executive interviews conducted for World Insurance Report 2012

Figure 2.6 Breakdown of Insurers' Business Agility Maturity Levels for Rate and Quote, 2011



Note: Each level of maturity is incremental in improvement over the preceding one
Source: Capgemini analysis, 2011; Executive interviews conducted for World Insurance Report 2012

Confirmation of Coverage and Policy Issuance

Nearly two-thirds of all insurers have reached at least a Level 3 on the maturity scale for Confirmation of Coverage and Policy Issuance, and are using electronic formats, including e-mail and the web, to distribute binders and other contract documents. That number is higher among non-life insurers (78%) than among life insurers (68%), largely because non-life insurers, especially personal lines insurers, typically have more commoditized policies, and face significant demand for self-service capabilities from their agents and customers.

As insurers grow more mature in this area, they will likely be able to better meet increasing demand for self-service capabilities and potentially gain cost efficiencies. Some insurers have captured these benefits by outsourcing these activities (characteristic of Level 4 maturity). Life firms are even more likely than non-life firms to externalize these activities (see Figure 2.7), because it is especially difficult for them to achieve the requisite agility in-house, given the broad range of external entities involved in the process, and the complexity of policy documentation. Indeed, the majority of life insurers that have outsourced these activities report doing so to reduce costs and improve customer service.

Still, more non-life firms (26%) than life firms (16%) have reached the highest level of maturity, because the demand from customers and agents for self-service capabilities is greater in non-life, where policies tend to be more commoditized.

One of the largest insurers in France, which offers both life and non-life products, issues policy/contract documents in electronic formats and via the web for mass-market clients that request them, and it has outsourced the Confirmation of Coverage and Policy Issuance function for some of its run-off portfolios. Moreover, the insurer's PA system is integrated with external entities to support the self-service needs of customers and channel partners, primarily for non-life and health lines of business, though self-service support has also been extended to those with unit-linked contracts.

Large insurers are most likely to be at the highest level of maturity, with many aggressively leveraging straight-through processing (STP) and mobile solutions to stay abreast of the competition in meeting the increasing demand for self-service options. These capabilities are also being hotly pursued, however, by many medium-sized firms.

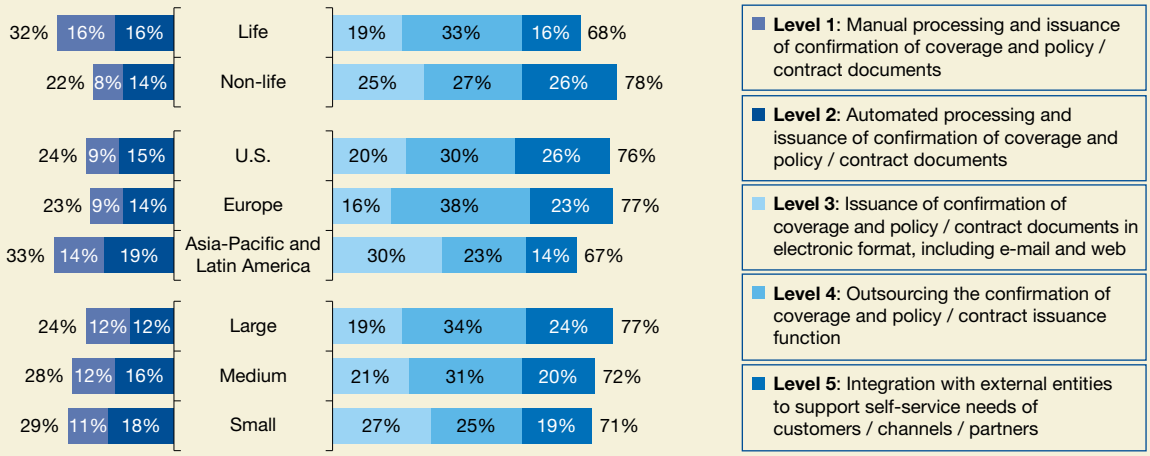
Policy/Contract Maintenance

The vast majority of insurers (79% of life insurers and 65% of non-life firms) have automated processing capabilities for all financial and non-financial policy/contract changes (that is, reached at least a Level 3 on the maturity scale, see Figure 2.8). These capabilities are especially evident among life insurers, because financial change requests, including fund switches, fund withdrawals, riders, and so on, are integral to life coverage, and thus already supported through online self-service modules by most life insurers. By contrast, 35% of non-life insurers still need to process financial change requests manually, even though some have automated non-financial change requests. Moreover since life policies are longer-term contracts than non-life policies, life firms seek to be more agile on the policy maintenance function in order to support long-term customer relationships.

Insurers with higher levels of agility on this function tend to be swifter in processing policy change requests, resulting in superior customer service and better retention levels. Outsourcing (Level 4 on the maturity scale) is a viable option for improving agility on this lever.

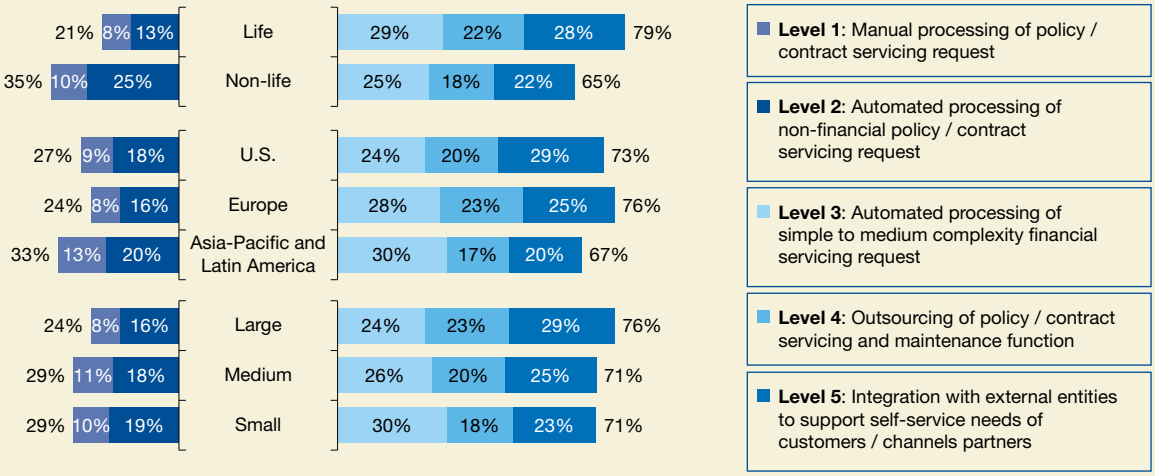
Of all insurers, 25% have reached the highest level of maturity, where they integrate services with external entities to support the self-service needs of customers and channel partners. For one leading Spanish insurer, this has meant providing policy/contract maintenance services for various product lines through multiple channels by integrating with third-party systems to improve the customer experience. For example, the company has developed web services to integrate brokers' systems, and created standard files to enable the interchange of information between entities. The insurer has also created an interface to integrate information (including premiums earned) on the various products and policies held by a single client.

Figure 2.7 Breakdown of Insurers' Business Agility Maturity Levels for Confirmation of Coverage and Policy Issuance, 2011



Note: Each level of maturity is incremental in improvement over the preceding one
Source: Capgemini analysis, 2011; Executive interviews conducted for World Insurance Report 2012

Figure 2.8 Breakdown of Insurers' Business Agility Maturity Levels for Policy / Contract Maintenance, 2011



Note: Each level of maturity is incremental in improvement over the preceding one
Source: Capgemini analysis, 2011; Executive interviews conducted for World Insurance Report 2012

Billing and Premium Invoicing

Nearly 80% of insurers are offering flexible billing with multiple payment options to customers, integrated with email and Internet options (i.e., they are at least at Level 3 on the maturity scale, see Figure 2.9). Flexibility and convenience in payment options are key to customer satisfaction, so insurers are offering more online, self-service transactions, and multiple payment options, especially in individual and personal lines of business. The use of payment gateways and electronic fund transfers has also become the norm.

About one in four firms surveyed offer account-level billing and tracking, and channel-focused billing to support co-branding and customization of insurance products (i.e., are at least at Level 4). This provides critical support for corporate and affluent clients, and high-performing channels, and facilitates the much sought-after single view of the customer to the insurer. Co-branding of products such as credit 'shields' with term life, and disability with auto coverage, is evident in many geographies, and bancassurance channels offer one of the most effective means for co-branding.

Another 23% of firms overall are using billing and collection data for analytics and risk profiling (they are at Level 5), but large and medium-sized firms are far more likely than smaller firms to do so. Non-life insurers mostly use billing and collection data to leverage advanced analytics for personal and commercial lines for risk profiling, while life insurers use such data to calculate key metrics, such as customer lifetime value (LTV) and share of wallet. Some, like one leading insurance company in Brazil, also leverage these capabilities to build business intelligence, and identify cross-sell/up-sell initiatives.

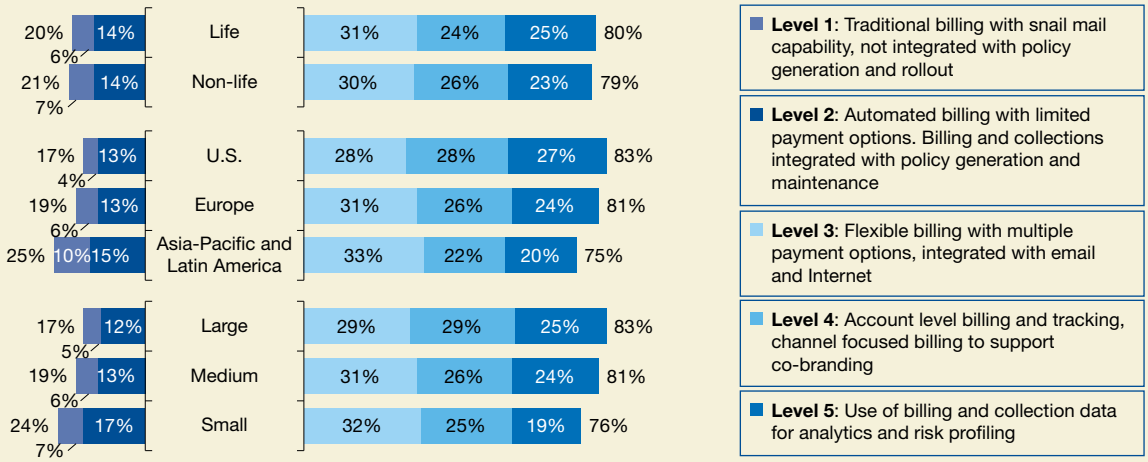
Premium Reminders/Renewals

Both life and non-life insurers continue to improve their Premium Reminders/Renewal processes, amid ongoing demand among customers for automation. Already, 57% of non-life and life insurers surveyed have at least automated policy reminders and renewals with the use of historical data, and in a way that can support co-branding (i.e., achieved Level 4, see Figure 2.10). For example, some non-life insurers offer automatic renewals for policyholders shown by their claims history to be good risks.

Separately, 30% of all surveyed insurers already integrate policy reminder and renewal activities with external and other internal systems, including enterprise analytics platforms (Level 5). Some life insurers, for instance, are also leveraging automated premium reminders as an opportunity to cross-sell other products to certain customers, based on the lifetime value of their business.

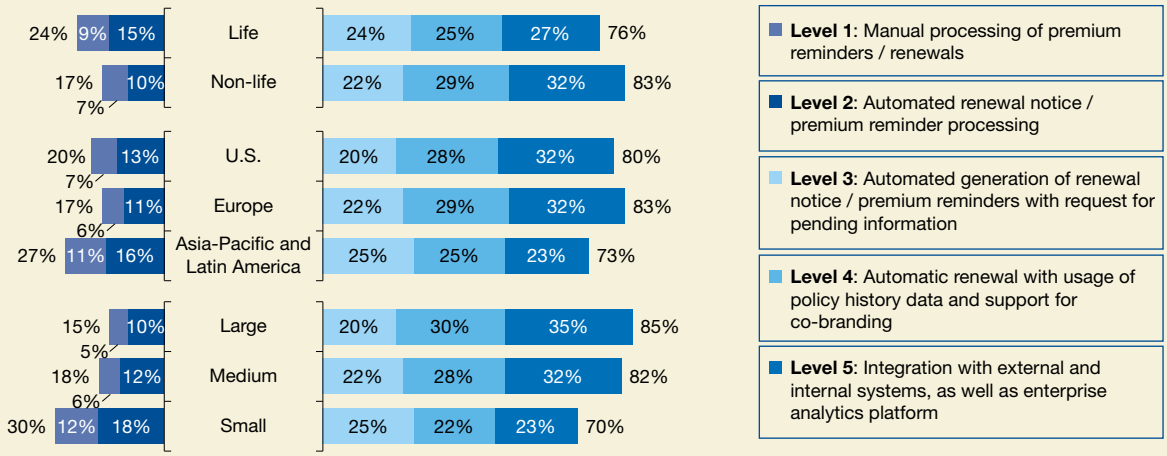
These capabilities can all help to boost customer satisfaction and retention, which is critical for driving growth in the currently depressed economic environment, especially as tech-savvy customers increasingly expect less manual handling of policy processes.

Figure 2.9 Breakdown of Insurers' Business Agility Maturity Levels for Billing and Premium Invoicing, 2011



Note: Each level of maturity is incremental in improvement over the preceding one
Source: Capgemini analysis, 2011; Executive interviews conducted for World Insurance Report 2012

Figure 2.10 Breakdown of Insurers' Business Agility Maturity Levels for Premium Reminders / Renewals, 2011



Note: Each level of maturity is incremental in improvement over the preceding one
Source: Capgemini analysis, 2011; Executive interviews conducted for World Insurance Report 2012

CASE STUDY

Leading Non-Life Insurer Uses Advanced Analytics to Drive Agility in Rate and Quote and Premium Reminders/Renewals

Genertel, the direct-insurance unit of Italy's Generali Group, wrote about €300m in gross premiums in 2010, mainly through direct channels (web, contact center), but also via commercial partnerships. Nearly 90% of its GWPs came from auto insurance (much of it mandatory coverage) in 2010. The capacity to attract customers who are good risks is a critical success factor for profitability in Italy's mature market, where claims ratios are high, but insurers cannot easily raise premiums as customers are very price-sensitive.

To bolster its position, Genertel wanted to reward good drivers, and promote responsible driving behaviors. The challenge was how to strengthen its reputation as an advocate and promoter of responsible drivers, and improve the market image of mandatory coverage (perceived by end-customers to be more of a tax than a service).

The insurer decided it first needed to improve its Rate-and-Quote agility so as to adapt pricing to changes in customer behavior, and to the competitive context. It leveraged advanced analytics (using constantly updating information on claims, risks, competitive pricing per segment, etc.) to generate special offers and commercial discounts automatically for its high-value customers. This improved the speed and flexibility of offerings for potentially more-profitable customers, and optimized the distribution of discounts.

The insurer then introduced the Genertel Quality Driver® program to facilitate Premium Reminders/Renewals for responsible drivers. The program hinged on data on three key metrics of driving behavior collected from a GPS-based "black box" installed (free of charge) in the customer's car:

1) "**Caution level**," based on the distance driven within speed limits;

2) "**Risk level**," based on the types of roads driven at different times;

3) "**Attention level**," based on the frequency and intensity of acceleration and braking.

Using the data, an algorithm automatically calculates and updates an individualized "Quality Level" for the driver, and customers can access their score through a personal web/Smartphone portal. At the end of their annual contract, a customer that has not caused any claims accumulates "security-credits" that translate into a commercial discount for the renewal (up to 25% of the previous year's annual premium). The discount is calculated automatically by the IT platform, and is proposed to the customer as a reward.

The "Quality Driver Pack," which also includes additional GPS-based services (e.g., 24/7 assistance, location-finding capabilities in case there is a crash or theft), has helped to attract and retain good customers, and bolster the firm's reputation as an innovative and discerning provider.

Compliance

The increasing levels of regulatory oversight worldwide have clearly prompted many insurers to pursue, adopt, and implement robust compliance mechanisms able to deal with regulatory changes that affect the PA function either directly or indirectly. About two-thirds of life and non-life firms already have enterprise-wide governance of compliance (reaching at least a Level 3 on the maturity scale), but large insurers with a multinational presence are most likely to have achieved the highest levels of maturity (see Figure 2.11).

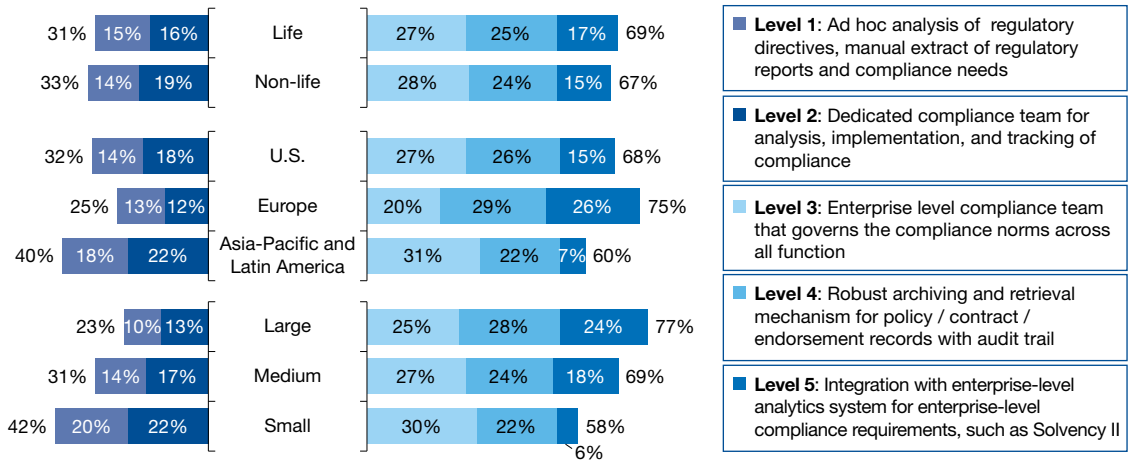
European insurers, especially larger ones, are the most likely to be integrating enterprise analytics into enterprise compliance (Level 5), as they have had to manage their response to the EU's Solvency II Directive. Nevertheless, other geographies are faced with a host of country, state, and local regulations, so compliance is in sharp focus across the globe. This trend provides ample scope for global sharing of best practices.

The most agile insurers on compliance report that there is a strong drive from their headquarters to provide regular training and 'blind tests' on compliance, and ensure management is well aware of new regulations, especially in the life sector, where regulation tends to be more complex. In many cases, there is a Central Compliance Officer, who outlines the strategy, and is responsible for overall reporting. A Decentralized Compliance Office may be responsible for business-line compliance.

CONCLUSION

Our research shows insurers are already reaping cost and efficiency benefits from prior investments in core PA activities. Now, insurers will need to decide for themselves the extent to which they must pursue ever higher levels of agility in different PA sub-functions. In general, more agile performers are more efficient and effective, but the cost of improvement programs needs to be weighed against the benefits. The net impact will depend greatly on insurers' strategic priorities, their current and desired market and competitive positioning, the needs and demands of customers, agents, brokers, and other channel partners in their business lines and markets, and the current and potential state of the operating budget.

Figure 2.11 Breakdown of Insurers' Business Agility Maturity Levels for Compliance, 2011



Note: Each level of maturity is incremental in improvement over the preceding one
Source: Capgemini analysis, 2011; Executive interviews conducted for World Insurance Report 2012

Policy Administration Is the Next Priority for Transformation while Driving Results

CHAPTER 3

INTRODUCTION

Gross written premiums (GWPs) are starting to recover from the declines at the height of the financial crisis, but growth is still weak overall, especially in industrialized markets. To protect and grow profits in this environment, insurers are focusing on capturing efficiencies through transformation initiatives. Policy administration (PA) is gaining attention as the next transformation priority.

More specifically, insurers are looking at ways to transform IT-enabled PA, which underlies the end-to-end management of insurance policies, from product set-up, underwriting and risk analysis, and rate and quote decisions to confirmation of coverage and policy issuance, and ongoing contract maintenance, billing and premium invoicing, and premium reminders/renewals. Compliance is also a key aspect of PA in which IT can be effective, as existing policies must be properly managed and amended to meet the latest regulatory standards.

In fact, IT-enabled PA can facilitate many interactions directly between insurers and their customers, agents, brokers, and other third parties throughout the lifetime of these relationships. As a result, while PA transformation affects the bottom line most directly, it can also have a positive impact on the top line, because of the potential to improve satisfaction levels among customers and other intermediaries.

Moreover, PA transformation can help insurers to manage many of today's big market and business challenges, including high costs, protracted product launches, regulatory-compliance issues, and aging and inflexible IT systems.

The following are some examples of the key market developments driving the need for PA transformation today:

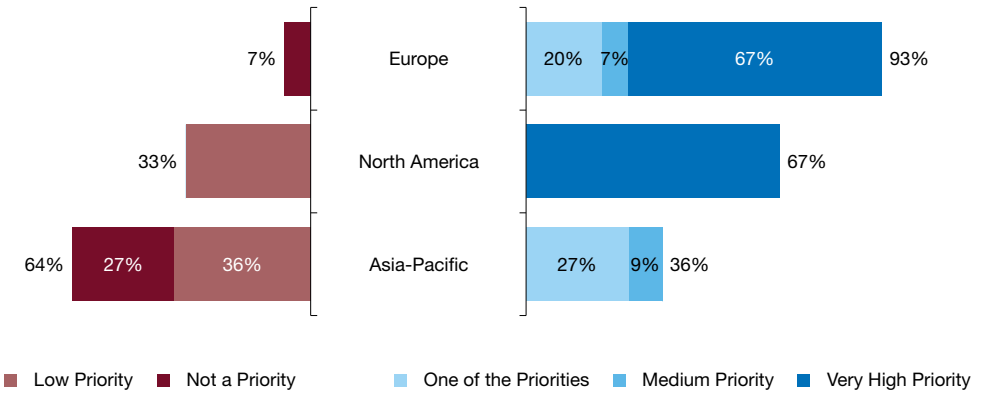
- **Escalating costs.** Many insurers are using up considerable resources (both time and money) to maintain costly legacy PA systems. To remain cost-efficient and lean, insurers will need to transform PA technology and processes. Global IT spending on PA by insurers is estimated at $16.8 billion in 2011, and is likely to show sustained growth of 4.9% a year for 2007-13.[9]
- **Speed-to-market and increased competitive pressure.** Increased competition and changing customer preferences (especially among tech-savvy Gen X and Y customers) are forcing insurers to be more agile, and improve their time-to-market for new/innovative products, but legacy PA systems may lack the flexibility required. One executive at a North American regional insurer said a new PA system was planned that could cut the IT time on developing, deploying, and managing a new product from 9 months to just 1-2 months.
- **Increased regulatory activity.** In the aftermath of the financial crisis, the insurance industry continues to experience waves of regulatory reform, and regulators are demanding that insurers achieve 100% compliance. Emerging regulatory paradigms also present a business challenge to insurers, which must evaluate complex effects, such as the net impact of higher capital standards demanded by the EU's Solvency II Directive. Insurers must also make sure compliance systems are themselves delivering value. Legacy PA systems may not be flexible enough to support a quick and effective response in this kind of regulatory environment.
- **Leveraging technology to enable anytime/anywhere customer service demands.** Front-end technology advances, such as real-time information access, are becoming standard in the insurance industry, and customers increasingly expect their service interactions to be anytime (24x7) and anywhere (voice, online, mobile). For insurers to respond effectively, they have to align legacy PA systems with the increasingly advancing technology around it. They also need a single view of the customer across channels and interactions, and data must be synchronized between front- and back-office systems.

As these and other factors make PA transformation more urgent, insurers will need to identify an appropriate transformation approach, one that thoroughly considers the risks and opportunities, and is consistent with overall business strategy.

In particular, insurers must first decide at a business level which parts of the business to retain, sell, or transfer (such that the insurer still owns the business, but end-to-end administration is transferred to a third-party administrator (TPA) or a business process outsourcer (BPO)). After that decision is taken, insurers need to proceed to transform the retained blocks of business (on their current systems) through business process re-engineering, consolidation, modernization, and sourcing strategies.

In formulating the PA transformation initiative, insurers will need to determine which of these strategies is most likely to deliver an optimal cost per policy, and insurers will need to ascertain that target cost by conducting an in-depth cost analysis of market standards, and their own PA functions.

Figure 3.1 Priority Global Insurers Place on Policy Administration Transformation, 2011



Note: Question asked: "If you have not initiated policy administration transformation in the last five years, how high of a priority is it for your company in the next two years?". Percentages may not add up due to rounding.

Source: Capgemini analysis, 2011; Executive interviews conducted for World Insurance Report 2012

[9] Capgemini analysis, 2011; Insurance Technology Spending Forecast Through 2013-Business Function Segmentation, Datamonitor

POLICY ADMINISTRATION TRANSFORMATION IS A HIGH PRIORITY FOR MANY INSURERS

Among surveyed insurers in Europe, 93% of those not already committed to PA transformation said it would be a priority for them in the next two years (see Figure 3.1). Among insurers in North America, 67% said it would be a priority, and those respondents all said it was a very high priority.

The imperative is stronger in Europe and North America than in Asia-Pacific (where only 36% of respondents indicated PA transformation to be a top priority), because those markets are more developed, and are more likely to feature proprietary, legacy systems that have often become costly and difficult to maintain. Significant merger and acquisition activity has also taken place in those markets, leaving many insurers with multiple or duplicate systems across and among different businesses. By contrast, many Asia-Pacific insurance markets are relatively young, and have only been opened to private players in the last decade or so. Their systems are also more likely to be modern and flexible.

Globally, many leading insurers acknowledge they cannot continue to rely on aging and inflexible PA systems, which lock them into legacy business practices, and inhibit their ability to compete in a customer-centric market. In fact, our field experience of PA transformation shows strategic value can be generated for insurers in four distinct ways, by achieving the following:

- **Operational and service excellence**, potentially improving business process and technological efficiency by up to 30%, eliminating redundancies across PA functions, and outsourcing closed and open-book operations.
- **Cost leadership**, lowering the total cost of ownership (TCO) by up to 40%, and the cost per policy by up to 30%.
- **Product leadership**, by improving time to market by up to 60%, tailoring customized products aligned with customer preferences and competitive dynamics, and utilizing more accurate analytics-driven pricing.
- **Top-line support**, by enhancing customer experience directly, and improving the satisfaction and capabilities of intermediaries, which leads to improved customer acquisition and retention rates.

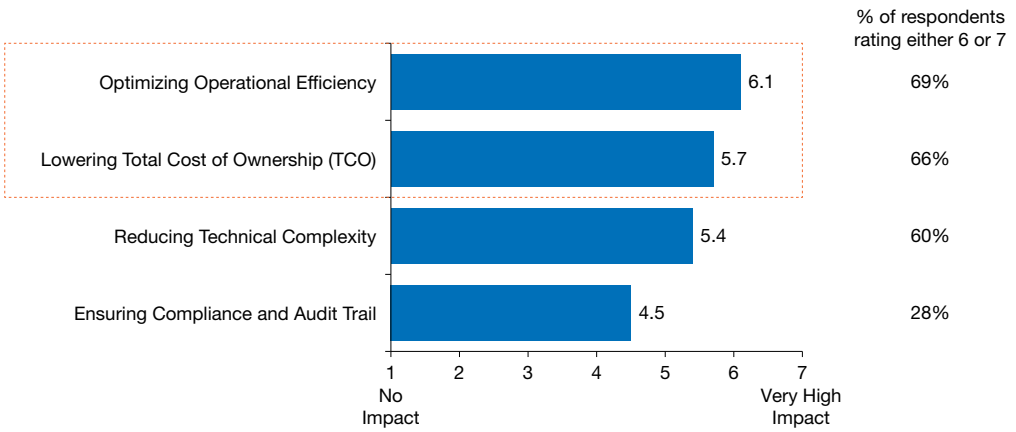
Ultimately, insurers that can differentiate themselves through efficient and innovative PA practices should be much better positioned in an intensely competitive market to maintain (or improve) market share and profitability.

PA TRANSFORMATION POTENTIALLY OFFERS BENEFITS TO THE TOP AND BOTTOM LINES

In short, the strategic benefits of PA transformation derive from both direct bottom-line and indirect top-line opportunities.

In regards to the bottom line, 69% of surveyed insurers (see Figure 3.2) said the ability to optimize operational efficiency was important in driving decisions to transform PA systems, and 66% said lowering the TCO was important. Industry examples show PA enhancements can improve and/or streamline activities broadly (e.g., across systems) and specifically within products. For example, one of the largest life insurers in North America needed a PA system that could support its newly introduced whole-life product. The product was a complex one, designed to meet a specific market need, and fill a gap in the insurer's offering, but it required complex calculations to support flex-term and client-attractive riders. The insurer implemented a

Figure 3.2 Level of Impact Different Factors Have in Driving the Decision to Transform Policy Administration Systems, 2011



Note: Question asked: "Please rate the importance the following factors have in driving the decision to transform policy administration systems." (Rate the importance of each area on a scale of 1 to 7, with 1 being 'Not Important' and 7 being 'Very Important')

Source: Capgemini analysis, 2011; Executive interviews conducted for World Insurance Report 2012

strategic PA platform that could support the product, and generally reduce the cost and time-to-market of new-product offerings. In particular, the new PA system was able to handle both upstream and downstream interfaces in an ACORD-compliant format to smooth and speed product distribution.

Another multi-national life insurance company operating in eight countries within Asia embarked on a strategic initiative that involved converging 11 legacy systems across six different countries into one regional core PA system. The insurer expects this effort to reduce costs, streamline operations and IT support, and improve customer-centricity.

In regards to the top line, surveyed insurers report that PA administration has a very significant impact on existing interactions with both intermediaries and customers (see Figure 3.3). As a result, insurers can expect PA transformation to bolster customer acquisition and retention rates by delivering, for example:

- Flexibility for customers wishing to update account details, both non-financial (change of address, etc.) and financial (coverage amounts, payment cycles, etc.).
- Continuous policy status updates via mobile devices or other means preferred by customers.
- Higher-quality contact-center interactions for customers.
- Faster notifications/updates on contract/policy updates.
- More self-service capabilities.

By enhancing intermediary and customer satisfaction, insurers can reasonably expect greater loyalty, which drives recurring revenues, and increases the opportunity for cross- and up-selling. Also, interviewed insurers said that transformed PA systems could improve time to market. One leading U.S. auto insurer, for example, recently implemented a single policy processing system in which rate revisions and product changes could be pushed through more quickly, enabling a faster response to competitive rate changes.

BUSINESS VALUE IS KEY TO DECISIONS ABOUT PA TRANSFORMATION STRATEGIES

To capture the benefits of PA transformation, insurers will still need to make sure their initiatives are clearly aligned with broader business priorities, and take proper account of numerous factors, from business risks and vendor capabilities to regulatory requirements. The first step in defining PA transformation, then, is to examine thoroughly the value of existing books of business, and the net cost/risk of transfer from current PA systems to new systems.

This "As Is" analysis assesses the case for retaining the business entirely vs. retaining the business but transferring the end-to-end policy administration to a third-party administrator (TPA) or business process outsourcer (BPO) vs. selling the business outright. The scenarios will depend on the business value of the portfolio and the net cost/risk of transferring the PA activities.

Figure 3.3 Level of Impact of Policy Administration Function on Different Areas in an Insurance Organization, 2011

Note: Question asked: "What level of impact does the policy administration function have on the following areas of your organization?" (Rate the impact level of each area on a scale of 1 to 7, with 1 being 'No Impact' and 7 being 'Very High Impact'); Non-renewal refers to policies not renewed at expiration (e.g., one-year auto coverage); 'Lapsation' refers to policies (e.g., long-term life coverage) on which premium payments lapse

Source: Capgemini analysis, 2011; Executive interviews conducted for World Insurance Report 2012

Case for using service providers/TPAs: If the net cost/risk of transfer is low, but the business value is high, it makes economic sense to find a new PA vehicle. However, the new approach must not impair the enterprise's ability to control the current administration and leverage the future potential of the underlying business. In this situation, then, a TPA is an ideal choice, but there are numerous key considerations, including:

- The availability of qualified TPAs in local markets.
- The ability of TPAs to provide acceptable service quality, and the ability of insurers to monitor and guarantee standards, for example through service level agreements (SLAs).
- The capability of TPA systems to provide the required levels of service, and integration where necessary, without significant modifications.

Case for using a BPO: If both net cost/risk of transfer and the business value are low, there is likely to be a dividend from transferring the business out of its current system for administration. Key considerations for the use of a BPO include:

- Quality of services.
- Cost of services.
- Financial stability.
- Process adherence.

The clearest benefit of the BPO route is the potential for cost savings. Global sourcing and economies of scale allow BPO providers to administer policies at a far lower cost than insurers with in-house PA. Outsourcing allows insurers to convert to fixed fees based on service levels, and reduce investments in permanent employees and fixed assets. It also allows insurers to focus on their core competencies of sales and marketing, underwriting, and asset management.

There are challenges, however. Insurers may not be keen to depend on a single vendor, which could expose them to potential risks of overpricing, vendor lock-ins, and disruptions based on operational failures. Clearly, a badly managed outsourcing engagement could damage the servicing of existing end-customers, leading to customer attrition and revenue losses.

Insurers can minimize these types of risks if they engage in long-term outsourcing arrangements that involve fundamental business transformation projects, rather than a piecemeal outsourcing of component tasks or processes. Such partnerships can lead to strategic benefits for both insurers and vendors. For example, a transformed and flexible PA system could provide more effective data mining, leading to valuable insights regarding customer behavior, product innovation and increased cross- and up-selling potential for insurers. And vendors can provide more value-based offerings that can leverage their delivery experience, and elevate the arrangement above a basic equation of wage or cost arbitrage.

Case for selling the line of business: If the net cost/risk of transfer is high and the business value is low, there is little compelling reason to retain the business, or even to transfer the administration. In fact, the best move is to sell the line of business outright, and let the new owner determine how to administer the business more efficiently. Key imperatives in deciding whether to sell a business will include:

- Assessing the degree of buy-in among stakeholders in a potential sale (e.g., customers, employees, shareholders).
- Conducting thorough financial due diligence.
- Evaluating all appropriate regulatory hurdles, and the likelihood of gaining requisite approvals.
- Calculating the impact of the sale on enterprise capital levels and the subsequent adherence to Solvency II norms.

Case for retaining the business: If both the net cost/risk of transfer and business value are high, there is little or no reason to transfer the business out of its current administration system. In fact, the business imperative for retaining control over administration is compelling. However, insurers will still need to consider potential ways to transform the administration of the retained business, and there are four core elements to transforming a retained PA function:

- **Business process re-engineering:** Involves analyzing and redesigning workflows and processes to increase transparency and speed up execution, and achieve improvements in critical measures such as cost, service, speed, and quality.
- **Consolidation:** Rationalizing the number of PA systems into a single or a few systems, based on size and business needs.
- **Modernization** of legacy policy systems by investing in flexible systems that enable faster product development and solution changes.
- **Sourcing IT Services:** Sourcing strategies that lower the total cost of application ownership.

BUSINESS PROCESS RE-ENGINEERING, CONSOLIDATION, MODERNIZATION, AND SOURCING ARE CORE ELEMENTS OF IN-HOUSE PA TRANSFORMATION

The overarching objective of **business process re-engineering** is to redesign and standardize PA processes to make the work flow simpler and more efficient, and to achieve improvements in critical measures such as cost, service, speed, and quality. This type of re-engineering delivers maximum efficiency for insurers when combined with product-portfolio rationalization, which is especially viable when lines of business are sold, allowing some processes to be changed or eliminated.

In any case, insurers will want to re-engineer processes so as to complement their target businesses and technical architecture. Multiple back-office systems can be integrated to increase transparency and speed execution. Re-engineering and standardizing business processes prior to consolidation and modernization will limit the amount of customization required, and can considerably reduce integration costs, which typically form the bulk of an insurer's transformation budget.

Consolidation initiatives require a well-defined approach that includes deliberate decisions about whether to build or buy, and which products/implementation partners to use. Insurers must also conduct thorough program planning and readiness assessments, and identify the critical rates/features of migration.

From a technology perspective, legacy conversion leads to a more standardized IT architecture, and a more reliable and scalable technology platform. As a result, consolidation is especially appealing to insurers with multiple systems. Among survey respondents that had already initiated PA transformation, 71% said they started out with five or more systems. Post-transformation, none had that many systems, and 72% had only one or two. Many insurers are targeting a maximum of two systems (one for life and one for non-life) to reduce the complexity and increase the agility of the PA function (see Case Study on page 41).

For those seeking to consolidate their PA systems, the first step is to identify the systems that best cater to the current and future needs of the business, and align with the overall organizational objectives. If business processes can then be standardized before systems are consolidated, it will limit the amount of customization needed for migration, and minimize the amount of training required. Data must also be cleansed prior to migration to minimize costs and errors resulting from the migration.

An iterative approach will also be needed to identify any gaps between what the target system(s) can provide and what legacy system(s) require to be migrated. A dedicated team will need to find solutions to fill each gap.

Insurers must also make sure they verify how quickly insurance policies will be migrated, and what form the policyholders' data will take. If data is not migrated effectively to the consolidated system, discrepancies could arise, leading to a loss of business and/or regulatory penalties.

Also critical is a rigorous analysis of the benefits and costs. Benefits include the potential to lower TCO and costs per policy, increase productivity and sales, and improve service quality. Costs relate to system enhancements, product licensing, additional infrastructure, and policy migration. It is vital, therefore, to create a model that can determine the cost per policy for existing systems, and benchmark that cost against future scenarios.

Systems **modernization** lends itself well to a step-by-step modular transformation. Traditional legacy PA applications are typically characterized by rigid and complex platforms, which lack scalability. They also tend to have functional silos, duplicate functionalities, and limited self-service capabilities. And many have high maintenance and integration costs. Modernized PA applications are more flexible (with more reusability options), are easier to maintain and integrate with third-party systems, and typically feature better self-service capabilities, and faster speed to market.

A stable modern PA platform should leverage technology to overcome the challenges posed by legacy systems, most likely including SOA-enabled product configurations, self-service capabilities, seamless integration with external systems, and scalability. Successful implementation will probably require thorough benchmarking against peers to understand the advantages and challenges, and a complete accounting of the business case. A modular approach can focus on the early roll-out of easy wins to demonstrate success before moving onto more critical and risk-prone components.

CASE STUDY

Leading Life Insurer Consolidates Firm-Wide Capabilities with the Help of IT-Enabled PA

Intesa Sanpaolo Vita, a leading player in the Italian life insurance market, was set up as the "one" Life company of Intesa Sanpaolo Group, incorporating life-insurance sales expertise from the large pool of bancassurance professionals spread across the different entities in its conglomerate group.

The main objective of creating the firm was to leverage the integration of capabilities and competencies from the Group's four firms (Eurizon Vita, Intesa Vita, Sud Polo Vita and Centrovita Assicurazioni) to optimize overall business and operational efficiency.

From the outset, the firm defined a new "Target Operating Model" that incorporated the Group's best practices, and identified core back-end and front-end platforms that would support the defined processes and model.

The different corporate entities have also undertaken a comprehensive assessment aiming to:

- Define process flows and functional requirements for selling and post-selling activities on the new online front-end system, and identify gaps between the existing and target models.
- Identify the target model for the unique PA system, leveraging the consolidation and enhancement of current capabilities.
- Analyze data porting, that is the IT procedures and programs needed to transfer the data from the source systems to the target one. Appropriate test cases were defined and developed.
- Guarantee the business continuity of the companies during the consolidation.
- Support end-users in getting trained on the new system.
- Support the companies during and after the transition.

The project represents a significant opportunity to create new value. Specifically, it should lead to a significant increase in efficiency, with cost synergies arising from the consolidation of the various separate systems and processes. Also, the consolidation effort should enhance commercial effectiveness, help to unify the product offering, and enable the insurer to re-evaluate more effectively the entirety of its product offering and investment policies.

Notably, many insurers associate PA modernization with a wholesale "rip and replace" of the existing IT estate, which is very costly. In fact, there are several less drastic options, depending on the quality of applications, and the degree to which they are unique.

For example:

- Applications with limited and targeted functionality but unique features, such as support-function applications like human resources systems, can be rewritten.
- High-quality, highly unique applications can be renovated using the latest technology, such as custom-built PA systems using an SOA framework.
- High-quality but standard applications, such as customer/agent portals, can be re-used by employing best-of-breed components from various vendors.
- Applications with limited and targeted functionality and standard features, such as certain finance systems, can be replaced with standard packages from product vendors.

Sourcing IT services, such as application management services, can reduce the cost of application ownership by as much as 40%. Notably, surveyed executives appeared quite comfortable with the idea of outsourcing IT services (more so than customer services or support functions). Those IT services could include application maintenance and enhancement, product support, and application help desks. The potential benefits include: faster delivery timelines, and cost savings in development efforts; lower TCO for applications (by as much as 40%); service-level based, fixed-fee, ongoing support services, with the flexibility to address demand fluctuations.

The degree to which business process re-engineering, consolidation, modernization, and sourcing of IT services helps to drive operational and service excellence, cost leadership, product leadership, and top-line growth will ultimately depend on the insurer's focus and investments (see Figure 3.4).

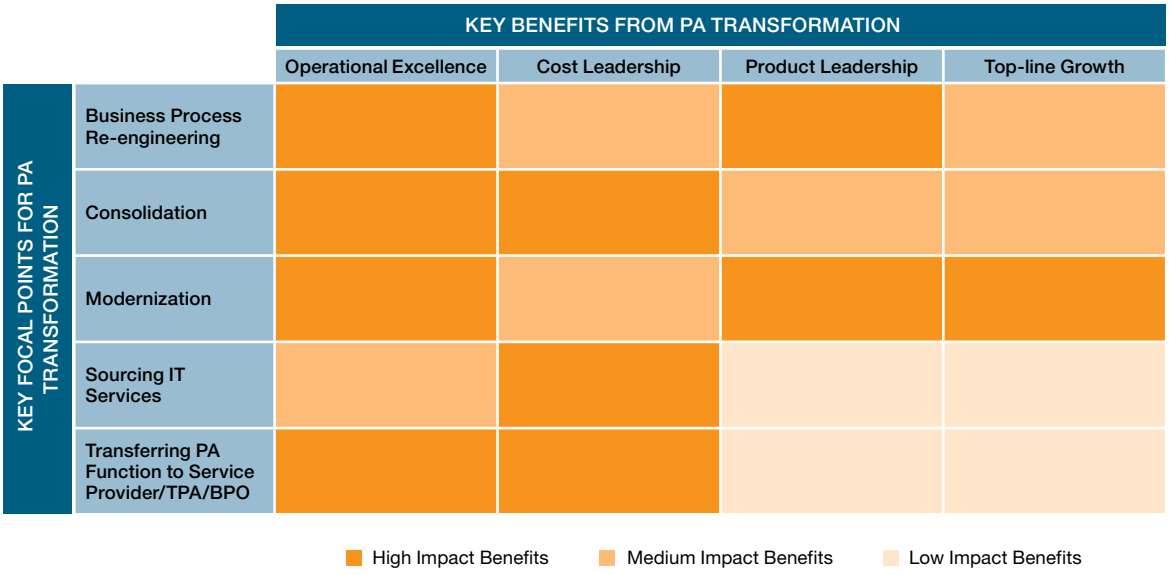
CONCLUSION

PA transformation most directly benefits insurers by creating cost savings and process efficiencies. However, there are also important indirect benefits, such as the enhanced experience for customers and intermediaries, and a greater capacity to meet new compliance demands quickly and effectively.

Today, though, it is the financial gains that offer most promise as insurers around the globe seek to improve margins amid challenging economic conditions.

Particularly in mature markets, it can be difficult to grow the top line when markets are well served, penetration is high, products are increasingly commoditized, and price is invariably the key determinant in buying decisions. In such conditions, PA transformation could prove to be an invaluable tool in delivering much-needed reductions in operational costs, and improvements in operational performance, while the enabling technology also creates a better experience for demanding customers.

Figure 3.4 Heat-Map Reflecting Benefits that can be Derived from each Key Focal Point of PA Transformation



Source: Capgemini analysis, 2011

CASE STUDY

Global Life Assurance Company Converts Policies Cleanly and Promptly in Far-Reaching Data-Migration Effort

A global life assurance company needed to migrate hundreds of thousands of universal life policies in two different markets to newer systems (migrating all to the latest Ingenium systems, some from older versions of legacy systems). Critically, the new PA system also needed to provide broad support for the firm's key business of selling and servicing life insurance, annuity and long-term care products in both the retail and corporate markets.

Ultimately, the data migration entailed a highly granular file-to-file conversion method, which involved:

- Analyzing all source system data fields.
- Mapping all source system fields and values to target-system fields and values.
- Identifying and resolving all data issues related to the conversion (>1000 issues in total).
- Generating conversion routines.
- Performing more than 300 consistency edits, multiple times, to guarantee accuracy in the converted data.
- Optimizing the conversion routines for time and space.

This migration of data in the initial two markets was completed on-time and on-budget, with no post-production clean-up required. The insurer's older systems were subsequently shut down successfully, and the firm is now planning to replicate the migration in other markets.

Methodology

SCOPE AND RESEARCH SOURCES

The *World Insurance Report* (WIR) 2012 covers both non-life (including health) and life segments (with a focus on non-life segments for some sections). This year's report draws on research insights from 19 markets: Australia, Austria, Belgium, Brazil, Canada, Denmark, France, Germany, Hong Kong, India, Italy, Netherlands, Philippines, Singapore, Spain, Switzerland, the U.K., the U.S., and Vietnam. We estimate these countries together account for approximately 66% of the global insurance market, based on data from our own analysis and from the "World Insurance in 2010" Swiss Re Sigma Report. The sample of countries covers 13 of the world's top 20 insurance markets in terms of premiums.

The WIR 2012 is based on a comprehensive body of research that includes in-depth focus interviews with 71 insurance executives. Of the firms interviewed, 41% sell both life and non-life insurance, 31% focus solely on life, and 28% are dedicated to non-life.

EFFICIENCY RATIO ANALYSIS

For each of the thirteen studied countries, we analyzed country-level financials for enough companies to ensure coverage of more than 50% of each market's total non-life premiums. For each of the analyzed companies, we obtained the country-level breakdown of financials (Gross written premiums, Claims, Commission and Expenses, Operational Expenses, Investment Income, Profit before Tax) through extensive secondary research sources, and from local Capgemini insurance subject-matter experts.

Where no country-level breakdown was available, we took the premium income of the parent company and estimated the cost data for the analyzed country, using the percentage of individual country premiums to global premiums. The few companies that did not provide verifiable data on either a country or global level were omitted from the analysis. The shortage of verifiable data explains the omission of China and Japan from the research.

Our Efficiency Model, valid only for non-life insurance companies, indicates the cost and financial-performance ratios of each country based on core and non-core insurance business. The efficiency ratios are calculated using various expense and profit metrics against GWP. The ratios are consistent with industry-defined ratios for individual insurers, but provide a better comparison for industry performance in different regions.

More specifically in our model:

- **Underwriting ratio**—Like the 'combined ratio' industry benchmark, it measures the percentage of gross written premiums an insurer pays out in claims and expenses. The lower the ratio, the less premium revenues are being eroded by expenses.
- **Claims ratio**—(total claims and benefits disbursed) / (GWP)—offers a proxy for underwriting efficiency. In general, a lower claims ratio produces higher returns.
- **Acquisition ratio**—(total commission and fees paid) / (GWP)—reflects the effectiveness with which distribution networks are being managed. While it is beneficial to financial results to keep the acquisition ratio low, these costs are inherently higher in some business models, so it may be more relevant for a firm to focus on the trends in its own acquisition ratios than to benchmark directly against other businesses or regions.
- **Operational ratio**—(total operating expenses) / (GWP)—helps to explain the maturity with which insurers are managing routine expenses. In general, the lower the operational ratio the better.

- **Investment ratio**—(net investment income + capital gains (losses)) / (GWP)—shows returns on insurers' investment portfolios. In general, the higher the investment ratio the better.
- **Profit margin**—(profit before tax) / (GWP)—measures profits from the overall insurance business.

In all cases, ratios depend on a variety of external factors, including general economic conditions, government regulation, business type, consumer preferences, etc. As a result, it is rarely relevant to compare ratios directly across regions. It is typically more germane to compare trends over time within regions, and perhaps within business types or insurance segments.

CAPGEMINI'S PROPRIETARY BUSINESS AGILITY MATURITY MODEL

Business agility measures the speed with which insurers understand and respond to changes in the external and internal operating environment to remain competitive. Capgemini's Business Agility Maturity Framework breaks the insurance value chain into four distinct links: Product Design, Front Office, Policy Administration and Underwriting, and Claims, and defines the levers that influence each link. In all, there are 28 levers for business agility across the entire insurance value chain (see Figure 2.1 in Chapter 2). For the purposes of agility analysis, each lever is then characterized by five maturity levels for agility.

We use both primary and secondary research of individual insurers to assign them a weighted score for agility in each lever. Taking into account the premiums of a given insurer, and the premiums of the country in which that insurer is based, the model then derives a comprehensive regional and global score for agility on that lever. WIR 2012 focuses on business agility in 'Policy Administration and Underwriting'; WIR 2011 focused on agility in the 'Front Office' and 'Claims' links.

We administered a Business Agility Survey as part of our research. The results produced responses from 11 of the top 20 insurance markets across the globe in terms of written premiums in 2010. Results range from mature European and American insurance markets to the emerging Asia-Pacific markets, so we had a diverse set of responses in terms of insurance density and penetration from which to generate insights around differences in agility maturity levels in different regions. The survey also covered a good mix of life and non-life insurers, and firms of small, medium, and large size.

About Us

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