A MAJESCO WHITE PAPER

The Changing World of Risk:

Insurers and Brokers at the Center of Risk

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majesco | Capgemini

Executive Summary

Risk. Every day there are various degrees of it that we deal with as people and businesses. From driving our car to creating the products or services we offer customers; risk is part of our daily lives. For insurers, it is at the heart of what they do – understand, assess, underwrite, and manage risk to provide the right products and value-added services to help customers manage in a changing world of risk.

But risk is changing. Gone is the predictability of risk and its impact and frequency. The rising number of extreme weather events and natural disasters has had a substantial effect on people and businesses – with over 18 catastrophic events in 2022 in the US alone. With rising property prices, materials and repair costs, many insureds lack sufficient insurance coverage, resulting in a gap and increased financial risk.

The 2022 financial impact for P&C insurers is astounding. The US P&C insurance market experienced a $26.5 billion net underwriting loss in 2022, a decline of $21.5 billion from the prior year's underwriting loss, according to A.M. Best. 2022 was a difficult year for the US P&C insurance industry: claims severities surged with inflation and natural catastrophe losses were elevated for a sixth straight year resulting in a loss ratio of 102.7%. State Farm, the largest P&C insurer in the US, had $13.2 billion in losses alone, the highest ever.

While environmental weather and natural disasters such as wildfires, hurricanes, or other catastrophic events, are top of mind, there is a growing set of new risks including societal and technological. And most recently we have once again seen the impact of financial risk with the recent failure of Silicon Valley Bank and the ongoing fallout. As noted in an article in Insurance Journal, the failure was a lack of effective risk management.

As a result, P&C insurers must rethink risk management strategies from products and pricing to claims and prevention. Instead of playing defense, insurers must go on offense. But that requires a different operational and technology strategy and approach.

Recently, Majesco and Capgemini hosted a roundtable with other industry insurer experts to discuss the changing risk environment and what offensive approaches they can take.

Risk Through the Lens of Past, Present, Future

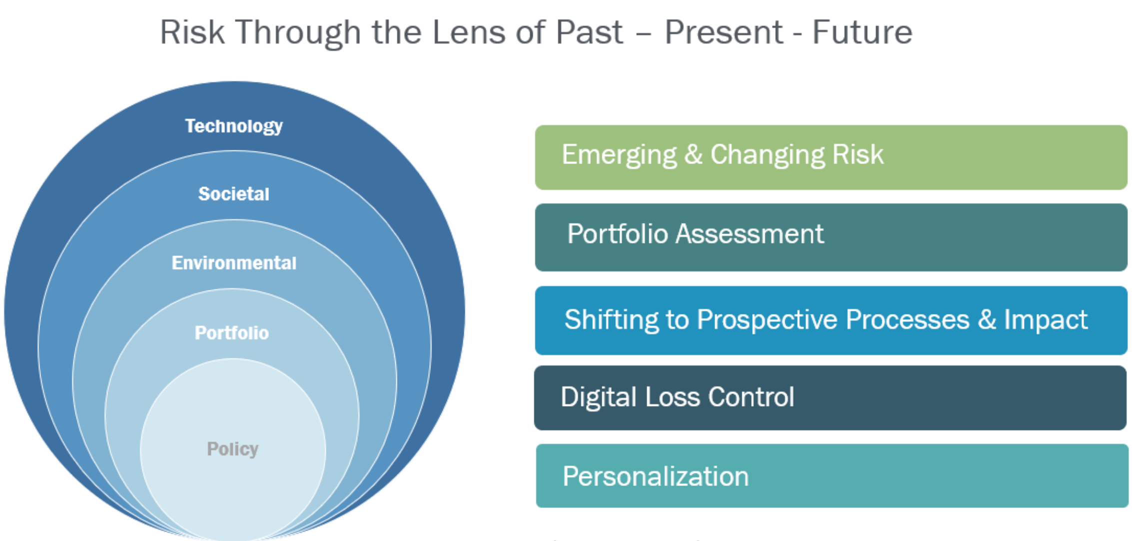
Talk with anyone in the insurance industry and mention that "times are changing," and you get no argument. Not only is the insurance industry changing, but fundamentally risk and the data defining it is changing which is the foundation of insurance.

Risk management and assessment has changed drastically over the last 20 years. While many risks remain, they have more layers of complexity reflected in Figure 1. In addition, new risks are emerging at a velocity the insurance industry is not familiar with. Loss patterns are different, demanding insurance step up to the change.

While in the past, we may have looked at a specific policy risk, today and in the future, we must look at risk through a multi-faceted lens including:

- How a policy risk impacts the overall portfolio risk and ultimately profitability
- What other layers of risk should be considered including environmental, societal, and technology
- How can loss control be used to assess every risk cost-effectively to manage the portfolio, reinsurance needs, and help customers mitigate risk
- How does personalized data shift underwriting and risk

Figure 1



Source: Majesco Research

"Risk has really shifted from looking at it just as a policy level to now looking at it at the portfolio level, determining whether or not you can take on that risk, what's the impact on portfolio profitability."

Roundtable Participant

Just consider one example of risk with Electronic Vehicles (EVs). As EV usage grows, we are now seeing the impact on claims due to accidents. But that is only the tip of the iceberg in risk. In an accident where a Tesla had an accident and had a fire, there were unintended ramifications that many fire stations and first responders do not know because dealing with an EV fire is much different than a fuel-based vehicle fire. EVs conduct electricity, which creates a new risk to consider. They require significantly more water to put out.

Because of the complexities of EVs, many are totaled because replacement of the battery is difficult or impossible to do, increasing the risk and cost. There are many layers to peel back and digest. One of those is the shifting of liability and ultimately who would be responsible for the incident. Would it be the owner? The auto manufacturer? For insurers, it becomes trying to solve a Rubik's cube of understanding all the possibilities and dimensions of risk.

Mindsets need to change within insurance organizations. A wider and broader view is needed given risk and loss patterns are changing.

The good news is that for the most part, change and risk is moving insurance in the right direction. It might be fearful in pace, but certainly not in the opportunity and result that create new value and benefits customers can expect:

- **Greater coverage** — more people and more businesses may find themselves covered through more relevant options and fewer steps to usage, including embedded coverage, reducing the insurance coverage gap.
- **Greater predictive protection** — insurance may improve underwriting profitability, reduce its own costs and customers' costs through a dramatic uptick in data-driven risk assessment for underwriting as well as avoidance or mitigation through proactive solutions.
- **Greater efficiency and effectiveness** — insurers are right now grappling with operational challenges including talent shortages and tech debt that will give them the "excuse" to redesign their operating models and introduce better solutions and ecosystems to improve operational results.
- **Greater resiliency** — a rapidly-growing set of risks is likely to touch off two ancillary trends: new product development and better risk knowledge and response.

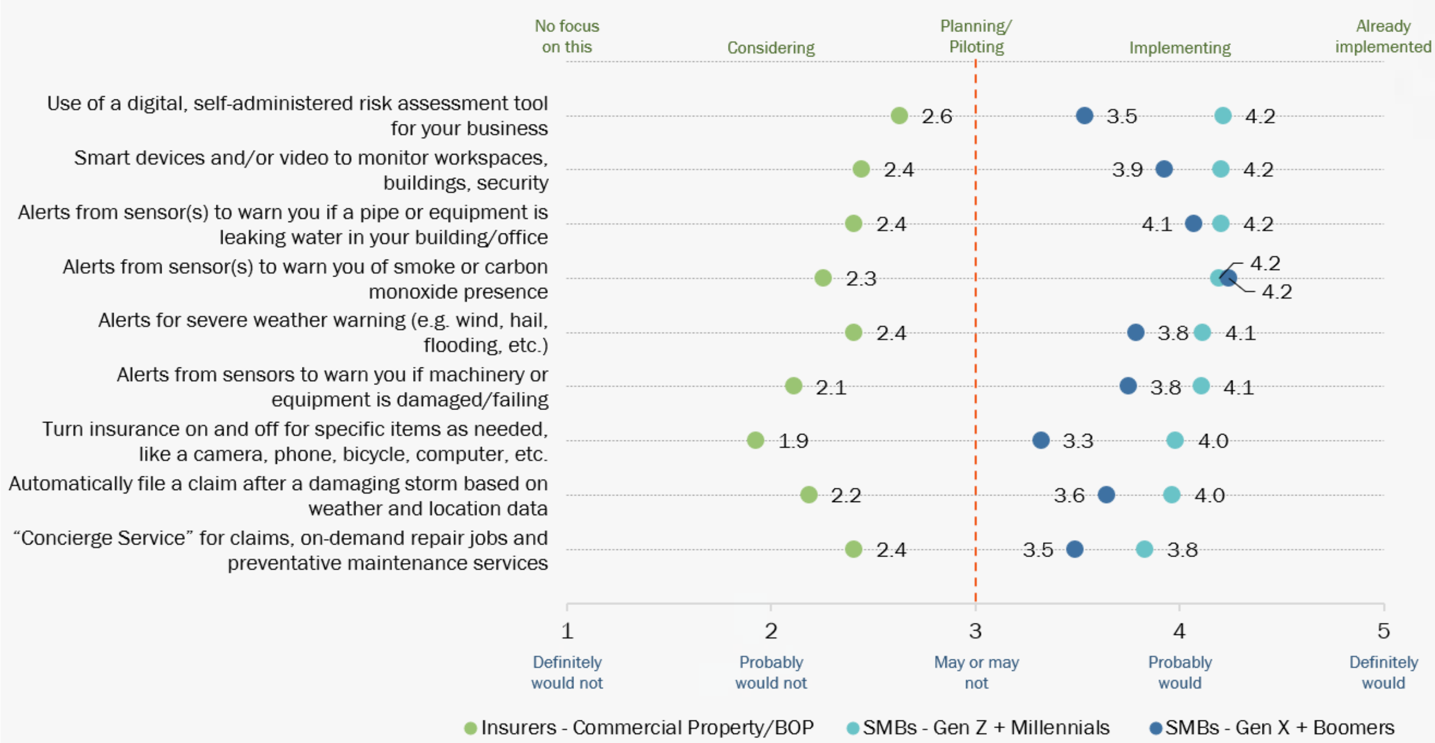
The Influence of the Customer

Today's customers, as we know, have completely different expectations than in the past. They are living different lifestyles and they exhibit far more robust digital proficiency. They demand different experiences, and they have different expectations about value. According to a recent AM Best innovation assessment report, "the rise of digital platforms and ecosystems will make relationships with customers even more important."

These changing expectations and needs are creating a disconnect in their experience and what insurers offer. The disconnect includes customer changing priorities and products needed, demand for risk mitigation and avoidance, personalized pricing and rating based on their specific risk profile, and a need for value-added services that extend customer value and loyalty as seen in Figure 2.

The gaps between customer expectations and what insurers are offering is nearly two-fold for both generational groups of SMBs and similar for consumers, based on Majesco research! Customers want more. To meet the expectations, we need to look at areas that are impacting insurers such as digitalization, data, and risk resilience — new ways of dealing with both the new customer and the new risks we are seeing in today's era.

Figure 2



Customers want personalized underwriting based on their specific data or a continuous assessment of risk. The traditional risk models or once-per-year, traditional approach does not work for the new risks. Data and analytics and how it affects our risk perspective on a micro level is more consumable in ways that do not strain our technology and our underwriting teams.

> "We're getting data from IoT devices, telematics data, and risk specific data. We can get data from anywhere we want that's readily available. That's great news because I think that underwriters and brokers can use that data to help assess and mitigate better."
>
> Roundtable Participant

This is why there is increased interest in usage-based or telematics-based insurance. In today's macro-economic environment, customers are trying to manage their costs, including insurance premiums, hence the increased demand for telematics-based insurance.

A great example of the value is in the recent earnings call from Progressive Insurance Group and a view from Mike Zaremski, Sr. P&C insurance equity research analyst and MD at BMO Capital Markets:

"Progressive is building upon its material first-mover competitive telematics advantage by offering a new crash-detection/safety service to its customers. We estimate PGR's competitive advantage in telematics is also structural in that customer adoption rates of telematics-based policies via D-2-C distribution are multiples higher than via a broker, meaning PGR is building upon its competitive advantage vs. its average peer on a daily basis (note, most of its peers distribute via insurance brokers)."[1]

This leads us into the concept of risk resilience.

We are living in a world that has increasing risk. Insurance can no longer be about just underwriting and then waiting for the claim to happen, but insurance also must help avoid or minimize the risk, creating greater customer value. As shown in Figure 2, value-added services are something that customers crave now.

> "We look at how we engage with digital devices, I think almost every person of every age is looking for a very simple intuitive engagement experience."
>
> Roundtable Participant

Customers want confidence and security, but insurers sell them a loss-recovery contract. While most insurers are focused on how they can better assess risk, many more are expanding to also focus on the prevention of losses and creating risk resilience for customers. The adage of "control what you can control" is now front and center for insurers as they look at new risk management strategies as a crucial component of their underwriting and customer service strategy.

Leading insurers are leveraging technology such as IoT devices, smart watches, loss control assessments, and value-added services to not only assess and monitor risk but to proactively respond to it with mitigation services and actions. From concierge services to monitoring water hazards and the safety of employees, to helping to live healthy lifestyles, leading insurers are shifting to risk resilience strategies that not only drive better business outcomes but also great customer loyalty.

This creates risk resilience.

The Role of Technology and Data & Analytics

One of the crucial areas for insurers to meet the changing world of risk is with technology and data and analytics. They must create a new foundation that enables optimization and innovation through the replacement of legacy systems, adoption of new technologies and embracing the strategic role of data and analytics.

Technology is the crucial foundation to adapt, innovate and deliver at speed to execute on strategy and market shifts. The rising importance and adoption of platform technologies, APIs, microservices, digital capabilities, new/non-traditional data sources, and advanced analytics capabilities are now crucial to growth, profitability, customer engagement, channel reach, and workforce change.

> "We're going to have to be in the cloud. We're going to have to have APIs. We're going to have to have microservices. There's this whole litany of technology elements that really come into the next generation type of technology foundation to really be able to do the things we want to do."
>
> Roundtable Participant

From the front office to the back office, SaaS platforms are reshaping the business focus from policy to customer, from process to experience, from static to dynamic pricing, from point in time underwriting to continuous underwriting, from a historical view of data to predictive and prescriptive data, from traditional products to new, innovative products, and so much more. Insurers' ability to create an interconnected tech foundation will deliver both growth and customer relationship opportunities.

In addition, analytics capabilities are poised to be a game-changer for insurance. When new and real-time data, advanced analytics, AI and machine learning are effectively combined, insurers can have a significant impact across the entire insurance value chain. Data is becoming more readily available and cheaper, becoming a commodity that allows it to spread across the entire value chain. And advanced analytics with AI, ML and NLP are emerging as powerful tools to enhance underwriting, identify and prevent risk, and to drive more efficiencies, leading to better profitability and loss ratios.

> "As we move along this bumpy path, we must do everything we can in our power to minimize frequency, severity and, hopefully, losses. And the best way to do that is through robust datasets..."
>
> Roundtable Participant

The swelling volume of data is creating difficulty for underwriters to uphold the volume of loss data available which is continuously increasing. The market is seeing massive data increases in IoT device data, telematics data, and risk-specific data.

Underwriters and actuaries cannot validate and devise their understandings quickly enough, leading to the necessity of automated techniques needing to be applied to the data to draw insight to create better and expedited business decisions. With the use of more accurate data, insurers can leverage predictive modeling to provide customized coverage and better pricing.

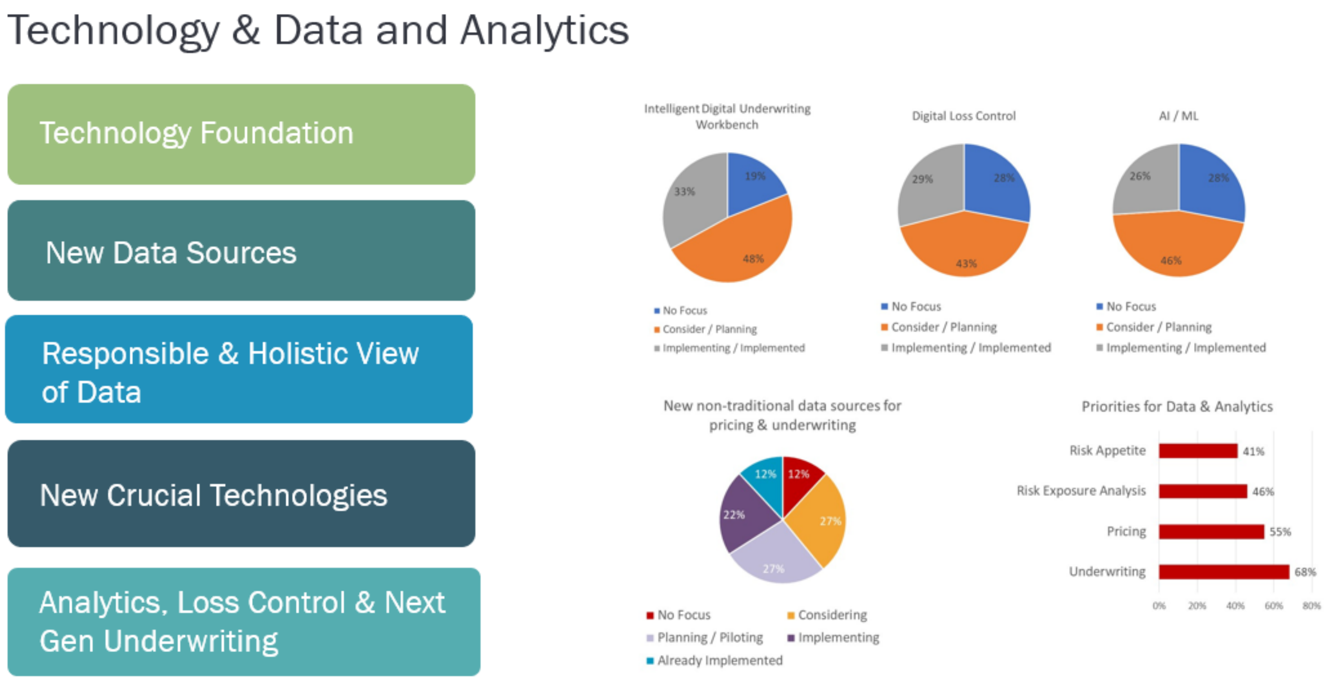
As the competition tightens in the industry, every part of the insurance organization must be committed to the use of next-generation technology and data and analytics to stand out from their competitors and to meet customer expectations.

Those stuck on legacy core systems are boxed in and are limited in their potential. Moving their business to next-gen cloud platforms is crucial, not just for single lines of business, but for the entire business to achieve real optimization and cost reduction. More importantly, it frees up resources to fund tomorrow's business.

Tomorrow's business must be digital, enabling the ability to rapidly introduce new products that capture new market segments, meet new risks, customer needs and expectations, and new distribution channels. It must embed insurance into other products and services to make it easier to understand and purchase.

For insurers, business processes ultimately need to be viewed differently than in previous times. It is about being aggressive in prevention and giving your underwriters (and other team members) the tools, they need to achieve the best results. Ultimately a renewed core and upgraded technology will play a substantial role and help insurers achieve an advanced loss control strategy. Within that technology platform, insurers must also not be afraid to utilize cloud capabilities that can help improve data usage and quicken the time that underwriters are able to produce coverage options.

Figure 3



Source: Majesco Research

The Role of Ecosystems

For decades, insurers have been constructing their own cages of technology and tradition. The idea that they would participate in the free market of open channels, limitless data streams and shared information was unthinkable. That is no longer the case.

Ecosystems are enablers. They take what should be natural in the way we live, work, buy and learn — and they make it happen the way it should. They do this not only for people but for companies, systems, automated processes, and the list goes on. Ecosystems capitalize on what is best in features and flow.

For ecosystems to work effectively, they demand APIs. APIs increase the velocity with which you implement any new or versioned product or process, new technologies, new products, new customer experience, or value-added service. The value of an API is that you can use it in many cases…making APIs the ultimate "value multipliers."

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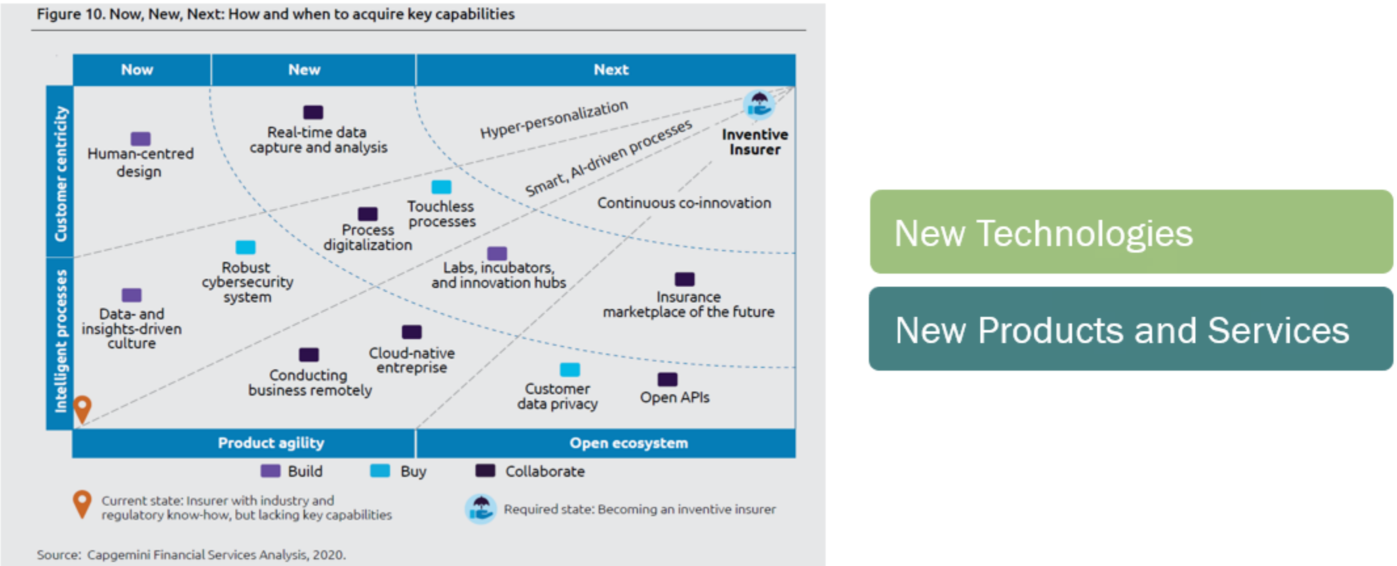
"We can get data from anywhere; we want what is readily available. That is great news because I think that underwriters and brokers can use that data to help assess and mitigate better. But some of the challenges are that underwriters and actuaries really cannot validate and draw their understandings quick enough."

Roundtable Participant

Figure 4

Role of Ecosystems



Source: Majesco Research

The Role of Talent

A 2021 report by the U.S. Chamber of Commerce states: "According to the U.S. Bureau of Labor Statistics (BLS), the number of insurance professionals aged 55 and older has increased 74 percent in the last ten years, leading the BLS to estimate that over the next 15 years, 50 percent of the current insurance workforce will retire, leaving more than 400,000 open positions unfilled."[2]

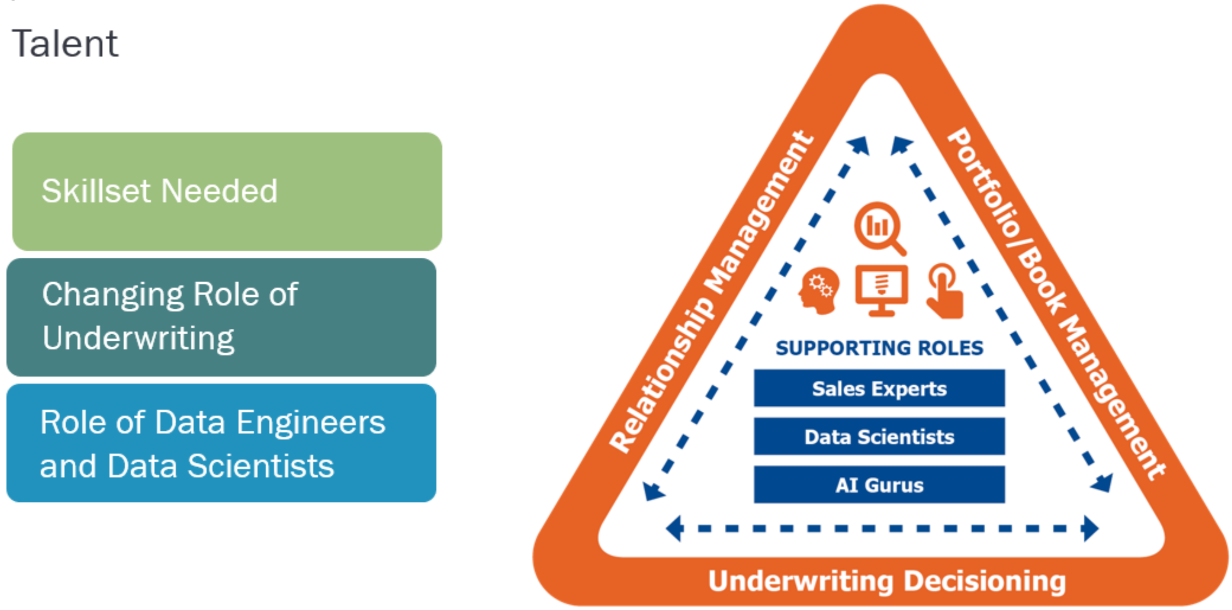
Talent acquisition will focus on Millennials and Gen Z who have higher expectations on the use of technology, putting further pressure on insurers to move to next-gen solutions.

At the same time, the adoption of technology and data and analytics is changing the role of many positions as well as the talent needed, with underwriting being one of those.

"As I think about talent, we have to redefine and talk about how we're redefining risk and where we need skills around those objectives of managing risk, while generating a consistent profit. Those underwriters are going to change and the skills needed will to as well, we can see it."

Roundtable Participant

Figure 5



Source: Majesco Research

Hiring the right talent with the needed knowledge and skillset to use underwriting workbenches that access vast sources of data and use analytics is increasingly critical. Data engineers and data scientists' roles will look at leveraging digital tools and data for visibility into deeper insights. Underwriters will be expected to use more analytics to optimize profitability. Underwriting teams will be sales-focused, leveraging data to seize opportunities, grow new and renewal business, and strengthen and expand relationships.

For example, underwriting at the individual level does not allow the underwriting to uncover drivers of underlying performance; therefore, underwriting will occur at a portfolio level instead. At the portfolio level, the quicker underwriters can identify underlying performance issues, the quicker necessary pivots can occur. It is imperative underwriters have a multi-licensed view of quantitative and qualitative analysis to have a predictive and proactive view of how exposures are expected to change.

Importance of Leadership

The impact of these risks is impacting profitability and growth, as well as channel and customer loyalty – creating potential headwinds to insurers' digital business transformation strategies and plans. The necessity for insurers is to accelerate their digital business transformation because technology and new operating models provide a foundation to adapt, innovate, and deliver at speed as risks shift and change continues its relentless path forward.

It is the leaders who are prepared for the shifts and change, leaping forward from the competition. They are nimble, creative -- and bold -- to remain competitive, relevant and to grow their business profitably.

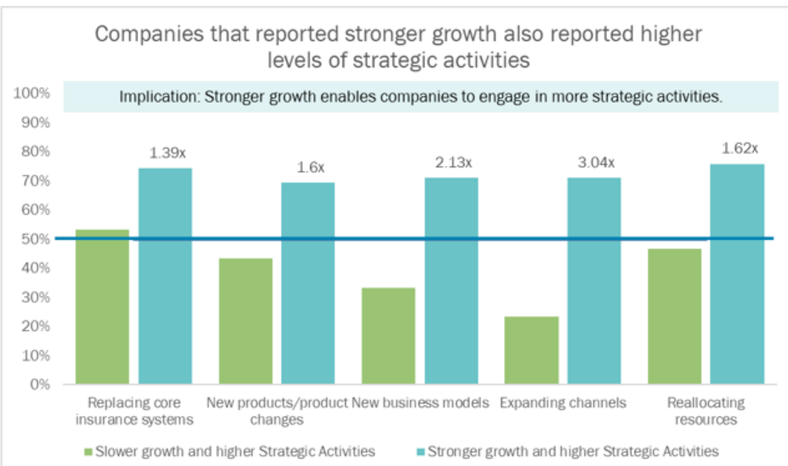
While undergoing this new vision of risk management and instituting the needed tactics to reach that goal, it will be a struggle if leadership does not communicate this image of what they want to the rest of their organization.

It is vital for leaders to produce a consistent message to their managers who can then relay it to other high-ranking organizational team members about what the mission is. Leaders also must understand the importance of change and adaptation. Gone are the days of sticking with the status quo and not being nimble.

In an industry full of change, insurer leadership must also have the willingness to adjust as part of their cultural DNA and learn to accept it. Successful organizations provide a consistent message from the top to the next layer down, get foot soldiers engaged, and relay the benefits of the mission.

Figure 6

Leadership



Business Priorities & Investments

Increase Investments Despite Market Challenges

Leadership for the Future

Source: Majesco Research

Leadership priorities should be focused on investments that will advance their ability to connect with customers and provide them with the ultimate experience. Customers are driving the bus when it comes to changes that are going on in the industry. It is up to insurers to force the change of company priorities and the importance of reinvestment in different areas that will help achieve better company efficiency.

Leadership's focus needs to be on getting team members to be comfortable with the constant change, understanding that pivoting investment dollars may need to happen as the market shifts, setting the right targets to measure, and constantly evaluating them.

The most effective leaders will have to be incredibly good at ingesting all the information at their disposal and be good storytellers of how these various changes will benefit the company in both the short and long term.

> "It really takes some strong leadership to help kind of guide that change and to force that change sometimes in a reprioritization and a reinvestment in different areas.."
>
> Roundtable Participant

Fundamentally, what separates successful Leaders from others is their focus on strategy – both operational and strategic. Leaders execute on their strategy and adapt where they need to but focus on execution diligently.

Conclusion

Over the last number of decades, insurers have demonstrated remarkable agility and resilience in light of many hurdles and challenges as it relates to the changing world of risk.

Undertaking digital transformation begins with customer-centricity. A true customer focus will drive insurers to deliver the capabilities that create great customer experiences, offer the products they want, and reach them through the channels they want that drive loyalty, growth, and profitability. But this requires insurers to rethink their business priorities and investments.

An investment in platform technology is a huge step for insurers to take to keep themselves ahead of the rest of the competition when it comes to risk prevention. Better technology is more responsive to changing risk data, new customer needs, and simulation to predict future risks on the horizon. Data is playing a substantial role in helping customers' underwriting experience. An enhanced platform will allow insurers to intake data quicker, make faster and better decisions, and provide the right risk profiling for underwriters. The ubiquity of data coming into organizations is unlike anything we have ever seen, which is why having a solid data platform is necessary for success. No longer can past assumptions be used. The amount of data being consumed within days and months is substantial and must be used to advance all facets of the business.

Like any business, insurers want to see a high ROI. The biggest fear of any insurer (or business) is picking the wrong bet on where the direction their organization needs to go. In the investing process, the best ROI would be in processes that touch the customer the most. We know the importance of designing the best customer experiences.

The importance of the investment in designing experiences around the customer throughout their time cannot be ignored. For that to happen, data and insights must flow within the company. Part of the investment should also include the ability to quickly pull out of technology if it is deemed to not be satisfactory and integrate versions that are a better fit. The consequences of not innovating and letting technology and data play a principal role will put insurers in a hole that may be hard to overcome.

Customer demand should drive us where our innovation is, not whether we do it at all. In the new world of risk, insurers must adapt their business to the changes that are happening around them or fail to be passed up by the rest of the competition.

Strategic discussions on how you prepare and manage the changing world of risk and the implications in your business models, products, channels, data and analytics, and technology is more important than ever.

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[1] Applebaum, Stephen, Demers, Alan, "Special Edition - Crash Detection: Consumer Safety vs. Insurance Claims Applications," Connected, March 2, 2023, https://connected.curated.co/issues/40?#start

[2] "The America Works Report: Industry Perspectives," U.S. Chamber of Commerce, June 1, 2021, https://www.uschamber.com/workforce/education/the-america-works-report-industry-perspectives