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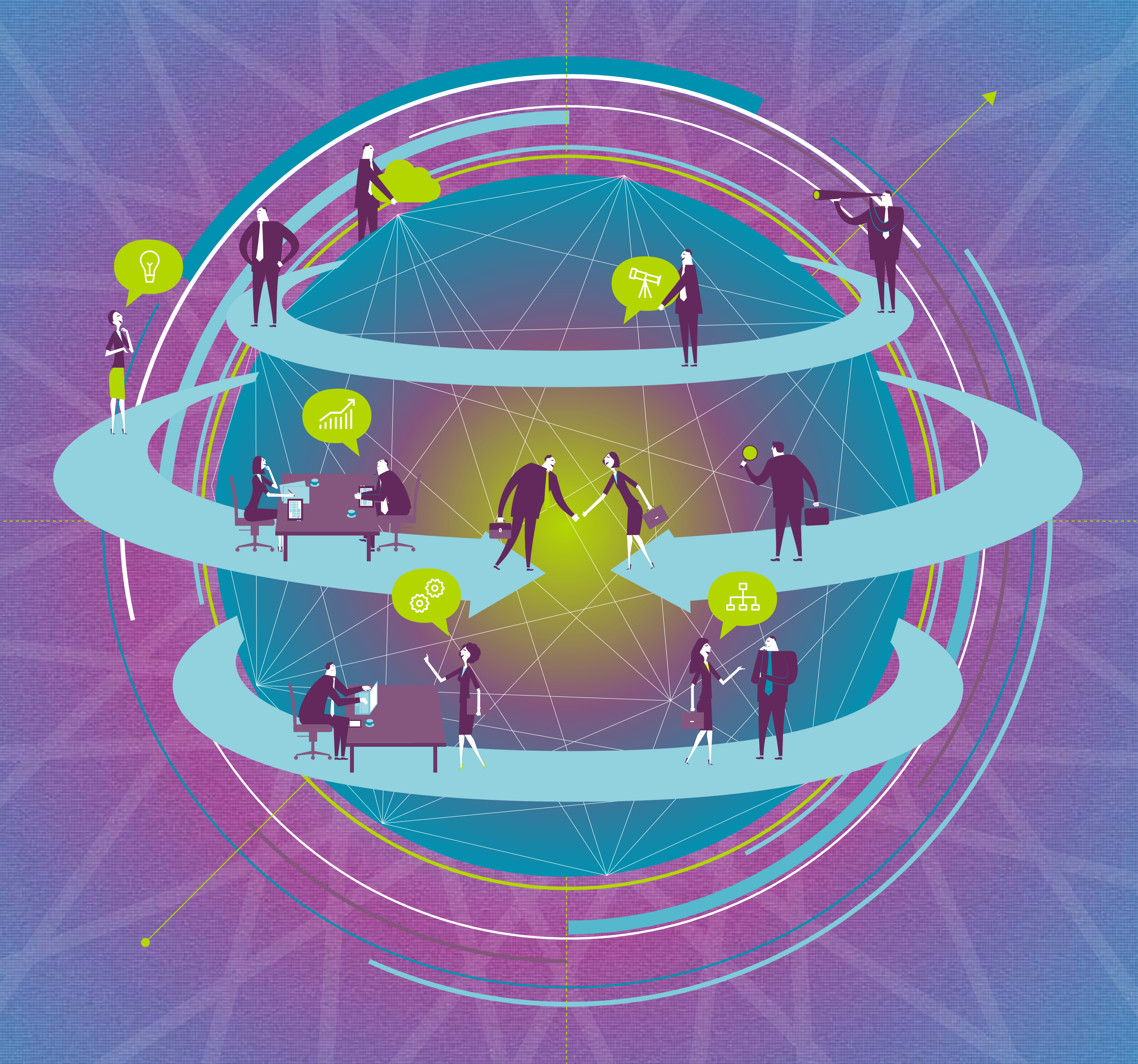

# Building new ecosystems in middle-market insurance

A research report by the Deloitte Center for Financial Services

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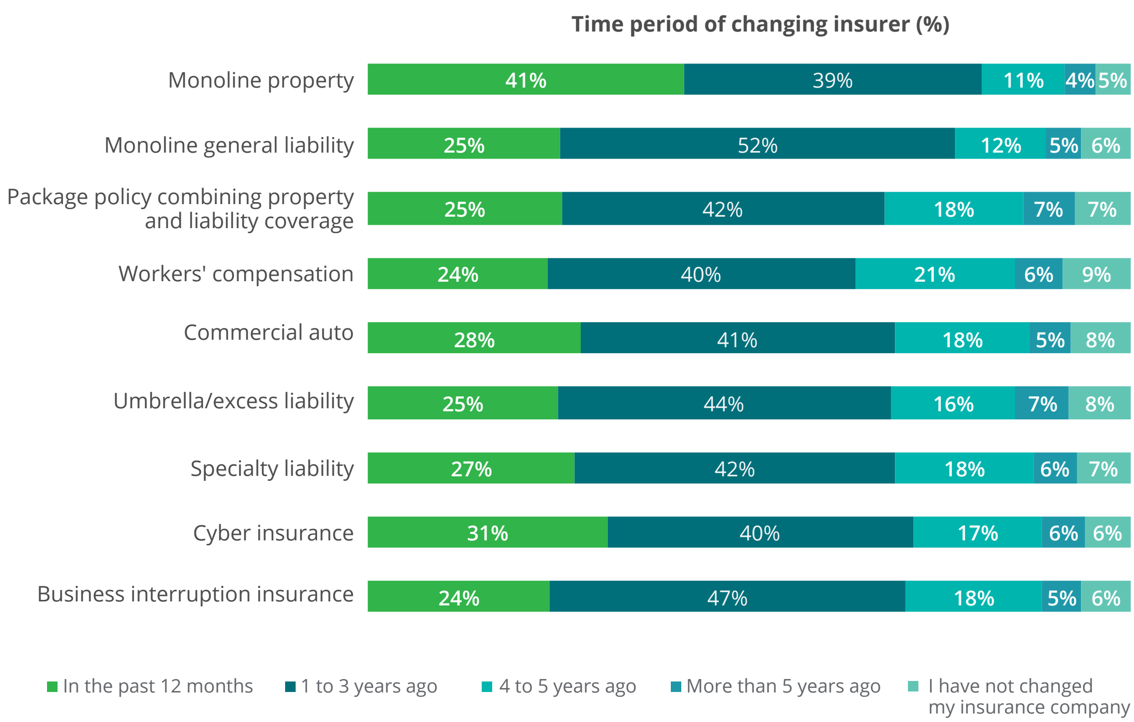
# Insurers should fortify middle-market accounts

## Bundling could raise the stakes for price shoppers

Many middle-market commercial insurers are looking for new ways to maintain and expand penetration and retention rates in an increasingly competitive, cost-conscious environment, with turnover on the rise. Indeed, at least one-quarter of buyers surveyed by the Deloitte Center for Financial Services had changed one or more of their carriers in the prior 12 months, while over two-thirds had switched at least once in the past three years (see figure 1).[1] Intermediaries surveyed confirmed the churn rate in this segment, with nearly one-half of respondents reporting that between 11 percent and 25 percent of clients part ways with at least one of their insurance companies in a typical year.[2]

One reason behind this volatility could be rate softening over the past few years in a number of commercial lines. When deciding whether to remain with a carrier or switch at renewal, most middle-market customers and intermediaries participating in Deloitte's survey cited *price* as the most important consideration.[3] (For details about who was sur-

**Figure 1. How often have middle-market buyers changed insurers?**




Source: Deloitte Center for Financial Services' *Middle-market insurance consumer survey*, 2017.

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veyed, see the section, "What do buyers think about expanded services?" below.)

Looking ahead, competition for this segment is likely to intensify. Carriers currently focusing on other lines and segments—such as small business, auto, and home insurers—may soon turn their attention to larger-premium accounts and comparatively stickier markets where higher-level underwriting and actuarial capabilities can yield more profitable results.[4] The entrance of new players should result in greater capacity, which would further increase pricing pressure on middle-market insurers.

However, this volatility may also create opportunities for insurers new and old to capture market share and improve retention rates through meaningful differentiation. But how can insurance companies set themselves apart from competitors when product distinction and prices are decreasing for major business lines, while demand remains fairly constant?

To meet this challenge, product innovation, segmentation, and bundling have been fundamental options, not just in insurance marketing but also across most industries for quite some time now. Many insurers in personal and commercial lines have taken one, two, or all three of these paths to differentiation at some point. However, few have been bold enough to stray far from their traditional offerings providing basic risk transfer, loss prevention, and claims management support.

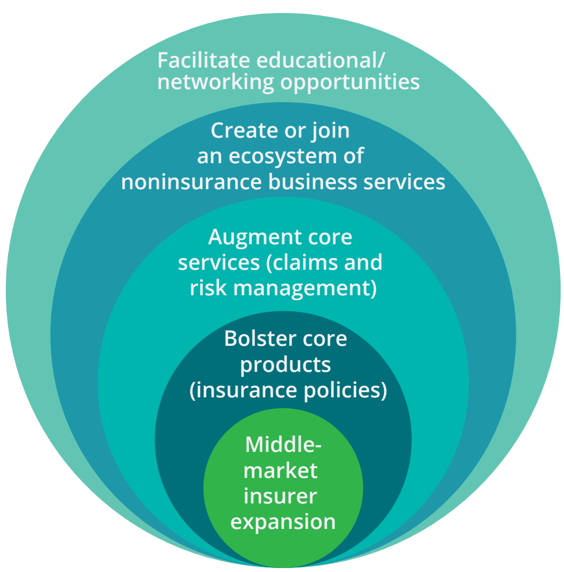
In this report, backed by our primary research, we suggest that middle-market insurers may want to consider expanding their horizon well beyond the standard product and service options they typically offer policyholders (see figure 2). This would involve creating or joining a much broader ecosystem offering a wider range of business support solutions, as well as facilitating educational and networking opportunities for customers.

Why would middle-market insurers choose to undergo this kind of business model transformation? The goals would be to:

1. escape a race to the bottom on price;
2. set companies apart as competition intensifies;
3. provide greater value and convenience to customers;
4. improve retention; and,
5. ultimately, command a larger piece of the overall market share pie.

However, an important question remains: Will policyholders be open to a much more comprehensive service relationship with insurers?

**Figure 2. Combatting commoditization by bundling nontraditional services**




Source: Deloitte Center for Financial Services.

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## A significant percentage of respondents were open to the idea of having insurers help arrange a much wider array of business services other than the risk and claims management support they currently provide.

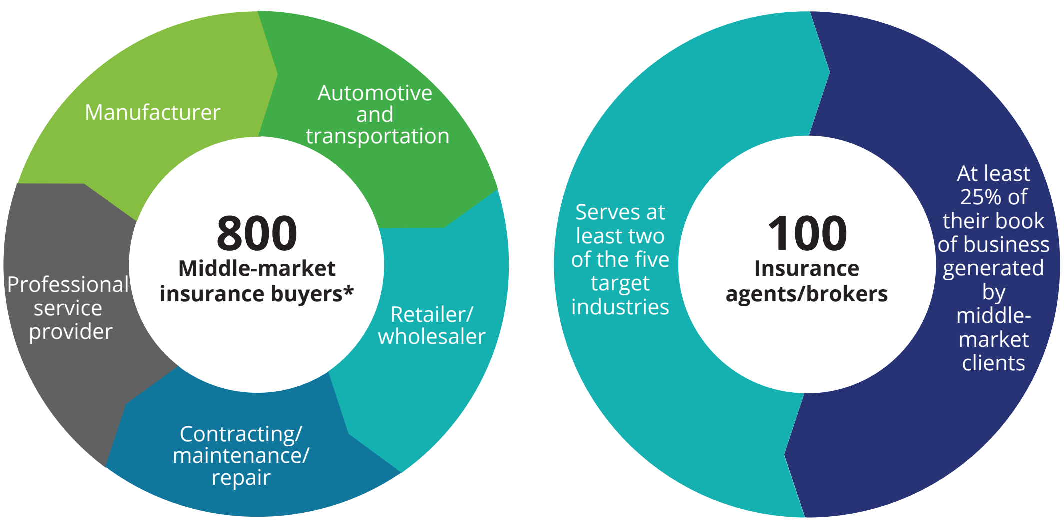
### WHAT DO BUYERS THINK ABOUT EXPANDED SERVICES?

To understand the evolving attitudes, expectations, and needs of middle-market insurance policyholders, Deloitte surveyed 800 buyers in this segment, spread evenly across five industries and four business size categories (see figure 3).

We asked the buyers to look at their insurers in an entirely new light—as a source of a broader range of services adjacent and even unrelated to insurance that could help policyholders protect their assets as well as manage and grow their businesses.

The survey revealed that insurers targeting the middle market do indeed seem to have a number of opportunities to differentiate their value proposition beyond price and other traditional cost-related levers such as deductibles, limits, and endorsements. A significant percentage of respondents were open to the idea of having insurers help arrange a much wider array of business services other

**Figure 3. Middle-market survey respondent breakdown**




*"**Middle-market buyers**" are defined as those making business insurance purchasing decisions at companies with between 26 and 1,000 employees, and who pay more than $100,000 and less than $2.5 million in annual premiums outside of group benefits products. Survey breakdown based on number of employees (26–100, 101–250, 251–500, 501–1000).

Source: Deloitte Center for Financial Services' *Middle-market insurance consumer survey*, 2017.

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than the risk and claims management support they currently provide.

Widespread disintermediation and direct sales in the middle market is unlikely for the near future, due to the complexity of coverage, the level of risk involved, and the need for experienced advisors to support buyers in this segment. Therefore, insurers looking to substantially broaden their service offerings will likely need to work in conjunction with their distribution force to ease the way forward into this new service-centric model.

With that in mind, to see if intermediaries would be on board with groundbreaking brand extensions, Deloitte conducted a separate survey of 100 agents and brokers with at least 25 percent of their business generated by middle-market clients (figure 3). The survey found them thinking along similar lines as their clientele. They also appear keen to add a broader array of services to their sales repertoire.

By facilitating or participating in the creation of a new, holistic middle-market ecosystem for business support services, insurers could conceivably achieve preemptive differentiation. This is not a new concept—at least not outside of insurance. As reported in a Deloitte Insights study, *Introduction: Business ecosystems come of age*, in general, many businesses are "moving beyond traditional industry silos and coalescing into richly networked ecosystems, creating new opportunities for innovation alongside new challenges for many incumbent enterprises."[5] The rise of such ecosystems is often "an opportunity for creating powerful new competitive advantages."[6]

To execute this transformation, insurers would likely need to take proactive steps to convince policyholders—as well as their agents and brokers—that a comprehensive portfolio of products and services is too valuable to disregard or abandon, even when insurance pricing may rise or cheaper coverage options are available. The objective of such a bundling strategy is typically to establish stronger, more elastic, and longer-lasting customer relationships, increase market and wallet share, and ultimately improve the bottom line.

In addition, to venture outside their in-house capabilities, insurers looking to be the hub of a more comprehensive ecosystem would need to build relationships with noninsurance service providers. Indeed, the ability to create and maintain a broad, high-quality services network in and of itself could be a critical differentiator for insurers.

As an alternative, carriers that don't feel comfortable creating a hub of their own could decide to join another facilitator's network of providers, becoming the insurance spoke in someone else's services wheel. In either case, whether taking the lead or joining another network, insurers would need to seek out and negotiate symbiotic arrangements with a variety of outside service providers to make this vision a reality.

# Insurers have options to achieve preemptive differentiation

## Buyers appear open to receiving broader business services

Middle-market carriers, along with their agents or brokers, often provide a range of insurance-related services to help policyholders prevent or at least limit potential losses, as well as facilitate claims handling should an event occur. This is typically an important element of an insurer's relationship with many buyers. For example, 55 percent of those surveyed by Deloitte cited *risk management services* as a key factor influencing their insurance purchase and renewal decision—the second most chosen option, topped only by the *price of the policy*.

In a deeper dive, Deloitte asked the respondents to choose the most and least valuable among a rotating group of traditional insurance-related options. The most popular choices to bolster a carrier's core value proposition included *multiyear policies with known premiums*, as well as *risk management advice tailored specifically for their industry*. *Crisis management/recovery* and *cybersecurity services* also scored high among respondents. A large majority of the intermediaries surveyed said such additional service options were so valuable that they think clients would be willing to pay additional fees to receive them. This indicates that at the very least, insurers should continue to advance the ball with enhanced policy, loss control, and claims management options to remain competitive.

However, to truly differentiate in a market prone to price sensitivity and commoditization, insurers should now consider the potential advantages of assuming a bigger role in supporting the businesses of their middle-market customers. Many of the buyers Deloitte surveyed were enthusiastic about the possibility of establishing a much broader business services relationship with their insurance carriers.

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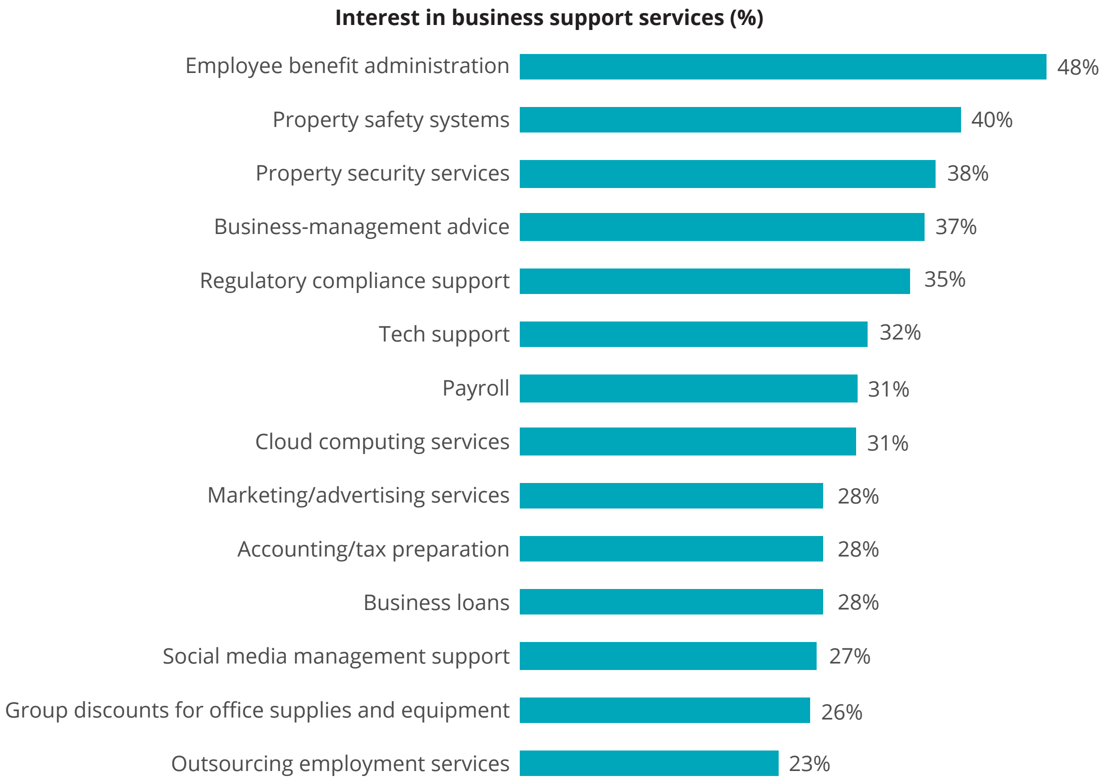
Nine out of 10 buyers surveyed said they would "welcome receiving additional business-support services" through their insurance company. Agents and brokers were supportive as well: Not only did most of the intermediaries surveyed indicate that significant percentages of clients would be interested in getting nontraditional services via their insurers, 86 out of 100 said they would "welcome" the opportunity to broker these added-value options on behalf of carriers.

While some possibilities seemed much more popular than others among buyers, at least one out of four surveyed expressed interest in each of the options provided (see figure 4). *Employee benefit administration* was the clear favorite, chosen by nearly one-half of respondents.

**Figure 4. What percentage of buyers were interested in receiving noninsurance business services via insurers?**




Note: This is a multiple select question. Percentages may not equal 100.

Source: Deloitte Center for Financial Services' *Middle-market insurance consumer survey*, 2017.

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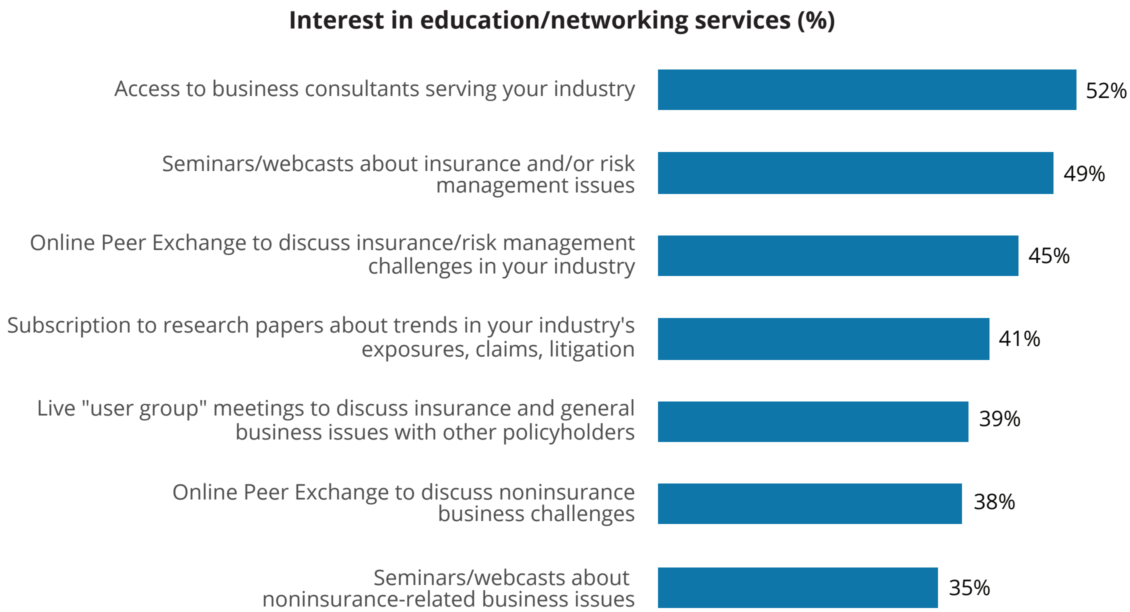
Property safety systems and security services were the second and third choices, respectively. *Business management advice*, *regulatory compliance help*, and *tech support* were also picked by about one in three respondents. A host of other possibilities, ranging from group discounts for office supplies and equipment, to business loans, payroll, and cloud computing services drew considerable interest as well.

For the most part, patterns were consistent across industries, with some differences depending on the respondent's business. For example, interest in cloud computing services was higher among professional services providers. Insurers should therefore consider customizing their additional service offerings to the particular needs of the targeted industry segment.

We also surveyed middle-market buyers to assess their openness to receiving educational and business networking services through their insurers. At least one out of three respondents expressed interest in receiving each of the proposed services. *Access to consultants focused on their industry* ranked highest, checked off by just over 50 percent of those surveyed (figure 5).

However, the respondents were much more interested in educational and networking services of all kinds—seminars or webcasts, peer exchanges, or research papers—when they were tied closely to their core insurance and risk management concerns. Interest waned when such opportunities addressed noninsurance and more general business challenges, although at least one-third of the respondents were still open to such options.

**Figure 5. What percentage of buyers were interested in receiving educational/networking services via insurers?**




Note: This is a multiple select question. Percentages may not equal 100.

Source: Deloitte Center for Financial Services' *Middle-market insurance consumer survey*, 2017.

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# Bundling, networking may become the ultimate differentiator

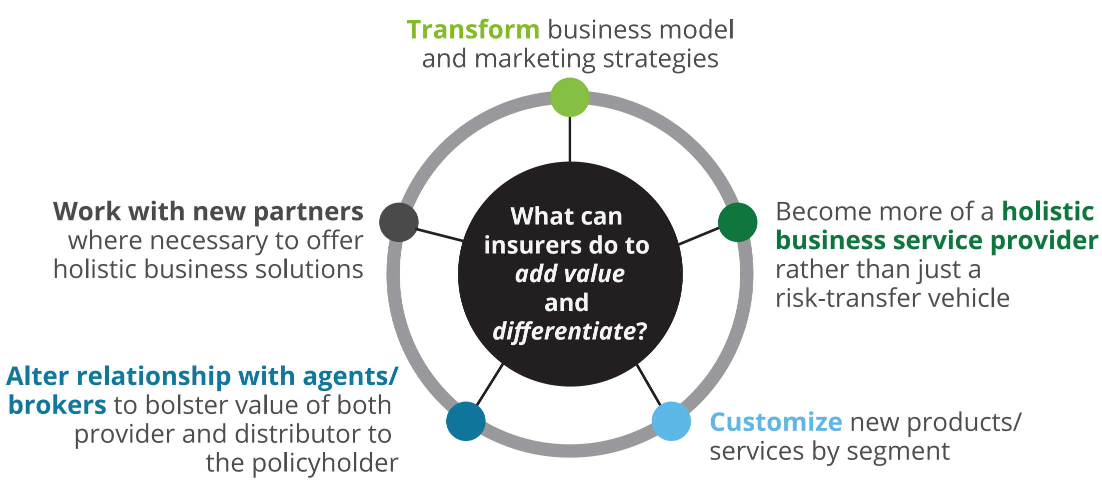
## If you build it, will middle-market buyers come, and will they stay put?

Creating and maintaining a more comprehensive business-support ecosystem, with an insurer as its hub, will likely require carriers to expand beyond long-established comfort zones and implement creative fulfillment strategies (see figure 6).

By entrenching themselves in a policyholder's day-to-day business operations as conduits to non-insurance services such as employee benefit administration, business consulting, and cloud computing, carriers can potentially strengthen their value proposition to clients, putting them in position to improve acquisition and turnover rates. Revenues might also be bolstered by commission or referral agreements with participating vendors, as well as potential fees from customers. And given the increased interconnectedness that will likely result, insurers may be able to harvest new sources of data for more customized and precise underwriting and claims processing.

However, effectively executing the game plan outlined in figure 6 will likely require a number of adjustments to a typical insurer's mind-set, approach, and standard operating procedures. Such considerations may include the following:

**Figure 6. The road to preemptive differentiation in middle-market insurance**




Source: Deloitte Center for Financial Services.

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### 1. DETERMINING HOW TO TRANSFORM THEIR BUSINESS MODEL TO EFFECTIVELY LEVERAGE A BUNDLING ECOSYSTEM.

Carriers may want to take more of a portfolio approach in coordinating insurance and noninsurance services for their customers. Cyber risk mitigation is a good example. If carriers facilitate loss-control support to help clients become more secure, vigilant, and resilient, that could also likely improve the policyholder's risk profile for a cyber insurance endorsement or stand-alone policy. The same principle could be applied for those arranging property protection or security services for clients. Therefore, this new business model also likely involves expanded, interrelated factors for insurers to contemplate when underwriting and pricing policyholder risks.

### 2. BECOMING A MORE COMPREHENSIVE BUSINESS SERVICE PROVIDER ALSO MAY REQUIRE A SHIFT IN OPERATIONS.

Many insurers (and their intermediaries) still maintain a silo mentality, with each coverage line operating as its own business unit, undermining cross-selling capabilities. This same dynamic could hinder any attempt to broaden a carrier's horizon to include more noninsurance services and external providers. While each product and service offering should stand on its own in terms of viability and profitability, carriers pursuing this strategy will still likely need to revamp their cross-marketing and distribution efforts, as well as their technology infrastructure to support the new ecosystem. They may also need to calculate, monitor, and assess prices, costs, and overall profitability of accounts in a more holistic way.

### 3. CUSTOMIZING NEW SERVICES CAN HELP IMPROVE AN INSURER'S VALUE PROPOSITION.

Leading middle-market insurers are often aligned by industry segment, a strategy seemingly validated by Deloitte's survey respondents, who indicated a clear preference for products and services tailored to their particular type of business vs. more generic, off-the-shelf offerings. Insurers should capitalize on this preference by customizing their extended services portfolio to the types of industries and businesses they are targeting.

For example, insurers focused on manufacturers could offer a wider array of property security and safety systems, as well as sensor-driven monitoring of equipment, commercial vehicles, and even the actions of individual workers to red flag potentially dangerous situations and prevent accidents. To accomplish this, it would help to educate buyers about how these additional services could help them limit losses while improving productivity and profit margins. Many survey respondents were ambivalent about permitting ongoing surveillance of their operations, perhaps due to concerns that real-time oversight might lead to higher, rather than lower, premium rates if potential vulnerabilities are spotted—at least in the short term.

### 4. COLLABORATING EFFECTIVELY WITH A VARIETY OF THIRD PARTIES OUTSIDE OF INSURANCE.

Many of the nontraditional service options we raised in this study—such as office supply and equipment discounts, tax preparation services, and business loans—would require the involvement of additional providers. Indeed, the ability to bundle groups of services and maintain a network of noninsurance vendors working symbiotically with carriers could be a major differentiator in its own right. Early adopters of this new business model may be able to gain a competitive edge over those who follow by establishing relationships with leading service providers, preferably on an exclusive basis.

Some carriers may feel they are unable or unwilling to become a hub for other noninsurance service providers. However, as noted earlier, such carriers could still benefit from a bundling model by joining another facilitator's ecosystem. That might involve partnering with a noncompeting insurer (for example, a professional liability writer becoming part of a services network established by a workers' compensation carrier), or a collaborator outside the insurance industry (such as a tech company, retailer, or manufacturer).

## Intermediaries play a key role in cultivating a new ecosystem

Last but not least, to effectively execute this business model transformation and launch a new ecosystem, middle-market insurers will most likely need to get their agents and brokers solidly on board.

The vast majority of intermediaries surveyed indicate they would welcome the opportunity to provide additional services to clients, including many options well outside the norm. However, this does not necessarily mean agents and brokers will fall in line when approached to sell an entirely new business-support ecosystem. On the contrary, they will likely want to know exactly what they are getting into, what is expected of them, and how they will be remunerated for their efforts.

Indeed, compensation could turn out to be the most challenging sticking point. Will it ultimately be worth an intermediary's time and effort to market the additional services, especially those that don't directly relate to insurance or risk management? One insurer we spoke with about this challenge suggested that just as a multifaceted, services-oriented approach could help steer policyholders away from a purely price-driven relationship, the same dynamic could conceivably work with certain intermediaries. This could help insurers move beyond pure insurance sales commission considerations to having a broader discussion about new revenue streams and stronger acquisition and retention potential.

In any case, it would likely be a good idea for insurers to get feedback from key producers early in the transformation process. Input could be sought up-front about what it might take to market a broader business-support network, rather than just present the new services menu to the distribution force as a done deal. Carriers may even want to make test runs of their new approach with a select group of distributors before attempting a wider rollout. Such collaboration with distributors could generate valuable feedback for insurers and help promote greater cooperation and enthusiasm down the road among those charged with selling the idea to policyholders.

Ultimately, the determining factor may be how well insurers can make the case that they are offering nontraditional business support, educational, and networking options not just to bolster their own value, market share, retention rates, and bottom line, but those of their intermediaries as well. Here, the role of agents and brokers could be transformed into broader business consultants providing clients with customized, concierge services.

To effectively execute this business model transformation and launch a new ecosystem, middle-market insurers will most likely need to get their agents and brokers solidly on board.

# Moving forward: Where should middle-market insurers go from here?

THERE are a number of questions carriers should address as they consider becoming a hub for a broader range of services, or whether to join someone else's network. Insurers will likely need to resolve these issues before proceeding with a nontraditional services-oriented transformation. Strategic and operational considerations may include:

- **Business lines:** How might this initiative impact the design and pricing of various insurance products? Would the effort and cost justify the potential gain in improved closing rates, retention levels, and additional revenue streams? How would "success" be measured?
- **Operations:** How would this transformation impact an insurer's product management, actuarial, underwriting, information technology, marketing, and finance functions? What new resources, skill sets, and training might be required? Who would be responsible for managing the new vendor relationships? Would offering any of these ancillary products and services raise regulatory compliance issues? Would there be any potential legal liabilities to consider?
- **Marketing:** How would carriers get the word out about their transformation to customers, prospects, and distributors? How could they best leverage advertising and social media to tout themselves as a hub (or a participant) in a new ecosystem? Should insurers rebrand themselves as full-service business-support providers?
- **Distribution:** How should agents and brokers be included in the planning process? Should insurers make test runs with a smaller group of intermediaries? What incentives would distributors be offered to broaden their service offerings beyond insurance and more traditional services? What kind of marketing support and training might be required? How would insurers deal with productive insurance sellers who resist or reject a broader services program?
- **Partnerships:** How would insurers recruit outside service providers to form their new ecosystem? Would this be a new source of revenue for insurers and their distributors, or simply a value-added customer acquisition and retention tool? What are the reputational risks of partnering with third-party service providers outside of an insurer's direct control, and how might such risks be managed? Would becoming the insurance provider in someone else's multiservice ecosystem be preferable to running a hub of their own? If so, what options are available to collaborate with other insurance and noninsurance providers?

# Closing thoughts

## Decommoditization could be critical for future growth and profitability

The options laid out in this report are not radical. On the contrary, they are in line with a broader movement toward bundling a wide variety of customized products and services and creating a broader ecosystem under one central facilitator. Many cable television companies aiming to prevent customers from switching carriers or cord-cutting are now offering telephone, Wi-Fi, cloud storage, home security, and cellular phone services as a package. For many years, the travel industry has attracted customers by leveraging partnerships to provide discounts on fares, hotels, car rentals, and other amenities.

Most insurance companies have not yet adopted such a model, or at least have not done so in any bold, comprehensive, or brand-differentiating way. Many remain siloed in their business lines and conservative in their service offerings. That will likely need to change, however, given the emerging competitive realities of the middle market, as well as the growing number of consumers gravitating toward convenience and one-stop shopping in other aspects of their business and personal lives.

Indeed, once competitors start reinventing themselves to remain relevant and thrive in this rapidly evolving, ecosystem-driven era, the biggest risk middle-market insurers may ultimately face is standing pat and perpetuating the status quo.

# ENDNOTES

1. Deloitte Center for Financial Services, *Middle-market insurance consumer survey*, August 2017.
2. Ibid.
3. Ibid.
4. World Economic Forum and Deloitte, “The future of financial services: How disruptive innovations are reshaping the way financial services are structured, provisioned and consumed,” June 2015.
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