Getting strategic about inorganic growth: Insurance CEOs speak

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Insurance chief executive officers (CEOs) are becoming much more strategic about their inorganic investments.

While the pace of deal making in the insurance sector may have slowed when compared to the prior year, our survey of more than 100 insurance CEOs indicates that appetite for inorganic growth remains high.

Almost half of all insurance CEOs — 45 percent — say they expect to undertake a merger with another firm in the next 3 years. Around four out of 10 say they will either buy or sell a business, asset or capability set from (or to) another firm. Half of the CEOs we surveyed believe that inorganic growth will be key to achieving their growth strategies.

Why, then, has this not translated into a flurry of deal making and consolidation across the sector? In large part, it is because insurance CEOs have become much more strategic about their investments.

Although many insurers expect to conduct traditional mergers and acquisitions over the next 3 years — our data demonstrates that they are equally (if not slightly more) keen to create partnerships and joint ventures with other firms to innovate and achieve their strategic objectives.

Our experience suggests that many insurance executives have become much more focused on creating stronger alignment between their mergers and acquisitions (M&A) activity and their business strategy. They are thinking carefully about how their businesses will win in their markets, and they are looking for acquisitions and partnerships that could help them enhance their competitive advantages. They are reshaping their portfolio of businesses and assets, centers of operational excellence and markets to meet future growth opportunities. And they are thinking carefully about what capabilities and skills they will need in order to innovate and win in the future.

Strategy-driven transactions

For most, this journey will start with formulating a very clear understanding of what makes their business unique and competitive in the market and then using that information to start to assess the real value and strategic fit of potential acquisition targets.

Say, for example, your business is a market leader for superior customer service. Assets or businesses that could help brandish those credentials or improve those capabilities should therefore be of higher value to you than they would be to a competitor who competes based solely on low prices. With this information in hand, insurers should be able to make more value-based investment decisions that ultimately lead to achieving their long-term strategic growth objectives.

Applying the strategic lens

Leading insurers are also starting to take a much more holistic approach to evaluating potential acquisition and partnership opportunities. They now look beyond the traditional financial due diligence aspects of evaluating the deal to also consider the strategic fit of the target's business model and the potential risks associated with integrating the target's operating model.

In most cases, this means extending and expanding the due diligence process at both ends: at the top end by including a more strategic analysis of the target's medium-term strategy; and at the back end where insurers are starting to conduct more strategic integration risk assessments of the target's businesses, its people, processes and systems that they are hoping to acquire and integrate into their operating model.

Creating alignment

In many cases, this may require closer alignment between members of the existing M&A function, the strategy function and corporate development function to enable strategy-driven transaction identification and evaluation for long-term growth. It will certainly require tighter screening and more frequent communication among the functions for better coordinated planning and execution of transactions.

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This article is part of KPMG International's CEO outlook series for the insurance industry. Data has been taken from KPMG International's global CEO outlook survey of 1,268 chief executives from Australia, China, France, Germany, India, Italy, Japan, Spain, the UK and the US. Of these, 105 are from the insurance industry.

It may also require a reassessment of the objectives and priorities of the M&A function to focus more on the expected and actual value that transactions deliver rather than simply on the successful execution and closing of transactions.

More than one lever to value

When we work with insurers to improve the value of their inorganic growth strategies, we focus on what we call the 'Nine Levers of Value'. The process allows executives to not only drive improved alignment between strategy and capability, but also to achieve a more holistic view of the relationships between each lever.

By focusing on the levers of value to evaluate a potential target's business model and create improved alignment with the potential target's operating model, insurers could have a much clearer view of how value is created for their businesses by adopting a strategy-driven transactions perspective. The point is to go beyond the traditional deal and transaction metrics to truly understand how value is created and what assets — at what price — will deliver that value.

The nine levers start with understanding your financial and strategic objectives over the next 3 to 5 years. The process then challenges executives to think critically about how their current markets, products, brands and customer segments help achieve those goals. With this information, the organization can then start to think about what technology, people and processes it would need to achieve their objectives, and what measurements would be required to ensure transactions remain on track.

Ultimately, this results in a much more holistic and integrated approach to strategy development and implementation, which, in turn, significantly improves the probability of successful integration and the achievement of the organization's financial and strategic objectives. And by framing the discussion within the context of financial and strategic ambition, we are able to help develop a robust plan that fits the company's risk appetite, competitive landscape and future customer trends.

Seeking long-term growth

Every insurer is looking for the next big growth opportunity. And in today's slow-economic growth and low-interest rate environment, it is clear that inorganic growth (via mergers, acquisitions, partnerships and alliance transactions) will continue to be a critical component of any insurer's long-term growth strategy.

We believe that as the insurance sector increasingly plans and executes its deal activity using a strategy-driven transactions lens that focuses on identifying, evaluating and integrating potential acquisition targets, and innovative partnerships and alliances, — will only make the industry stronger. ■

> Insurers are reshaping their portfolio of businesses and assets, centers of operational excellence and markets to meet future growth opportunities.

Nine Levers of Value framework and questions to consider

1. **Financial outcomes, structuring, investment and capital allocation:** What are the 3- to 5-year financial and strategic objectives?

2. **Markets:** Does the current portfolio of businesses support the financial and strategic objectives?

3. **Propositions and brands:** How should the portfolio of propositions and brands be managed over time to deliver our financial and strategic objectives?

4. **Clients and channels:** What changes to the operating model can enable customer/channel performance?

5. **Core business processes:** What are our priority business processes to deliver the financial outcomes and a winning business model?

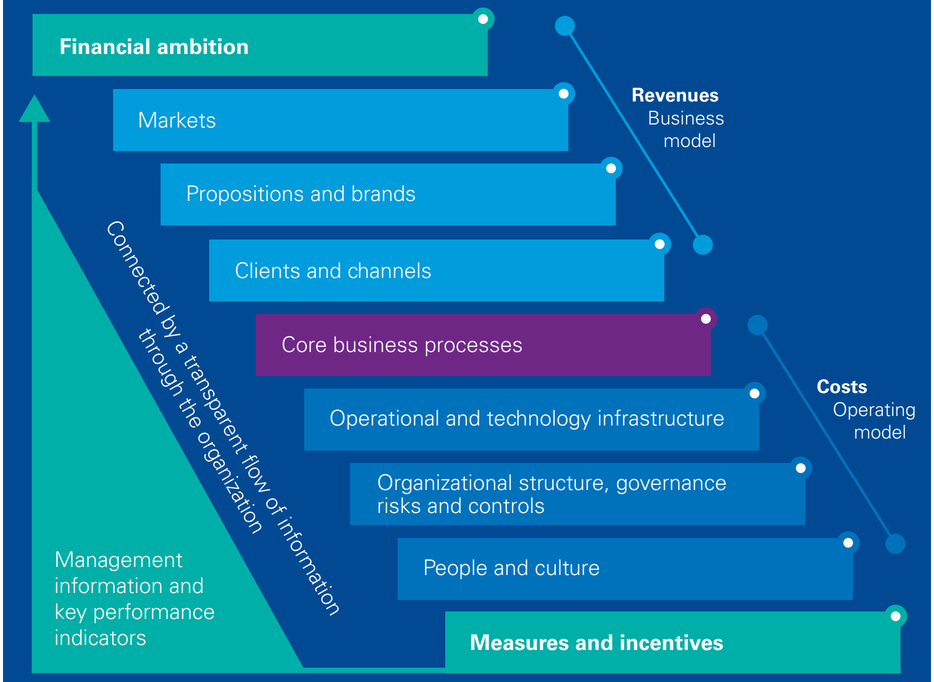
6. **Operational and technology infrastructure:** What are the priority infrastructure and technology elements that will be required to enable the strategy?

7. **Organizational structure, governance, risk and controls:** What does the organizational structure need to be to enable the strategy?

8. **People and culture:** What leadership is required to drive the transformational change, and what culture and behaviors are required as enablers?

9. **Measures and incentives:** What will you measure to monitor progress on strategy, identify issues and enable action where required?

The Nine Levers of Value methodology



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