The rise of risk aggregators

How can commercial insurance players turn disruption into competitive advantage?

Thriving on disruption series

As risk aggregators disrupt the small-to-medium-sized enterprises (SME) insurance market, insurers face some tough choices. Do they take on the aggregators at their own game with an efficient, platform-based offering? Or do they go for the premium customer, with sophisticated solutions based upon personal relationships, prevention and protection?

Paul Merrey
KPMG in the UK

Matthew Smith
KPMG in the UK

Albert Lee
KPMG in the UK

Global Strategy Group

KPMG International

The rise of risk aggregators

Aggregators are a significant disruptor to the small-to-medium-sized enterprise (SME) insurance market.

The evolution of aggregators from simple comparison engines to sophisticated platforms is likely to be the largest disruptive force in the SME insurance market. With growing functionality, expanding product coverage and a widening end customer base, we believe the rise of aggregators will result in:

— Traditional broking being less relevant in the commercial SME market

— SME primary carriers being forced to compete predominantly on price and bundled solution offerings.

The way in which commercial insurance products are sold has changed considerably — most notably in the SME segment. As products become simpler and more commoditized the need for advice is reducing. At the same time aggregators are evolving into sophisticated platforms and increasingly these will fill the space once ruled by brokers, triggering the withdrawal of traditional brokers from the SME market. More specifically, we need to think about the small ('S') and the medium ('M') of SME differently. In future, broker interactions will polarize between aggregator-led quotations at the 'S' end of the market, and high-touch, premium broker-led advice at the 'M' of end of the market.

In a market where risk aggregation is prevalent, price becomes the primary purchase criteria. This will in turn force carriers to compete on price or offer bundled solutions that meet the entire needs of the end customer. We anticipate premium rates to decline by up to 10 percent, with carriers increasingly needing to grow by taking market share.

A transformative shift

Aggregators have become integral to the way in which commercial insurance products are sold.

Today's aggregators are little more than just simple price comparison engines but integral to the way in which commercial insurance products are sold. This has changed considerably, most notably in the SME space, where online platforms facilitate the exchange of information between insurers and traditional broker intermediaries. The growing sophistication of these online platforms is increasing the depth and breadth of product coverage and widening the end customer base, and in the process, driving a transformation across the entire market.

Looking at the UK motor aggregator experience, three key lessons emerge with relevance for commercial lines:

— Firstly, aggregators exacerbate underlying structural changes in the market. To remain competitive, insurers need to be more nimble, not just in pricing but also in product development, in order to respond faster to any changes in the overall market

> **Example: The soft cycle experienced by the UK motor market in 2011 (post personal injury reform) was accelerated and extended by the singular focus on being cheaper**

— Secondly, insurers that focus on achieving a lean, low-cost operating model are better equipped to compete during a prolonged period of downward pressure on premiums

— Thirdly, insurers which develop 'value-add' elements to their proposition and engage in ongoing dialogue with their customers, are able to enhance brand loyalty and minimize 'churn' at the end of year one.

Familiarity with personal lines aggregators has set the tone for channel migration in commercial lines, as consumers are comfortable purchasing online. This trend is likely to be supported by concerted efforts from both aggregators and insurers to cross-sell into the commercial market in search of growth.

The rise of risk aggregators is therefore inevitable and likely to be the largest disruptive force in the SME market, but can be navigated if players are prepared to embrace this phenomenon and outmanoeuvre their competitors. But if this trend is ignored, brokers and carriers face increasing challenges, with the following potential consequences:

— Traditional broking will reduce as the 'S' end of the market may also lose relevance across the broader SME segment

— Primary carriers will need to compete predominantly on price and not service.

Traditional broking will be less relevant in the commercial SME market

Further simplification and commoditization of SME products is likely to vastly reduce the need for traditional broker advice.

Current service levels offered by brokers to SME customers are often transactional in nature, especially for smaller accounts typically handled by relatively inexperienced staff. In these cases, the role of the broker is essentially reduced to collecting quotes to present back as a bundled solution. As we've seen in the personal lines space, online aggregators can do this far more effectively.

Man versus machine

Given this dynamic, we foresee a future comprised of two vastly different types of intermediary interactions:

- Online portals aggregating quotes from a number of insurers, using a minimal question set, incorporating elements of simple advice to meet business-specific cover requirements. We expect this type of buying journey to make up the majority of SME insurance at the lower end of the market
- High-touch interactions, involving detailed advice and options from a broker. This would meet the demands of highly involved SME decision-makers, who either crave greater service (and are willing to pay for it), or have an emerging insurance risk that cannot yet be underwritten automatically. Such a high-end, service-orientated segment may always be present to some extent, but is only likely to make up a minority share.

The customer should be the ultimate beneficiary, thanks to falling premium rates on SME commercial package products, as commissions diminish in a market where the majority of transactions occur online (or are initiated online and completed via telephone). Any savings should be passed on directly to the customer in the form of reduced premiums.

Primary carriers will compete on price and bundled solution offerings

In a market where risk aggregation is prevalent, price becomes the primary consideration. Providing a bundled solution should also drive customer value.

Of course, providers still have to offer basic service levels, but claims service, for example, is traditionally seen as a 'hygiene' factor in a commoditized market. Experience in personal lines suggests that simply being price-competitive will not overcome a negative claims reputation. But equally, a strong claims image rarely justifies a higher premium. Regardless of their chosen strategy, insurers cannot be complacent about service levels, and should continue to invest in the customer experience.

Growth in a changing market

To date, the soft cycle has had less effect on premium rates in the SME segment, which has not been impacted to the same extent as some of the larger segments of the commercial market. But we believe aggregation will lead to greater price competition, causing a 5–10 percent fall in SME premiums by 2020. Insurers without sufficiently sharp or granular pricing could suffer a direct hit to bottom line profitability, reducing margins below required return hurdles.

When you factor in the aforementioned reduced commissions, then overall growth in the SME market will be challenging, increasing pressure on insurers to find growth through taking market share.

In a market where risk awareness is inherently low, providing a bundled solution which is simple, convenient and timely should positively drive the customer value proposition.

Why it's different this time

Facing the tipping point in the SME market

An aggregator dominant SME market is not a new concept. But we believe that a number of factors have broken down barriers to change and brought the commercial SME market to a tipping point. The biggest impact of aggregation will likely be felt in the 'S' of SME.

Barriers to change in the SME insurance market[1]		
Barrier	**Factor / Force**	**Result**
Bespoke underwriting of individual SME risk sections	Reducing complexity of bundled commercial package products, as covers standardize across the market	Tailored products for specific industries, made possible through building existing base covers with limit options
Nature of broker/ insurer relationships	Increasing use of platforms by both insurers and brokers	A form of quote aggregation already exists in the market (albeit performed manually by a broker) and is increasing in use and ease
Role of intermediary advice	Increasing amount of online resources that help educate customers	Potential reforms to distribution (like the UK's Retail Distribution Review (RDR) outcomes)
	Increasing need for price transparency	A number of major players are actively competing for growth in the SME market and are willing to participate
Reluctance of insurers to participate in platforms (from the UK motor experience)	SME markets generally more fragmented with no true dominant players	A number of major players are actively competing for growth in the SME market and are willing to participate
	Lack of commercial insurance brand recognition from historical absence of direct marketing investment	Insurer strength rating (rather than brand) is likely to be the key influence on the purchase decision

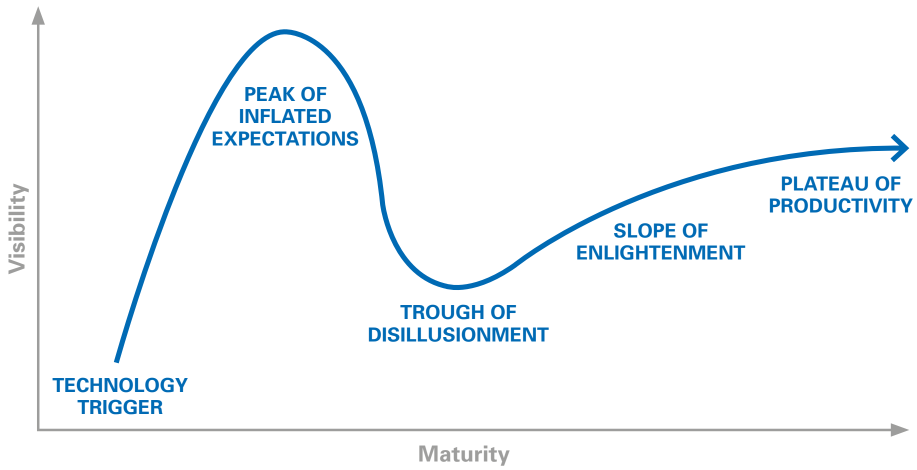
We believe the emergence of a number of Insurtech start-ups suggest the time may be ripe for change: These businesses cater for a wider, more complex customer base whilst also incorporating leading customer experience approaches.

These companies embody the underlying trends discussed in this paper, swiftly enabled and accelerated by technology. Some current examples of venture capital (VC)-funded start-ups already active in the market include:

- CoverWaller: digital first, omni-channel advice, quote and policy management platform
- Embroker: electronic broker platform with 100 percent online capabilty
- QuotePie: quote aggregation platform, using panel of local agents.

We are entering the much anticipated phase of greater adoption of SME insurance aggregator platforms. As hype is replaced by reality, risk aggregators are now being more widely accepted as their application and benefits are better understood.

To the right you will find Gartner Hype Cycle which "drills down into the five key phases of a technology's life cycle" including Technology Trigger, Peak of Inflated Expectations, Trough of Disillusionment, Slope of Enlightenment and Plateau of Productivity. From this KPMG has provided its own analysis based on the risk aggregator market.[2]



Technology Trigger	Peak of Inflated Expectations	Trough of Disillusionment	Slope of Enlightenment	Plateau of Productivity
2002 First personal lines aggregators enter market	**2005** SME insurance applications expected Simply Business (UK) launched	**2011** Commercial lines aggregator penetration remains low	**Today** Number of VC-backed start-ups entering commercial lines increasing	**Near Future** Majority of SME volume transacted directly through aggregator platforms

Implications for insurers and brokers

The changing SME landscape, brought on by the rise of aggregators, requires all players to take a radically different approach to this segment.

The role of intermediary advice is likely to diverge towards opposite ends of the spectrum.

At the low-cost end, the majority of transactions should be online without any human interaction, leading to greater commoditization. Price then becomes the key buying criteria, so primary carriers need to be confident in auto-rating most of the market.

Winners in this market should capitalize on first mover advantage by creating a 'low-cost, customer-friendly, scalable platform'; capturing the benefits of an improved operating margin before prices drop.

At the opposite end of the spectrum, we see brokers adopting a more premium advice solution, entailing greater levels of service generally reserved for more 'corporate'-type accounts.

Winners in this market should be able to differentiate their service levels by developing clear, 'value-added' features for their clients such as dedicated relationships, comprehensive risk reviews covering prevention and protection options, as well as integrated solutions to crisis response. These advances should help them command higher premiums and associated commissions, and potentially, gain alternative sources of revenue.

Given the inevitability of aggregation, traditional brokers should be decisive in both strategy and execution, to successfully navigate and win in the SME market:

1. Decide whether to play in the premium SME advice space, and invest in up-skilling staff as required
2. Create a digital direct proposition, by providing an online aggregated service that enables customers to compare bundled products, supported by a broader omni-channel experience
3. Consider build, buy, rent or collaborate options to access these opportunities and gain first mover advantage, without risking the primary brand
4. Consider incorporating auto-advice elements (similar to those seen in funds management, where robo-advice is emerging).

Turning disruption into competitive advantage: a strategic response

To maximize the changes of sustainable success, it is vital to answer a range of strategic questions, and to align your business and operating model with your chosen strategy.

Risk aggregation will force primary risk carriers to compete on either price, or through bundled solutions that meets a range of client needs. With premium rates expected to reduce by 5–10 percent by 2020, the need to grow market share should intensify. In this environment, winning businesses could adopt a number of strategic responses:

1. Building and enhancing their online direct SME proposition for direct marketing, whilst ensuring they have the capability to plug in to other online platforms
2. Improving their auto-quote capability, to provide coverage across all industries/ occupations and minimize manual referrals
3. Remaining price-competitive on preferred risks in order to win business on major quote platforms, such as the online exchanges emerging from industry investment in technology partnerships
4. Optimizing modular pricing options by offering additional relevant sections or 'add-ons,' to capture the greatest premium from the customer, in a pure online and omni-channel manner
5. Maximizing positive user experience of aggregators, to increase renewal rates
6. Minimizing costs associated with servicing SME business, to soften the impact of the 'winner's curse' in a price-competitive market with thin margins
7. Establishing robust fraud mitigation capabilities, to ensure customer familiarity.

Four thoughts to take away

Ultimately, anyone seeking to triumph in the SME market needs to answer four key questions as part of their strategy development:

1. What will we be famous for?
2. What role do we want to play in our clients' lives?
3. Where will we play?
4. How will we win?

Sourcing & notes

1. KPMG analysis based on a range of market sources and market participant interviews.

2. Gartner Methodologies, Gartner Hype Cycle, http://www.gartner.com/technology/research/methodologies/hype-cycle.jsp

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Contacts

Paul Merrey
Partner
Global Strategy Group
KPMG in the UK
E: paul.merrey@kpmg.co.uk
T: +44 (0)20 7694 5276

Matthew Smith
Director
Global Strategy Group
KPMG in the UK
E: matthewg.smith@kpmg.co.uk
T: +44 (0)20 7694 3060

Albert Lee
Associate
Global Strategy Group
KPMG in the UK
E: albert.lee@kpmg.co.uk
T: +44 (0)20 7694 5635

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