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Why Digital Transformation In Insurance Does Not Have To Be Disruptive

Christoph Tatje

Managers across industries see digital transformation as a major challenge that calls everything into question. They must 1) rethink and change their business model, 2) migrate from physical to digital channels, 3) buy and integrate startups, 4) understand new and emerging technologies, and 5) get rid of legacy systems immediately. This perception of a digital transformation can overwhelm even the best manager. As a result, managers are reluctant to start the digital transformation journey. Instead of creating a clear vision and strategy for the future, many managers react to trends in technology and what their competitors are doing. This mostly leads to additional frustration and creates a vicious circle.

In an article published in the Harvard Business Manager, Nathan Furr and Andrew Shipilov disprove five common myths about digital transformation and explain what digital transformation is really about. Their findings show that digital transformation does not have to be disruptive at all. Digital transformation is about meeting customer needs by taking advantage of new technology, which can be integrated step by step. Managers can gain back control and create a strategy that gives their company a competitive edge.

Let's apply Furr's and Shipilov's findings to the five most common myths about digital transformation in the insurance industry to illustrate how insurance managers can develop a digital transformation strategy and gain competitive advantage.

Myth #1: We must rethink and change our business model.

Reality: Use digital tools to meet customer needs better.

The insurance business model works like this: Individual risk is transferred to a collective, in which the insurer is the intermediary that collects premiums, manages the policies and pays in case of a loss. Overall, this business model will remain the same – despite ongoing digitization.

But there is more to it. New technologies are offering new ways for insurance companies to manage their customers' needs. This means insurers must continually ask themselves whether their current mode of operations meets customer expectations. For example, if a customer is expecting to pay out after loss within a couple of days, insurers must ensure they are accomplishing this with their current claims processes. If not, they must evaluate their process for ways to optimize and automate.

Implementing a new technology just because it's available is the wrong approach. Insurers must ask whether a new technology can help meet customer needs or add value to the customer experience. If not, new technology should not be implemented. A good example is blockchain technology. In the past, insurers tried to come up with new processes and products based on blockchain that were not successful because customers did not see additional value. Insurers must find the customer value first and then the technology to support it.

Myth #2: We must change from physical to digital channels.

Reality: Physical and digital channels will coexist.

The insurance business has always been a people business. For a long time, insurers did not have direct contact with their customers. Agents and brokers were used as intermediaries, and these roles still conduct a lot of client interaction, which means insurers have very limited knowledge about their customers. Today, insurers are becoming aware that they need to know their customers more holistically to be able to meet their expectations. They're investing heavily in the digital customer journey, chatbots and digital products that help them gather the relevant data and stay in direct touch with customers.

Physical and digital channels are effectively separated. The key to success lies is completely integrating of physical and digital channels to give customers omnichannel 24/7 access – no matter if they started their journey online or with a broker. Insurers have to clean up their product portfolios, find ways to integrate agent and broker platforms in their omnichannel plan and take advantage of customer data.

Myth #3: We must buy and integrate startups.

Reality: Take advantage of startups as partners that can create innovations without immediately integrating them.

Insurance companies are facing increasing competition from InsurTechs that leverage technology to offer a better customer experience for at least parts of the insurer's value chain, such as digital online applications. Though many large insurers have opted to buy out startups and integrate them into their existing value chains, some have found different cultures are hard to combine and can lead to friction over the long run. An insurer should be wary of integrating a newly acquired startup and give it autonomy by providing enough capital to foster innovation for additional value. The relationship between an InsurTech and a traditional insurer has to be tight enough to allow the parent company to learn from the founders and get synergies out of the collaboration while allowing the startup to retain its own culture.

The German insurer Allianz, for example, made a strategic investment in the startup Lemonade that is using artificial intelligence (AI) to offer a unique customer experience and individualized products. Allianz's doesn't currently intend to integrate Lemonade into its value chain but is exploring synergies and ways of collaborating in the future.

Myth #4: Digitalization is all about technology.

Reality: Digitalization is all about the customer.

A common misunderstanding of digital transformation is the focus on technology and on how it will have an impact on the future. But digital transformation is much more than just technology. It is also about customer centricity, so then insurer can understand its customers and provide customized products and experiences that keep them around. Technology like AI will support this approach, but there also has to be a change in mindset for the insurers' employees. They need to understand that "the customer is king" and that it is their job to make them happy – a concept that may be new to some who are used to bureaucratic structures at some large insurance companies.

Many insurance companies understand this new imperative and are positioning themselves as "life-time partners" to their customers, providing "tailor-made products and services" to meet their clients' needs.

Myth #5: We have to get rid of all our legacy systems immediately.

Reality: Modernize step by step as needed.

Digital transformation leads to new requirements for backend systems, which is a challenge for insurance companies that have had their systems in place for decades. An immediate overhaul of existing legacy systems might introduce too much risk and cost. Instead, insurers need to come up with new front-end applications that meet customer expectations and replace underlying legacy systems step by step in an agile way. In the meantime, the new front-end applications can be connected to the legacy systems through middleware interfaces (APIs). Alternatively, individual business units could come up with new front-end and backend solutions that reflect the ideal customer journey and are independent from the legacy systems but run in parallel until the legacy systems are decommissioned.

Industrial insurer HDI successfully implemented a middleware interface which relied on its backend system for ongoing operations. The company needed the front-end solutions to respond flexibly to the client and ensure security of processes and customer data. It implemented a "front-end layer" that allowed it to decouple the user interface from the rest of the IT infrastructure. Now, the tariff-relevant data from HDI's existing IT systems is passed on to the application via a separate communication layer with precisely matching interfaces.

Digital transformation for the insurance industry does not have to be disruptive. New technologies lead to major changes. But change has always been a part of the industry – and insurers and their core business model have always survived. Managers in the insurance industry should think of digital transformation less as a threat and more as an opportunity to grow.

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CHRISTOPH TATJE

Christoph Tatje successfully consults and supports his customers in various transactions as well as in transition and transformation projects in different business areas of the insurance industry (e.g. healthcare, casualty) as a project manager. His customers benefit on the one hand from his wide project management expertise and on the other hand on his broad expertise in the insurance sector. Furthermore, he has a profound technical and processual understanding.

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