RESET4VALUE

Four Acts of Unconventional Leadership for insurers to reset value and transform their organization

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EXECUTIVE SUMMARY

COVID-19 has created massive upheaval but also unique opportunities to maximize value and refocus the growth trajectory in insurance.

The crisis has, in many respects, made resetting your business for fast value creation more achievable than it was pre-crisis. Unmet customer needs are clearer, capabilities are easier to build and/or acquire, remote working has required stronger operational resilience, and flatter organizational models have evolved to enhance faster, more collaborative, remote decision-making.

While the environment will remain challenging as the pandemic peters out, economic uncertainty also remains high. Leaders will remain pressured to deal with the twin challenges of sharp, ongoing cost and consolidation pressures, and a need to find new sources of profitable growth against the disruptive headwinds caused by lower for longer interest rates and emerging Insurtech. The key is to keep calm and **RESET4Value.**

How can your business best leverage disruption to drive new opportunities? We prescribe four actions to accelerate value creation and come out of the crisis stronger and leaner than before. In this perspective, we propose a new approach to resolving today's cost and growth challenges, and showcase examples of recent client successes. Using our **RESET4Value** approach, benefits typically emerge as early as six weeks.

For those thinking, *"I've tried multiple cost transformation efforts before, and have rarely achieved sustainable results,"* our view is that it's not that cost programs are unproductive, but rather that the traditional mindset is flawed.

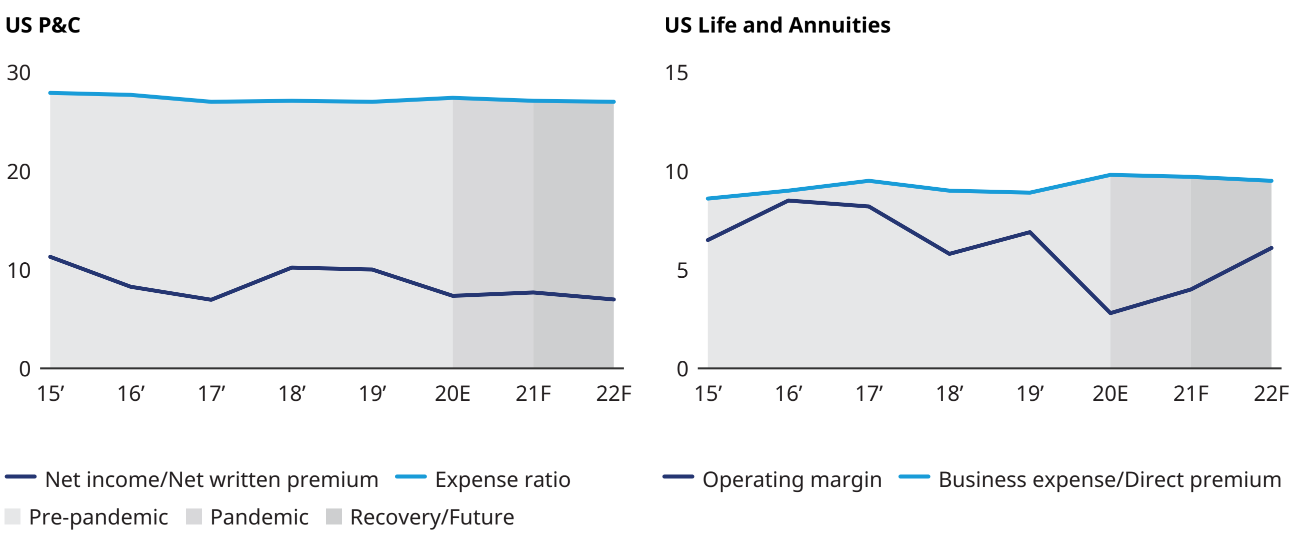
There is a mindset shift that is required for teams today. We feel that "Unconventional times require an Unconventional mindset," and what follows are **"Four Acts of Unconventional Leadership"** to help your organization manage costs while fueling business growth.

PROVOCATION: COVID-19 HAS CHANGED INSURANCE

The pandemic catapulted the insurance industry into massive and unexpected disruption across almost all elements of operations. Leadership teams have battled through multiple waves of unforgiving challenges — massive economic instability, record-breaking natural catastrophes, and unprecedented shifts to remote working styles to name a few. Premium growth stalled, net incomes were significantly hit, and even allowing for recovery, businesses will remain challenged in 2021.

Exhibit 1: Property & Casualty (P&C) vs. Life & Annuity (L&A) sectors

In %



Sources: Conning Insurance Research (1) Conning's quarterly Property-Casualty Forecast & Analysis by Line of Insurance Highlights, Fourth Quarter 2020; (2) Conning's Life-Annuity Forecast & Analysis By Line of Business Year-End 2020 Forecast for 2020-2022; and (3) Conning's 2021 U.S. Insurance Industry Outlook, February 2021.

Looking forward, traditional growth paths will be harder, margins will continue to be pressured, and disruption will continue.

In 2020, generating income from traditional businesses was difficult. While recovery is occurring, profitability will remain challenged in 2021 as interest rates remain low, losses remain elevated, and expenses stay close to pre-pandemic levels.

Exhibit 2: Four forces impacting the insurance industry

Four main factors compounded to drive industry outcomes — the rapid shift to remote working, elevated risks, lower interest rates and sharply higher unemployment.

1. Pandemic disruption

First, working from home quickly became the new normal. For an industry that relies on building strong customer relationships as a critical component for success, the lack of face-to-face interaction created complex sales barriers (especially for new sales) and strained revenue generation.

What's next: The impact on both the wholesale and agent distribution processes has forced insurers to rethink strategy and ramp up digitization efforts in both the near and long-term.

2. Higher risks lowering profitability

Second, as insurers took on higher risks their main revenue drivers, consisting of underwriting profitability and investment returns, were increasingly impacted.

What's next: The COVID-19 pandemic and the record-breaking number of 2020 natural catastrophes were a wakeup call for the insurance industry. The more firms can do with new digitization capabilities, distribution channels and a simplified operating model — the more resilient their business will be for future disruption.

3. Ultra-low interest rates impacting investment returns

Third, for life insurers, the collapse in interest rates had a much greater impact on the business than the overall pandemic. This forced insurers to venture from safer, traditional fixed income assets (buy and hold) to risker assets classes.

What's next: Insurers will need to add new capabilities to appropriately invest in new asset classes, while resetting their cost and expenses.

4. Spike in unemployment increased policy lapse frequency

Fourth, the lapse frequency for insurance policies increased as many individual holders faced job losses, furloughs or reductions in salary last year. Group life insurance was the hardest impacted.

What's next: Insurers may need to consider new lines of capabilities, such as supplemental insurance.

Source: Oliver Wyman analysis

Insurers need to reset fast to prevent client value from eroding and ensure near-term financial constraints do not compound into more serious long term threats.

OPPORTUNITY

WHY NOW IS THE TIME TO RESET CUSTOMER VALUE

The good news is that creating long-term value is more achievable now than ever, due to a once-in-a-generation chance to accelerate change. The issues stated above are well understood; what's difficult is modulating the response. The natural reaction for executives is to launch cost-cutting efforts, but our view is that traditional cost transformations are fraught with challenges and often will not generate sustainable results. The answer must be to treat costs as investments to accelerate growth around a clear business narrative and to reinforce this through an intuitive execution framework.

WHY COST TRANSFORMATION EFFORTS FAIL

It's easy to achieve short-term success when reducing costs. However, most cost transformation attempts ultimately fail because they adopt a conventional mindset — asking teams to do more with less, while lacking the visibility and motivation into how this savings will be used to 'fund the future' (see Exhibit 3 below). This conventional approach puts the business into an unsustainable cycle. As a result, after removing the biggest pockets of expenses and returning to business-as-usual, managers see costs creep back in and need to start again.

Without a clear plan, leaders tend to:

- Manage to their existing business portfolio and internal profitability, instead of considering client needs as the first priority.
- Label costs as 'bad' and starve key capabilities necessary for growth, while overinvesting in other capabilities.
- Organize and reorganize to focus on reporting lines and eliminate cost.

The key to a successful cost transformation is to make the program sustainable. It's not enough to make this process a one-time effort or to only reduce the largest expenses of the business. Leaders should use cost exercises as opportunities to increase growth ambitions and drive new value and service quality for clients.

Exhibit 3: Seven key challenges of cost transformation

	Key challenges	Warning signs	Typical fallout
1	**Asks teams to do more with less; does not address complexity drivers**	• Avoids participation choices (for example, products, markets)	• Encourages pausing vs. stopping • Backfilling erodes save over time
2	**No clear blueprint for change; does not address target operating model**	• Minimal change in CEO+1 roles, responsibilities	• Lots of staff pushback • Loss of leadership credibility
3	**Unclear mechanism for cross-P&L savings and reinvestment**	• Accountability set primarily through top-down targets	• Rely on interim control tower and off-ramp legit governance
4	**Focuses only on P&L impacts vs. speed, quality**	• Resulting client benefits unclear or intangible	• Erodes client value, putting further pressure on margins
5	**Does not embed sustainable process for continual savings/ reinvestment**	• More than one firmwide cost reduction exercise in last three years	• Employee cost burnout • Leadership keeping score
6	**Lacks visibility into details of the real opportunities**	• Relies heavily on benchmarks • Does not address partial full-time employees	• Ditch plans and resorts to finding savings anywhere
7	**Takes focus, time and attention away from growth**	• Uses of reinvestment unclear • Turnover of top performers	• Slows commercialization and innovation, pressuring growth

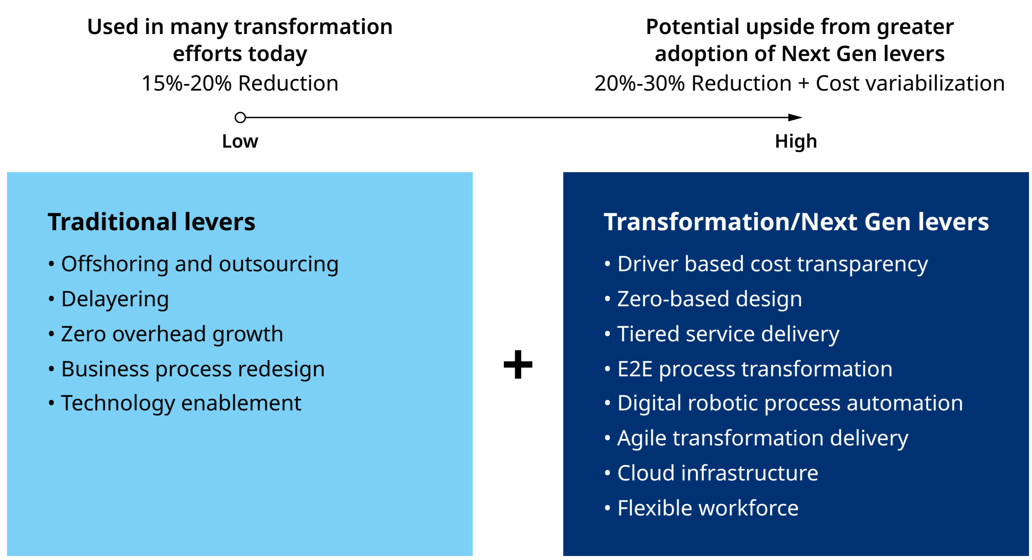
Source: Oliver Wyman analysis

Executives should consider their businesses' strengths and the value they deliver — for example, premier customer or advisor service, radical convenience, transparency and speed of execution.

In our work with insurance leaders, we observed that most have come close to exhausting traditional cost levers such as outsourcing, business process redesign, digitization, etc. (see Exhibit 4), while selectively choosing next generation levers such as cloud infrastructures, robotic process automation, etc., but not necessarily changing how they work. Disruption has accelerated the need for some of these levers. Far reaching business goals and long-standing "nice-to-haves" are now priorities. For example, COVID-19 has shown that it's essential to have digital and contactless client experiences. Customers want options for dynamic coverage that adjusts over their lifetime; solutions that are socially responsible and meet Environmental, Social, and Corporate Governance (ESG) efforts; and they are looking for improved customer experiences to process claims or buy supplemental insurance coverage.

In our view, leaders who want to get to significant, sustainable cost reductions must pull both traditional and next generation levers at the same time and change how things really get done. Adopting next generation levers improves the success of cost reductions by 20 to 30 percent, transforming fixed costs into variable costs that can move with the firm's incremental revenue and growth opportunities.

Exhibit 4: Insurance leaders need to pull both "Traditional" and "Next Gen" levers at the same time



Source: Oliver Wyman analysis

It's easy to say and hard to do, of course, which is why we've developed an approach through our work with executive teams which we call **"Four Acts of Unconventional Leadership."**

RESET4VALUE

FOUR ACTS OF UNCONVENTIONAL LEADERSHIP

In our view, "Unconventional times require an unconventional mindset." *So, what does this mean?* With ongoing COVID-19 disruption, performing one-time cost-cutting initiatives is destined to be difficult and will ultimately hurt the future profitability of your business. Rather than performing a one-time slash of expenses (that often trickles back in), leaders need to change their mindset and view cost programs as a way to fuel growth.

Exhibit 5: Four Acts of Unconventional Leadership

We believe companies must:

1. **Re-envision how you create client value**

   Anchor on the client: Get specific how client value is delivered and use as a key lever to drive execution

2. **Segment capabilities based on value creation**

   Focus on making hard trade-off decisions: Be clear what the firm can and needs to do best

3. **Link your cost, growth, investment agendas**

   Treat costs as investments: Prune what doesn't matter to invest more in what clients value

4. **Change how the work gets done**

   Leverage cultural strengths: Builds on and enhances business-as-usual behaviors across all op model levers

Source: Oliver Wyman analysis

Unconventional times require an unconventional mindset.

ACT 1: RE-ENVISION HOW YOU CREATE VALUE

Start with customer value and focus on future growth

Cost cutting alone will not solve all the challenges. Leadership teams need to have a holistic transformative mindset, starting with consensus on what customers' need and value and use this to prioritize growth initiatives. Top-line growth is a key driver of sustainable earnings expansion and reduces the need for and negative effects of perpetual cost-cutting.

Resetting customer value

Leaders should be very clear and specific when considering, *"Why are clients coming to us?"* Are clients coming for first-rate customer service or the convenience of our experience? Do they want higher premiums for greater coverage or a lower risk profile? And this exercise is not to select your most profitable product or service. Value drivers may be different depending on the segment or offering and should be defined specifically for each, bringing in the voice of the customer. The key here is to consider, *"What do my clients value?"* and *"What value can my business provide to them?"*

Exhibit 6: Customer value considerations

What do customers value?

For example, consider:

- Higher coverage vs. lower expenses?
- Speed/convenience vs. individual customization?
- Policy features vs. service?

What are the unmet needs?

For example, consider:

- Risk prevention vs. simple risk coverage
- Demand for dynamic coverage (for example, adjusts over lifetime)
- Heightened attention on health/safety/ESG

What are they willing to pay for?

For example, consider:

- Higher premiums for greater coverage; lower risk minimums
- Services expected to be given away (for example, democratized advice)

Source: Oliver Wyman analysis

Driving growth

After getting specific on the value you are delivering to clients, use this as an opportunity to accelerate growth and consider which capabilities to invest more or less in. Look beyond where you have traditionally played and consider the specific value customers are expecting from both traditional and non-traditional competitors, as well as the unmet customer needs not yet fulfilled by players in your market. This will allow you to choose capabilities that truly differentiate and are unique, while reducing spend on capabilities that matter less to customers.

Results: For example, on a recent project, we worked with an insurer looking to support the next wave of growth in their business. The company had driven significant financial performance gains immediately before the crisis but was now struggling to find new areas of opportunity, and 2020 became more challenging as expense growth outpaced revenues.

Our team identified specific drivers of customer value, such as “service” versus “policy features,” that aligned with their current business capabilities. This helped the management team to develop a view across their siloed businesses and products. The analysis also quickly identified an alternative operating model and governance structure designed around customer needs and the capabilities needed to meet them. The management team was able to quickly execute a future-and growth-focused transformation program.

The required cost transformation effort became evident, and the combined growth-cost program quickly became self-funding.

Overall, we helped transform the client’s business, improving cost structure by 25 to 30 percent of base but also, more fundamentally, drive a scalable, modern infrastructure and customer interface — with digital-first process excellence and automation.

ACT 2: SEGMENT COSTS AND ALIGN TO CUSTOMER VALUE

Use the Four Zone approach to make hard trade-off decisions

Leadership teams often get trapped on a treadmill, chasing multiple opportunities and investment initiatives without a clear ‘right to win.’ The twin cost-growth challenges we now face require that this problem be addressed directly. Executives must ask themselves: *What does my business do best? Are our products and services addressing the most urgent needs of my clients? Am I efficiently allocating resources across a portfolio of today’s businesses and bets that will drive me into the future in 3 to 5 to 10 years’ time?*

Act 2 of the approach allows leaders to build on re-envisioning customer value from Act 1. Here we segment and align costs and investments across four zones: Performance, Efficiency, Incubation and Activation. This allows you as a leader and your team to systematically reallocate resources to areas that will drive future growth, extracting from low-growth businesses and non-strategic programs.

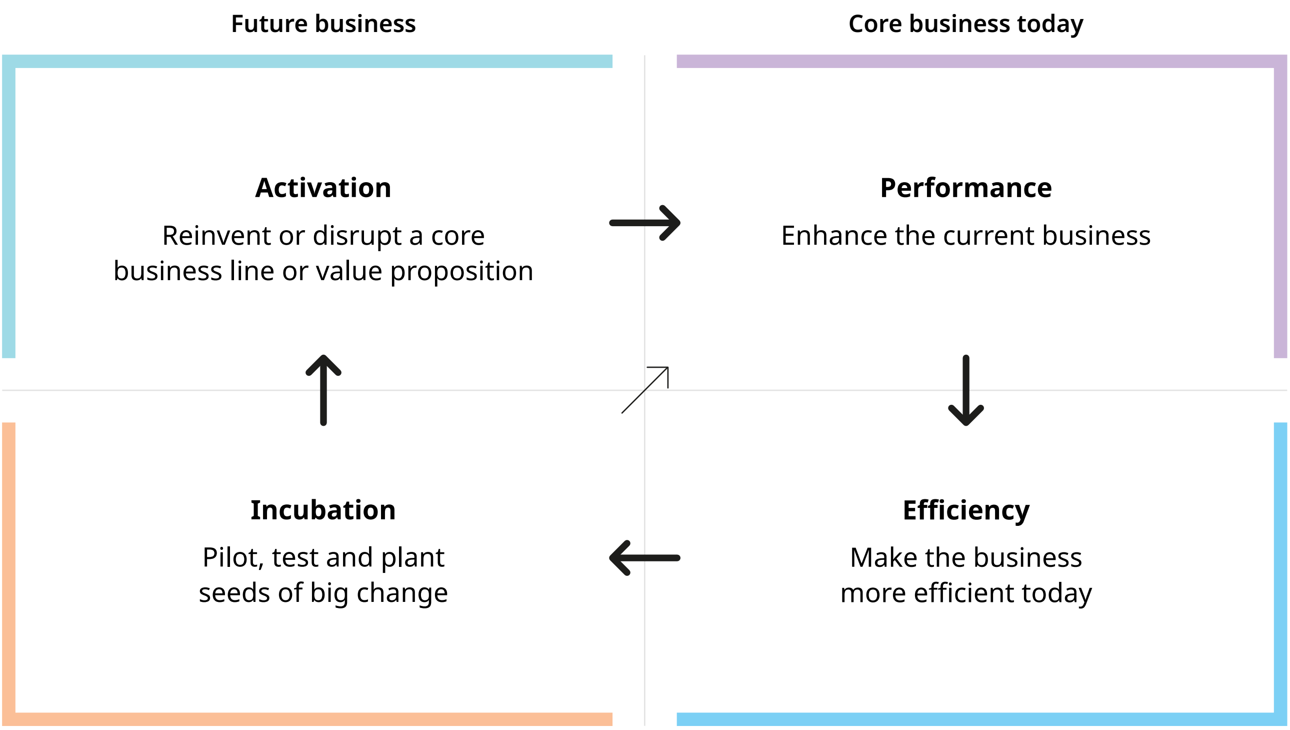
By deliberately segmenting businesses and capabilities into value creation zones you can:

- Force discussions on which capabilities drive growth the most.
- Consider how every function, front-to-back, ties to each capability; and based on this, helps decide where to invest less AND more.
- Effectively communicate to your full organization how process frees up capacity, resources and increases speed.

The Four Zone model systematically enables focus and hard trade-off discussions. Oliver Wyman collaborated with Geoffrey A. Moore, author of *Zone to Win* to develop the Four Zone model. Leaders can synthesize the business portfolio and ensure that they are spending the appropriate amount of time, money, resources and attention to the right areas and priorities. As new lines of business and capabilities are piloted, integrated and scaled, careful attention is paid to moving between zones and managing on an ongoing basis (see Exhibit 7 below).

Exhibit 7: Four Zone approach

Generate long-term value creation for your business



Source: Oliver Wyman analysis

It's important to understand that this is an active, ongoing, cyclical process. Business capabilities and portfolio activities move through the zones over time. Each organization continually decides where to reallocate or invest more or less.

Exhibit 8: Moving between the Four Zones

Activation | **Performance**

4

From Incubation to Activation Zone followed by Activation to Performance Zone

Today's innovations will become tomorrow's legacy businesses. Through the process of continual piloting and incubating bets, businesses can scale capabilities to maturity.

1

From Performance to Efficiency Zone

Move capabilities in the performance zone that need to be managed more efficiently. For example, capabilities that are undifferentiated or not adding value.

3

From Performance to Incubation Zone

Take the business's core capabilities and form new ideas to pursue growth opportunities based on those capabilities.

2

From Efficiency to Incubation Zone

Any financial savings you received from managing the capability more efficiently can be put into the incubation zone to help the business pilot new products or services and invest in new growth opportunities.

Incubation | **Efficiency**

Source: Oliver Wyman analysis

For example, a few years ago an insurer pioneered a car tracking sensor or telematics device. The device allowed customers to receive discounts on their premiums for positive driving performance (speed, mileage, braking). This product and service savings became attractive in the industry, and today many auto insurance companies now offer this to their customers. This was initially piloted because of strong customer demand and has now become a core offering for auto insurers.

It is imperative that capabilities placed in the Incubation or Activation zone must be linked to their existing capabilities system. These cannot be unrelated capabilities.

Exhibit 9: Where do insurance capabilities fit across the Four Zones?

Activation

How to identify capabilities in this zone:
- Do the products, services or business lines have 4 to 6 quarters of meaningful contribution (5-10 percent) of revenue?
- Does growth from these areas match or exceed the high market growth rate?
- …

How to manage capabilities in this zone:
Test your way to 'right' and scale a disruptive option to materiality
- Minimum viable product (MVP) possible outside of existing businesses
- Capabilities being managed to maximize value within 3 years
- …

Performance

How to identify capabilities in this zone:
- Does the capability enable a high proportion (25%+) of today's revenue?
- Is the capability still growing or evolving, but from a starting point?
- …

How to manage capabilities in this zone:
Focus on differentiated capabilities to deliver revenue and margin commitments
- The capability is a primary focus of the senior operating team
- The capability emphasis is on steady management (do no harm), and you are able to focus on few fit-for-purpose execution metrics
- …

Incubation

How to identify capabilities in this zone:
- Is your business's portfolio of targeted growth bets aligned to differentiated capabilities with the potential to be the next big thing?
- Is the capability in a high-growth market, but yet to scale and prove whether it can contribute meaningfully (5-10%) of firm revenue?
- …

How to manage capabilities in this zone:
Accelerate and de-risk
- Use specialized teams to quickly develop innovations (for example, STEAM talent)
- Drive sustaining innovation with clear thresholds for reinvestment to scale or reallocate to the other bets
- …

Efficiency

How to identify capabilities in this zone:
- Is the capability not differentiated or adding value to the business?
- Is the capability slowing or stagnating top-line growth?
- …

How to manage capabilities in this zone:
Optimize for efficiency, effectiveness, and sustainability to fund investments for the future growth
- The business extract resources are from non-differentiated or value-creation work
- The capability can be reinvested in other zones or improve the bottom-line
- …

Source: Oliver Wyman analysis

ACT 3: LINK YOUR COST, GROWTH, INVESTMENT AGENDAS

Force the discussion on where to invest less and fund the future

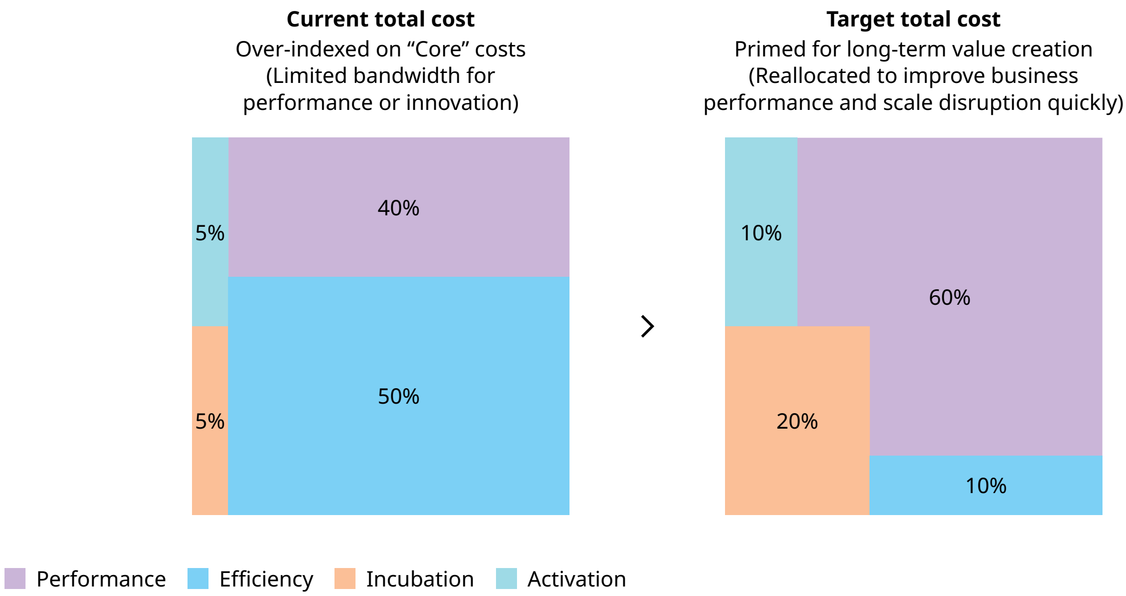
With uncertainty and disruption, the natural reaction for many leaders is to drive efficiency by reducing the largest costs. However, this does not prime the organization for long-term growth and ultimately leads to disadvantage.

We believe in powering your business for sustainable growth. The third act links cost, growth and the investment agenda. Following this approach, leaders treat costs as investments — ruthlessly trimming offerings that are non-differentiating and investing more in what creates value. Margins are sustainably managed while proactively managing reinvestment to enable growth. Resources and money can be quickly and flexibly reallocated to improve business performance and scale disruption.

Act 3 also creates capacity for a portfolio of smaller, more focused bets to pilot, test or fund new ideas (Incubation Zone). This also sets up the business with a robust investor narrative on future trajectory with demonstrable, credible proof points based on innovation zone outcomes.

Exhibit 10 provides a visual illustration on reconfiguring cost reduction within your portfolio (displayed on the left) to invest more in what client's value and power future growth (shown on the right).

Exhibit 10: Typical approach vs. powering your business for sustainable growth
'4-Zones' to cost reduction and reinvestment



Advantages
Why it makes a difference:
• Brings transparency to opportunities by segmenting costs into four zones
• Connects cost to growth and investments, from front-line to back-office
• Protects costs that drive growth and where to invest
• Challenges temptation to continue spending on legacy commitments

Source: Oliver Wyman analysis

On the left side above, we see the typical approach used by businesses today, with 80 to 90 percent of resources used for fixed core costs to run the business, and 10 to 20 percent of the expenses focused on growth and innovation (for example costs are distributed into 50% efficiency, 40% performance, 5% incubation, and 5% activation).

Our Four Zone model is shown on the right side, where the business radically trims costs (in the efficiency zone) that are non-differentiating or do not add value to the business. Here, the business is primed for value creation. The business protects their capabilities and expenses that drive growth in the performance and disruption zones, with 70 percent of the resources focused on fixed core costs and 30 percent of the expenses are used to innovate, experiment and drive new growth (for example costs are distributed into 10% efficiency, 60% performance, 20% incubation, and 10% activation).

Results: We recently worked with the CEO of an insurance holding company to link their cost, growth and investment agenda. Using the Four Zone framework, we quickly realigned cost structure and trimmed non-differentiating offerings to match the relevant performance zone. We helped the business adopt both traditional and next gen levers and successfully unlocked 20 to 30 percent in savings. This savings was then reallocated across a portfolio of 10 organic and inorganic growth 'bets' facilitating a robust board and investor narrative.

ACT 4: CHANGE THE BUSINESS CULTURE AND BEHAVIORS

Change how the work gets done

Act four is the key ingredient to successful cost transformation — culture and organizational behavior. Leaders can spend resources on the most innovative, expensive technology, but if they do not retool their workforce or change how the work is performed, they will not generate the returns originally envisioned.

Success is powered and driven by the entire organization. Empower your employees to drive change in their everyday jobs. Listen to your team, allow them to make decisions and be a part of the transformation. When needed, retool their skill sets and enhance work-life balance to make your organization an attractive place to work.

Reimagine how business activities get done through launching new digitization efforts and using greater speed and data quality to manage P&L accountability. Consider moving to a flatter organizational model, with fewer layers, to enhance collaborative decision making, accountability and the ability to tap into employee talents.

Overall, leaders need to embed elasticity or operating leverage into their organization. For example, keep resources flowing to "good" costs, such as taking on new customers or adding new services, and away from activities that do not add value. This allows the business to handle future growth in a more profitable and sustainable way. Below our operating model ecosystem illustrates the various business considerations.

Exhibit 11: Traditional levers/Next Gen levers plus operating model ecosystem

Our 'operating model ecosystem' approach to change how work gets done

Traditional levers

- Offshoring and outsourcing
- Delayering
- Zero overhead growth
- Business process redesign
- Technology enablement

+

Transformation/ Next Gen levers

- Driver based cost transparency
- Zero-based design
- Tiered service delivery
- E2E process transformation
- Digital robotic process automation
- Agile transformation delivery
- Cloud infrastructure
- Flexible workforce

+

Operating model ecosystem (OPEC)

Organization & talent
- Flattened organization
- Shared functions
- Balanced workload

Governance & accountability
- Clear decision rights
- More collaboration

Culture
- Constructive behaviors
- Agreed cultural norms

Sourcing & location
- Efficient office
- Negotiated rates
- Metered vendor usage

Processes & controls
- Digital authentication
- Automated underwriting
- Self-service claims

Technology & data
- Tech debt free architecture
- Single view of clients

Source: Oliver Wyman analysis

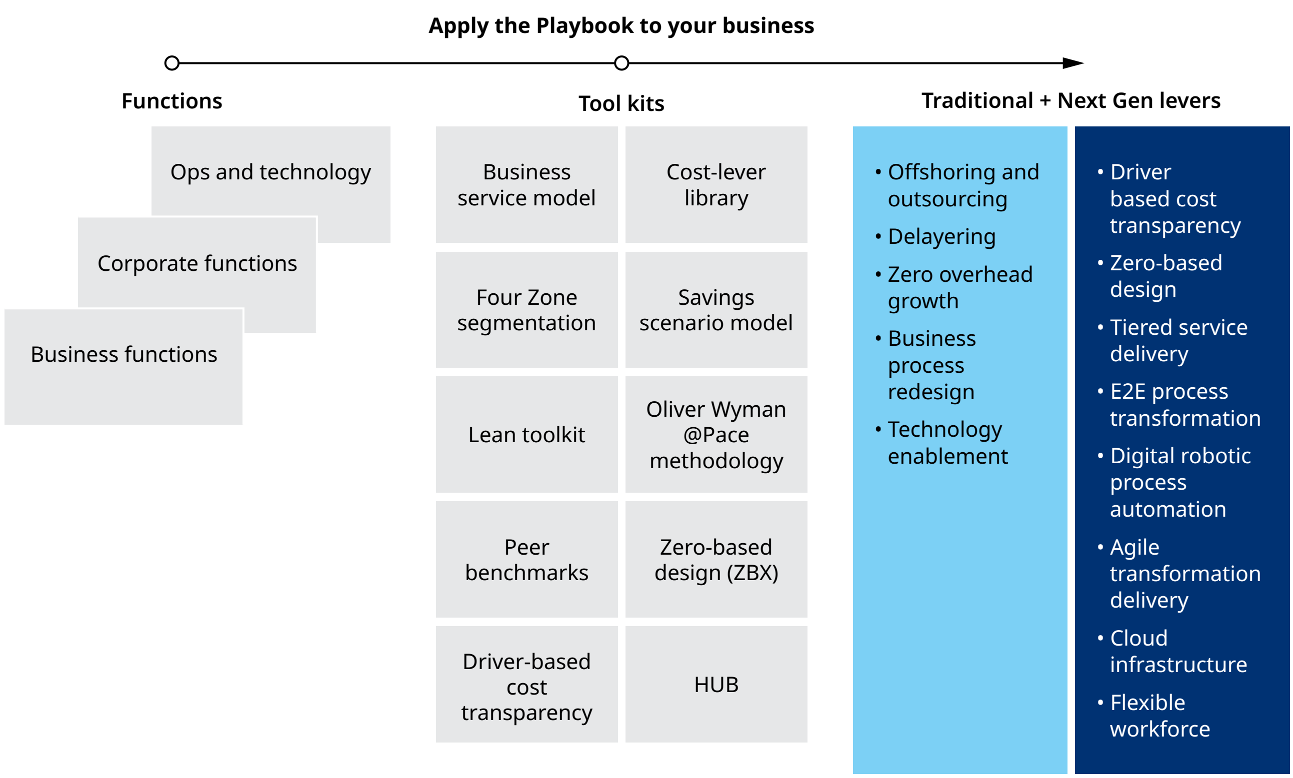
GET STARTED WITH OUR PLAYBOOK

Successful cost leadership in this new normal is possible and attainable. Using the "Four Acts of Unconventional Leadership," we have worked with multiple CEOs and their leadership teams to come out of this crisis stronger and poise their business for accelerated growth.

At Oliver Wyman, we can help your business achieve the same. Whether your organization wants to lower operating costs or uplift revenues, we can support you with making the right types of decisions to thrive today and in the post-COVID world.

Our practical and actionable playbook offers a fast, structured approach to bring large opportunities into plain sight and allow a true view of your firm's differentiation. Putting this into practice builds collaboration within your teams and helps elevate discussions to the right level.

Exhibit 12: Oliver Wyman's RESET4Value Playbook



Source: Oliver Wyman analysis

Leaders can pick their spots for quick wins, reallocate resources to the highest priority areas, and accelerate self-funding to monetize new capabilities. Overall, the playbook encourages innovation and provides a sustainable way to embed cost transformation and growth into your current business activities.

Performing the “Four Acts” in a cohesive, self-reinforcing whole is key. Many times, leaders may re-envision customer value and segment their costs, but do not take further steps to link their cost, growth and investment agendas or ultimately change the organization’s behaviors.

As we’ve said, these “unconventional times require an unconventional mindset.” Building courage in your convictions and allowing time for the reset to take shape makes a difference.

Oliver Wyman can help your business execute these challenges and fuse your cost transformation together.

The time to get started is now.

Oliver Wyman is a global leader in management consulting that combines deep industry knowledge with specialized expertise in strategy, operations, risk management, and organization transformation.

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