

2016 Life Insurance and Annuity Executive Survey

In search of innovation: life insurers and annuity providers seek new ideas, technologies and ways to operate

The EY logo consists of the letters 'EY' in a bold, white, sans-serif font. Above the 'Y' is a yellow chevron shape pointing to the right. The logo is positioned in the bottom right corner of the page, set against a background of a person's hand holding a magnifying glass over a green printed circuit board (PCB).

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About this survey

During the summer of 2016, EY's Insurance practice conducted interviews with more than 20 CEOs and executives from leading US life insurance and annuity companies, distributors, reinsurers and regulators.

This is our third annual survey, and the central theme is innovation – how companies see the need for innovation, how they're investing in it, and what they plan to do in the future to achieve growth through innovation.

Our objective was to gain insight into the current state of innovation in the industry, detailing the highest priority opportunities and most pressing challenges.

We also wanted to share the actions that respondents suggest should be taken for companies to be able to traverse the many “disruptors” that may come their way.

Executive summary

With stagnant growth and lingering low interest rates, the life insurance industry faces a challenging future. Low engagement with current customers, limited penetration among currently underserved segments (including the middle market and millennials), outdated technology infrastructure and inefficient processes are among the many issues forcing life insurers to re-evaluate how and where they do business.

Results from EY's *2016 Life Insurance and Annuity Executive Survey* confirm that a growing number of senior leaders across the industry recognize the need for accelerating change and, in some cases, a more radical transformation of the business model. New thinking and new capabilities are needed across the entire enterprise, from underwriting and product development, to sales and service, claims and financial/risk management. Innovation is now broadly viewed as an imperative, with plans and priorities varying by individual company.

Survey respondents recognize that they are operating in a time of great disruption and spoke openly about the need to embrace innovation and change with a scale and urgency not previously seen in the industry. They also provided insights about the impacts of innovation and disruption.

1 New thinking and cultural shifts

Recent technological advancements have placed new emphasis on the need for cultural change as companies rethink their approaches to innovation. More experimentation, a willingness to take on prudent risk and the ability to learn quickly from mistakes (“failing faster”) were common themes among the responses around innovation. There is a clear understanding that while not every new idea and technology will prove beneficial, it's important that companies commit time and resources to experiment with the most promising ones.

2 The customer experience front

Customer experience is where many changes are starting to occur. The majority of participants acknowledged the need to keep improving the customer experience following the examples of leading firms that continue to raise the bar on consumer expectations. Participants were also clear on the path forward and highlighted the need to increase transparency, digitize more processes and enhance selling approaches. Enhancing internal infrastructures and updating processes are still not as high on companies' agendas as their focus on the customer experience.

3 Technology-driven innovation in the near and long term

While technology-driven innovation is high on nearly all respondents' lists, there is considerably less consensus on what to do first and where to start. The pursuit of technology innovation (in the form of FinTech and InsureTech) is on the rise. Companies are establishing non-traditional partnerships and exploring other ways to adopt, develop and integrate new tools and technologies. However, participants made it clear that outdated legacy infrastructures and lack of technology-adept resources are big challenges that must be overcome.

4 The industry's perception problem

Many respondents talked openly about the need to communicate a clearer and more compelling value proposition for the industry. The perception of the industry as dull and non-innovative is a long-term problem that has contributed to the current talent shortage and opened the door to competition from non-insurers, including FinTechs.

This report will explore additional insights around these themes and share revealing commentary from survey respondents.

1

New thinking and cultural shifts

Insurers must take on more risk, fail faster and rethink core operational approaches across the enterprise

Change is needed

Senior executives expressed intense interest in innovation and a strong commitment to change, while also openly acknowledging that the industry can no longer operate as before. This thinking will need to be backed up with concerted action. One respondent noted, "Insurers are very quick followers, but very seldom are we trying to lead." Another pointed out, "Everyone wants to be second. No one wants to be first," in adopting new technologies or operating models. It is possible that such emulation can lead to innovation, provided organizations identify ways to adapt existing technologies or create new solutions specifically for the insurance industry.

While some in the industry have embraced innovation, insurers have considerable work to do to catch up to innovators in other industries and protect against disruptors. Some companies will need to take on new strategic directions, while others may be in course-correction mode.

"Failing faster" and "experimentation" were common themes among many participants. Day to day, workers at every level of the organization must think and act differently. "We need to get people to be willing to make mistakes," was how one executive framed the idea. Some executives seemed almost excited by the prospect of change. "There is a lot of 'test, learn and refine' that needs to be done here," was one representative comment.

"Insurers are very quick followers, but very seldom are we trying to lead."

Initiating change

Underwriting is where many important changes have been initiated. This is largely due to necessity, both from the operational excellence and competitive perspectives. As one respondent put it bluntly, "The underwriting process is archaic." Another commented, "Large data-driven and technology companies like Amazon can change underwriting."

Embracing new technology

Innovation must happen in other areas, including claims processing, a customer-facing process that is ripe for change. Consumers want speed, access, collaboration and personal service when filing a claim. They also need compassion and understanding during what are likely difficult and stressful times. As one survey participant said, "The day that you file a life insurance claim is the worst day in your life." New technologies will deliver convenience to customers and potentially improve claims processing time, efficiencies and costs.

Slow to adapt

Historically, the industry has been slow to embrace change and adopt more innovative practices, especially when it comes to customer-facing operations. For an industry that calculates risk down to the penny, there is an obvious struggle with the idea of doing things differently or blazing new trails. At this point, creative innovation, a faster following and widespread emulation of customer experience leading practices should be the goal for insurers.

"Everyone wants to be second. No one wants to be first."

Action items

- ▶ Develop ways to incent and reward prudent risk taking and allow failures
- ▶ Design pilot programs to address highly specific issues and assess solutions such as streamlining the customer application process
- ▶ Experiment with innovation across customer-facing processes
- ▶ Quickly emulate leading customer experience leading practices



The customer experience front

Life insurers have significant work to do to meet 21st-century customer expectations

The customer experience needs to be improved

Insurers know they need to improve at selling, underwriting and serving customers, largely because they are now judged by the standards defined in technology, retail, travel and hospitality, and other high-profile sectors. Even if it seems unfair, insurers are compared to leaders in the technology, distribution and hospitality industries that have made customer experience an art form.

Common practices among these companies, from easily accessible account information and user-friendly products and services, to quick processing and delivery, are not attributes of insurance carriers. Executives understand the issues. “Not having the ability to access information drives customers crazy,” said one respondent. “We need to learn to ask for data once, rather than multiple times,” said one executive, while another suggested that a transformation of customer experience should be within reach: “Customer engagement is serving the customers the way they want to be served.”

In rethinking their interactions with customers, insurers should be guided by value propositions that serve both policyholders and the company. For instance, cutting down the initial application and underwriting process to 30 to 60 minutes from 30 to 60 days offers great benefits to the insured and insurers alike. Several respondents commented that this is a worthy and attainable goal.

Commonly cited areas of improvement

Digital

Digital is the default interaction channel for huge numbers of consumers. It's where they go to get answers to their questions, research products, communicate and shop. The

industry needs better mobile apps, a stronger social media presence and more intuitive online tools. Insurers need to improve access to more and more personalized information and offer a paperless option. With the rising demand for seamless digital experiences, some organizations have created a chief digital officer role to help bridge technology and marketing.

Transparency, disclosure and simplification

Survey respondents emphasized the need for the industry to be more transparent in nearly everything it does. Information about policies and products should be easily accessible and written in a way consumers can understand.

Product innovation

Product design is directly related to customer experience. The industry needs to go beyond standard products to develop more flexible, transitional, life-cycle products that provide new combinations of benefits. By aligning to customers' changing needs and life events, transitional products also offer advisors new opportunities to re-engage with customers at different stages of their lives.

Selling approach

Current commission structures do not encourage or create better customer service. The way most transactions are managed today, the primary alignment between advisors and policyholders occurs during the initial sale process. Companies and advisors need to consider the lifetime value of their customer relationships, which means a greater knowledge of their needs to make the right offering at the right time. Survey respondents referenced the concept of team selling to emphasize stronger customer relationships. A respondent seemed to encourage the industry to accept the difficult realities of the status quo: “Distribution is a partner, not a customer anymore.”

Meeting customer expectations

Individually, these problems can seem small, but when addressed collectively, the solutions offer significant upside for insurers because of the net effect on customers. What customers want, after all, are “trust and personalization” and “a greater level of confidence that they are making the right decision,” according to respondents. More transparency, better data sharing and more intuitive transitional products will help promote these outcomes.

Life insurers must move now because rising consumer expectations mean they could fall further behind and unknown “disruptors” could meet those expectations. Fast and frictionless experiences, with high degrees of personalization and consistency across channels, are the current baseline of consumer expectations – and the industry has significant work to do to meet it.

Action items

- ▶ Build apps for customers to access and evaluate their insurance products
- ▶ Design and pilot “team selling” approaches to increase the potential number of customer interactions
- ▶ Re-evaluate current commission structures

3

Technology-driven innovation in the near and long term

To reduce costs and unleash performance gains, insurers must modernize systems and process and deploy enabling technologies

Insurance update needed

Respondents recognize that chronic underinvestment in technology means the industry must make significant investments to upgrade technology. As one respondent put it, “The companies’ legacy systems are a noose around their necks.”

There is considerably less consensus, however, on what to do first or where to turn for answers. Respondents described searching for solutions in many different locations around the world, from the biggest technology players in Silicon Valley, to mid-sized disruptors in Des Moines, to innovation hubs in Bangalore. Many insurers have taken the initiative to learn everything they can about technology and new data sources, committing senior leaders to do the necessary in-depth research.

Investing in technology

Insurers are evaluating potential investments in companies that are developing leverageable technology for core insurance operations and distribution processes. In addition, insurers are seeking trusted partners to help them identify emerging technologies and integrate existing tools and data assets.

“FinTechs” and “InsureTechs” present opportunities for partnering or acquisition. The challenge is to figure out how the technology can be adapted to the unique needs of the insurance business. Respondents mentioned underwriting and sales as likely areas for early investments. One respondent noted that, “Technology is a substitute for the distribution that is moving out.”

The survey results confirm that technology overhauls are prominent on the agendas of senior leaders. Their advocacy and support are necessary to overcome formidable barriers to innovation, which include inflexible legacy systems and a severe lack of talent in the new technologies. Inherently risk-averse cultures and the fear of investing in the wrong things - an understandable consideration, given current macroeconomic pressures on the business - are major challenges. Mastering technology may take more “people to be willing to make mistakes,” as well as picking the right tools and applications for investments.

Technology talent is a need

Regarding innovation and technology, one survey respondent was clear, “There is a talent issue with both operations and technology.” Insurers now need software developers, programmers and user experience architects to create mobile apps and better digital experiences. Similarly, compiling and analyzing data is critical to insurers’ success, driving a need for more data scientists and advanced analytics professionals to conduct sophisticated data mining.

“The companies’ legacy systems are a noose around their necks.”

“Technology is a substitute for the distribution that is moving out.”

Tools and focus areas

Among the specific tools and areas of focus cited by survey respondents as near-term priorities:

New data sources

Fluid collection is one aspect of the underwriting process ripe for change because it's invasive and time consuming. One respondent indicated, "We must have substitutes for physical medical data." Accessing medical databases, credit scores and other types of data on individuals could ultimately shorten underwriting timelines.

Predictive analytics

Insurance companies have lots of data, but few are able to generate actionable insights via predictive analytics. With a better understanding of the data, insurers can gain new visibility into product performance and customer buying habits. They can uncover hidden growth opportunities, devise new cross-sell strategies and measure distribution efficiency. The goal is to better predict which products will be successful, the optimal price and how long customers will keep them in force. As one respondent said, "There is no such thing as bad risk, just bad pricing." It is worth noting that other mature industries in advanced economies with low projected organic growth and competitive pricing have relied on predictive analytics to compete and drive growth.

Wearables

Wearable technology is used by millions of consumers across the country to track their daily activities and overall health. Many in the industry are wondering if wearables can be used for underwriting purposes and to pass on better rates to consumers who lead healthier lives. Some respondents are skeptical. One stated that, "Wearables are gimmicky and have no value." Other

executives pointed to more sophisticated applications, such as providing medical-grade vital signs from anywhere, at any time. These types of wearables may ultimately prove more useful for health insurers, but not exclusively.

One survey respondent shared a big idea: "We should find ways for insurers to help people be healthy." This can be done in a variety of ways, including offering life insurance products that motivate and reward healthy behaviors. Such products can be supported by wearable technology to keep track of consumers' progress, with premium savings and/or policy discounts offered for meeting certain milestones.

Robo-advisors

Robo-advisors use algorithms to provide automated financial advice or suggest products that suit consumers' goals and risk tolerance. Many consumers today prefer self-service, digital channels and will first turn to the web or their mobile devices to research and shop for insurance. Because they don't require human interaction, robo-advice models may undercut traditional distribution channels.

Blockchain

Blockchain, or distributed ledger technology, is another highly disruptive, but potentially useful force in life insurance. The upsides are reduced costs, increased information accuracy and reduced risk based on blockchain's ability to streamline transactions, such as monthly closes and execution of payments. Consider how blockchain can help reduce asset management costs for global insurers that spend millions of dollars every year in hedging fees to protect themselves from currency fluctuations. Similarly, blockchain can strengthen fraud-prevention capabilities by validating users and transactions and

securely linking vendors in fully auditable ways. Claims management is another potential use case. A distributed ledger can enable the insurer and various third parties to instantly access and update relevant information.

Companies are already starting to experiment with the technology. In fact, one of the largest insurers in the world is currently exploring how to use blockchain in an insurance environment to streamline new investments management, business processing, policy administration, customer payments and distribution of proceeds, among other processes.

Machine learning and cognitive systems

New technologies use algorithms and self-learning to assess more data faster, detect anomalies sooner and provide more precise modeling and rules definition. Faster and improved process automation may produce better assessments of lifestyle risk as part of the underwriting process and liberate senior underwriting associates to focus on anomalies and outliers. This not only enhances the speed of underwriting, it also moves it closer to becoming completely paperless.

Action items

- ▶ Begin piloting predictive analytics by combining existing internal data sets with third-party information
- ▶ Develop "buy vs. build" business cases for robo-advice models and other FinTech solutions
- ▶ Develop algorithms for the underwriting process
- ▶ Hire software developers, data scientists and advanced analytics professionals

4

The industry's perception problem

Innovation and dynamism are necessary to change common views of the industry

Public perception must change

Survey respondents agreed that the industry has an opportunity to upgrade its image by articulating the benefits it offers to consumers and society. There is fear that the industry is viewed as outdated or being behind the times. As one survey respondent asked, "How many people say with pride at a cocktail party that they are part of the insurance industry?" Another respondent, a CEO, confessed that he wouldn't recommend a career in the industry to his own children.

The "perception problem" affects nearly every part of the organization:

- ▶ Products are difficult to understand and in some cases do not align to the real-world needs of current and prospective policyholders.
- ▶ Better technology and more information can help engage a younger and more diverse base of customers.
- ▶ Consumers expect shorter process timelines in underwriting and greater responsiveness in claims.
- ▶ Both self-service channels and in-person advice must be available.

Developing better products

The industry is not known for its flexibility. As one respondent put it, "We need to create the nimbleness people expect today." The modern consumer values self-service and, thanks to mobile technology, expects fast and convenient access to the product and pricing details they need to make their purchasing decisions. They also value the omni-channel experiences offered by other companies.

"How do you attract the next generation of customers while still maintaining relationships with the current ones?"

New products must be easier to understand and connect with consumers on their terms and at various points in their lives. The current focus on highly standardized, low-engagement products for high-net-worth individuals must evolve to reflect the unique needs of a broader and more diverse customer base.

Better products can also help with public perception about the industry's reason for being. One executive asked, "How can you encourage people to take their financial health more seriously?" Clearly, there is a societal need for increased retirement savings (especially in the middle class).

The life insurance and annuity industry is uniquely positioned to help more people have a secure retirement, but respondents agreed that the industry has not done enough to educate consumers or promote financial literacy. One respondent was blunt on this point: "As an industry, we do a terrible job at marketing."

Engaging and educating customers

The industry can do more to communicate a clear and compelling value proposition. One respondent highlighted that the public is generally not aware that insurers survived the global financial crisis in much better shape than any large bank. It won't be easy, of course, as the industry must sell to people who would "rather spend money on SmartPhones than life insurance," according to one executive. Another cited the difficult balance the industry must strike: "How do you attract the next generation of customers while still maintaining relationships with the current ones?"

The focus should be on engaging and educating customers with media and channels that customers are comfortable using, including social media, mobile apps and video. Agents, in particular, can use these tools to improve customer experiences and educate them on the value of insurance.

Action items

- ▶ Communicate a more clear and compelling value proposition
- ▶ Promote financial literacy in schools and elsewhere throughout the US

Bottom line: innovation and experimentation are not optional

While the survey results may seem troubling to some, it's clear that the industry recognizes the opportunity and need to change for the better. It's exciting to see that senior industry executives have begun to shape a strong and ambitious agenda around innovation, from enhancing the customer experience and product sets, to embracing technology and transforming operations.

While some do not have a firm grasp on where to begin, industry leaders know that change must happen faster and more broadly. For a traditionally risk-averse sector, this is no small task.

Change means updating fundamental operating models and recruiting new talent with different skills and different attitudes about technology.

It means quickly "testing and learning" from multiple innovations and eliminating the stigma of failure (since failing fast is a hallmark of the most agile and innovative companies in other sectors).

And it means that experimentation must become more the rule than the exception if insurers are to develop the nimbleness they need.

Innovation is now imperative for the insurance industry.

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