WHITE PAPER

TURNING DIGITAL CHALLENGES INTO INNOVATION OPPORTUNITIES

Lenders and Insurers

Today's unforgiving economic climate, combined with the lightning speed of technology innovation, confronts financial services firms with a multitude of challenges.

The good news, however, is that many of these challenges can also be seen as opportunities.

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"As the financial services industry shifts out of recovery mode, companies are looking beyond compliance investments and thinking about where to direct investments to increase growth and operational efficiencies."

–Bob Contri of Deloitte LLP in the *Wall Street Journal*

"No matter where you are within the cycle, one thing is clear: Firms need to move onto the next generation to grow the business by getting back to an acceptable return on new capital and using technology for operational efficiencies. Firms are forced to reinvent themselves every few years to be successful in this landscape."

Here, we review some specific challenges and explore how forward-thinking companies are tackling them.

Key needs in insurance

How can I remain relevant as an insurer?
Traditional firms are facing massive competition from online sources, and in response they're both leveraging their knowledge and making their offerings more convenient, accessible and easy to understand. Providing a range of helpful online information draws millennials who like to conduct their own research before talking to a sales rep, and tailoring communication methods to customer preferences shows synchronicity. "You now must prove your wealth of knowledge is far greater than a website," advises **Scott McLaren** of Fortegra. "Bring new policy options to the table when able, present policy updates or changes in layman's terms and position yourself as your customers' very own FAQ page. Do this by learning the ins and outs of your customers' lives, and don't be afraid to point out loopholes in policy purchases."

How can I create reasons for customers to remain loyal to me?
A recent **Accenture** report points to this as a huge struggle as digital-savvy firms take business from the non-savvy. Only 29 percent of insurance customers in the study report being satisfied with their current provider, only 27 percent think highly of their provider's trustworthiness and a significant 21 percent believe most insurance carriers are the same in products and services offered. The good news? All that uncertainty means "as much as $470 billion in property/casualty and life insurance premiums are up for grabs."

How to respond? Accenture recommends all insurers maximize digital technologies, focus on customer relationship-building and/or team up with outside-industry partners to offer "adjacent non-insurance products" like State Farm's smart home risk-management services.

How can I take operational costs out of the business?

Many insurers are finding profit margins problematic due to low interest rates, industry-wide price transparency, consumer cost consciousness and regulatory change. But the savviest are countering that, says a **McKinsey** study, through operational and performance improvements. Patterns it identified include:

- Reduction of product and process complexity, often through streamlined IT platforms offering advanced automation and cross-channel standardization of business. For one subject, such tactics lowered operations costs to half the industry median. "Understanding the details behind their cost levels — on a per product, per channel or per location view, for instance — will enable insurers to get to the root causes of business complexity and develop targeted countermeasures," the research notes.
- Customization of operating models that address processes, location footprint, supporting technology, employee skills, sourcing, organization and governance structures. One subject consolidated operating units into one central location, for example, to gain economies of scale.
- Digitization of processes. The study shows several examples of how IT streamlining correlates to cost reduction; one subject reduced claims regulation costs by 20 to 30 percent, processing costs by 50 to 65 percent and processing time by 50 to 90 percent.
- Sustainable performance management that produces new mindsets and behaviors, new performance metrics and targets, new processes and better performance dialogs between hierarchies. One subject achieved a 20 percent back-office cost reduction through such changes.

Key needs in banking

How can I remain relevant as a banker?

Industry prognosticators say the future of banks depends on their ability to capitalize on their longstanding advantages — including tradition and wealth of capital — while embracing cutting-edge technology, as well as products and services offered through their customers' preferred channels. They must also overcome trust issues, partly by displaying a positive social influence. "The relevant bank will be technology enabled but will remain human," reads a report on **Capco.com**. "It will grow as an enabler for individuals to effectively manage one of their most important resources. It will overcome legacy issues — structural divisions, technology complexity — and reclaim the advantages of 'heritage' — experience, longevity, brand familiarity and trust." A recent **Gartner report** outlines how traditional banks must adapt in segments including digital banking, payments and payment architecture, "programmable economy" and digital ecosystem.

How can I effectively sell the right products across digital channels?

Because end clients increasingly demand digital functionality and cost efficiency, revenues are migrating toward banks that switch to digital automation, create new products, improve regulatory compliance, transform customer experiences and disrupt key components of the value chain, reports **McKinsey & Co**. It predicts "digital laggards" could see erosion of 35 percent of their net profits, while winners may realize a profit upside of 40 percent. Its specific recommendations include:

- Improve the customer journey through personalization, speed and ease of use in qualifying and applying for loans, maximizing accounts, reconciling payments, etc.
- Applying advanced analytics and real-time data for better cross-selling and up-selling.
- Creating an agile company culture that's more open to experimentation.

How can I make use of emerging FinTechs as digital channels?

The 12,000 or so FinTechs worldwide are gaining ground by maximizing the use of predictive analytics, machine learning and other cutting-edge methodology. That was reflected last year at FDIC-insured institutions, where commercial loans of less than $1 million represented only **21 percent** of all commercial lending compared to 34 percent prior to 2008.

Some banks are responding by partnering with FinTechs in creative ways. The banks bring to the table capital, market reach and existing customer relationships, while startups bring flexibility, agility in emerging technologies and speed in addressing clients' pain points. In some cases, banks are offering up capital, mentoring, work space and legal, marketing or technology support. The Accenture-sponsored Fintech Innovation Lab in New York City, for example, invites startups to create pilot projects in exchange for mentoring, while Wells Fargo invests up to $500,000 for each participant in its accelerator program, which generates new products for possible acquisition.

Such arrangements are worth exploring but can be expensive for banks, which should consider ROI before investing.

How can data help me sell effectively while helping manage risk better?

Now and into the future, big data will be a boon to companies segmenting audiences to fine tune sales strategies so they get the most bang for their buck. Data-driven methodologies are being maximized to target high-value prospects, keep existing customers on board and expand opportunities, among many other business functions.

To manage risk, forward-thinking lenders are increasingly using predictive analytics, the computer methodology that uses copious historical data to predict future group behavior. Another tool is machine learning through which computers create models based on patterns found in big data, tracking, analyzing and comparing millions of data points about consumers and their business histories. That's combined with economic data and proprietary information from borrowers to nimbly analyze the likelihood clients will repay their loans.

Key needs in both banking and insurance

How can I use data to improve the business value of a process?

Many businesses are focusing on a methodology called "process mining" to draw conclusions about improving various business functions. Advanced statistics are able to offer insight into what happened, why it happened, what will happen next and what the best possible outcome could be in any given business setting. The **methodology** bridges the gap between traditional model-based process analysis and data-centric analysis techniques such as machine learning and data mining, using event data such as log files and transaction journals to find areas for improvement. According to IBM, the method can produce graphical information showing event paths or processes, sequences, durations, common paths, outlier paths and bottlenecks. It's been used to improve processes for call center operations, refund processing, purchasing and payments, internal audits, medical diagnosis and treatment practices, and other functions.

How can analytics be prescriptive and predictive, rather than only reflective?

The relatively new method of predictive analytics allows vast amounts of historical data to predict future behavior among groups. **Harvard Business Review** notes it can be used in business to predict metrics like customer lifetime value, next best offer (what your customer might buy next), future sales figures and the most effective media for your upcoming ad. However, users need to vet the quality of the information gathered by verifying data sources, ensuring samples represent relevant populations, identifying outliers and checking assumptions.

"Even with those cautions, it's still pretty amazing we can use analytics to predict the future."

– Thomas H. Davenport in *HBR*

How do I effectively use internal and external data together?
Companies that can incorporate both often have a competitive advantage, and reasonably priced and easy-to-use software on the market can integrate both categories to make patterns easier to see. Insurers, for example, can incorporate open-source intelligence derived from news and social media sources to better identify client risk, while bankers can use advanced analytics to gain insights and evaluate opportunities to improve cross-selling and up-selling. Often the challenge lies in determining which of the copious kinds of data available will be of most value to a given organization.

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