

Commercial lines insurtech: A pathway to digital

Rather than fear the disruptive potential of insurtechs, commercial insurance executives should view them as a catalyst for digitization.

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Companies across industries are seeking to embrace digital technologies—to support new business models, improve efficiency, and gain a competitive advantage. Commercial insurance executives recognize the benefits of digital but face several obstacles in making headway. Large incumbents lag behind because the complicated nature of underwriting and claims often requires human judgment and interaction, transactions are sometimes low volume and bespoke in nature, and legacy IT systems and processes make the transition resource intensive and complex. What’s more, commercial insurance has historically been slow to change, and a lack of companies with clearly demonstrated impact from digital has left many executives focused on their own plan of action.

Enter insurtechs. Rather than seeking to completely transform commercial lines, most insurtechs are focused on enabling or extending the insurance value chain. In personal insurance, insurtechs have played the role of digital attackers and captured market share at specific points in the value chain. Lacking the scale and expertise needed to excel in commercial, insurtechs can be viewed by executives not as competitors to be feared, but as potential partners that could accelerate their digitization efforts.

The rapid proliferation of commercial insurtechs has created a challenge for large incumbents: how to identify and prioritize worthy candidates for investment and collaboration. Due to this uncertainty, many commercial insurers have been sitting on the sidelines.

The urgency to embrace digital is accelerating, however, so those who wait may miss out on opportunities to benefit from this wave of innovation. As a first step, executives should become more familiar with the areas in the value chain where insurtechs are concentrating their efforts. Armed with this context, insurers can prioritize their engagement toward insurtechs in ways that can add value to their own strategy. This strategic collaboration can help to usher in new, tech-enabled approaches that should inspire commercial incumbents and accelerate the digitization of their enterprise.

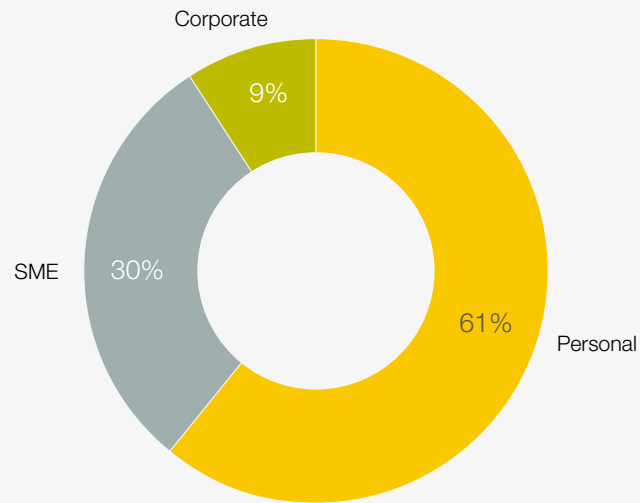
How insurtechs will affect incumbents

Over the past few years, global investment in insurtechs has grown by leaps and bounds—from \$250 million in 2011 to \$2.3 billion in 2017. Although the United States was the pioneering market for these companies, only 38 percent of all insurtechs are currently headquartered there. According to the latest figures, there are more than 1,500 insurtechs globally, and 37 percent are based in Europe, the Middle East, and Africa (EMEA)—in particular, Germany and the United Kingdom. An analysis from McKinsey’s Panorama Insurtech database shows that around 39 percent of insurtechs are focused on the commercial segment, mostly in small and medium-sized enterprises (SMEs), as shown in Exhibit 1. (See sidebar, “About the research.”)

As the number of commercial insurtechs grows, their influence will take different forms. Some will partner with incumbents to provide innovative new products and services, and others will be acquired and integrated into incumbents. The majority of commercial insurtechs (63 percent) focus on enabling the insurance value chain and partnering with incumbents. Only a small number

Exhibit 1 Insurtechs are entering the commercial lines space, especially in the SME segment.

Insurtech focus by customer segment, %



Source: McKinsey Panorama Insurtech database

of insurtechs (9 percent) are attempting to fully disrupt the insurance market (Exhibit 2). These companies do not currently pose a serious threat to incumbents, but in the coming years they might be able to make inroads in certain segments or niches and take market share.

Despite significant digital advances, commercial lines still rely heavily on human judgment and manual processing—particularly in underwriting. This high-touch model not only increases operating costs but also limits the ability of incumbents to provide superior customer service (such as risk prevention and loss control) for a select few clients, specifically those with large accounts or where change in risk behavior would have considerable impact. Insurtechs, however, can help scale and expand risk-prevention services. In doing so, companies can extend their services beyond the largest accounts while significantly improving performance and efficiency.

Commercial insurtechs are currently concentrated primarily in two areas: digital interaction and core insurance capabilities (Exhibit 3).

Digital interaction models. Inspired by the success of digital brokers and advisers of insurtechs in personal lines, a number of commercial insurtechs, such as Finanzchef24, Insureon, and Zensurance, are providing new and seamless digital customer experiences. Others, such as Gather, are inspired by the digital peer-to-peer (P2P) models seen in the retail segment. The new digital interaction models also lower the cost to serve customers and increase transparency in pricing and coverages.

About the research

To assess the current state of insurtechs, we drew on McKinsey's Insurtech database, which includes more than 1,500 commercially successful insurtech start-ups. Each start-up's business model is analyzed in detail to understand its location in the value chain, line of business, customer segment, and monetization model. The database is used to map and navigate the insurtech universe and support efforts to identify investment or partnership opportunities. It also tracks developments and uncovers trends and patterns of the insurance business—critical insights when prioritizing relevant innovations.

Furthermore, some of the digital brokers interact directly with reinsurers and other capital providers while outsourcing insurance processes, such as claims handling. These emerging models may support consolidation in today's heavily intermediated value chain. Notably, the digital interaction models used by commercial insurtechs will most likely have the greatest value in the SME segment.

As the customer decision journey for the lower end of commercial lines starts to resemble personal lines, North American traditional companies and insurtechs are actively pursuing commercial SMEs using digital solutions. Key trends include more automated or streamlined underwriting, a shift from brick-and-mortar to digital service and delivery, the replacement of intermediated with “direct” customer engagement, and the development of aggregator solutions.

Digital core insurance capabilities. By adopting new technologies, insurtechs in commercial lines are at the forefront of reducing manual touch and enhancing human judgment in key insurance processes, such as underwriting and claims. The increased dependence on technology lowers costs and allows insurers to adjust their approach from “art” to “science” in key disciplines, including underwriting, risk selection, and claims leakage prevention.

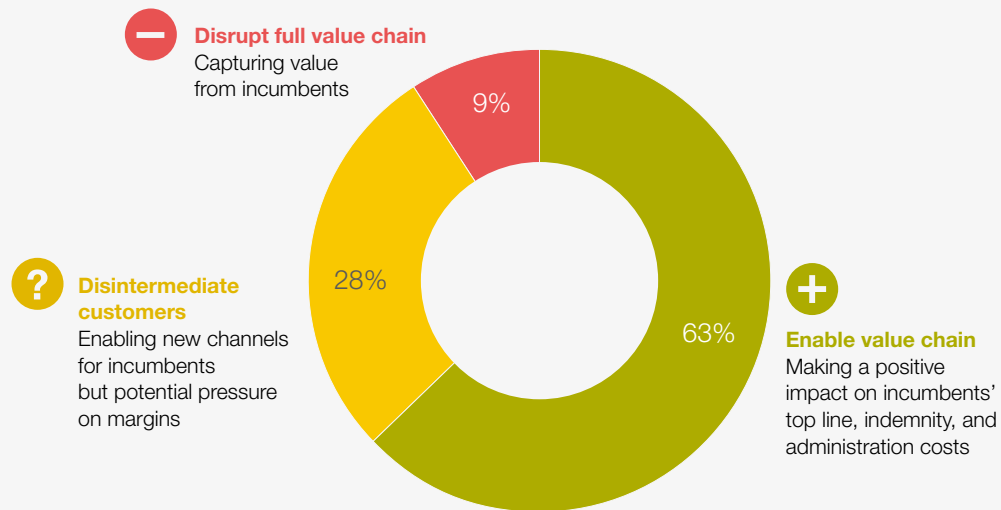
Moreover, insurtechs are using approaches with the potential to provide new services to their customers, better enabling them to monitor, prevent, and mitigate their own risk at an affordable cost. The following use cases are relevant to both SMEs and more complex commercial lines segments:

- *Virtual reality and drone technology* to improve underwriting and claims inspection data and decisions. Several start-ups have built enhanced inspection capabilities in property and agriculture. Dozens of others are building drone-based capabilities focused on insurance.

Exhibit 2

Insurtechs are both friends and foes raising strategic questions on competition and collaboration.

Insurtech role, %



Source: McKinsey Panorama Insurtech database

- *Blockchain technology* to assess the provenance of items and thereby avoid claims leakage. Examples include Everledger for diamonds and Blockverify for electronics and pharmaceuticals. XL Catlin and MS Amlin, along with Maersk, have partnered to build a blockchain-based marine cargo platform.
- *New data sources for underwriting and claims prevention.* Meteo Protect, for example, uses weather data, Augury captures status data from Internet of Things (IoT) machinery, and Windward for marine data and analytics. Wearables are becoming more commonplace as risk-mitigation tools, whether in trucking, workers' compensation, or dozens of other uses.
- *Advanced analytics.* Adapt Ready, for instance, deploys machine learning to reduce business interruption by improving risk selection.

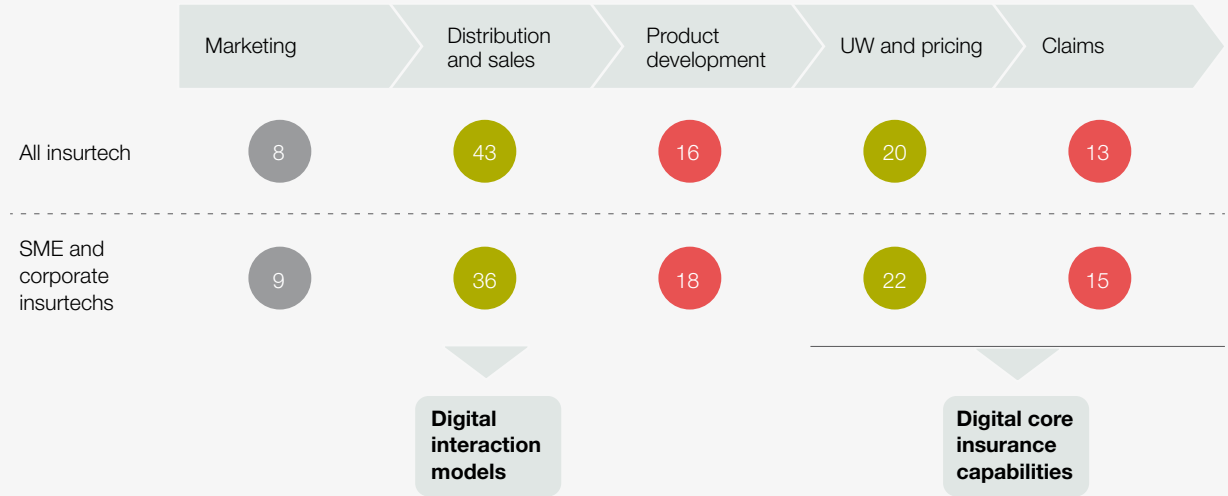
It is still unclear where digital innovation will have the greatest impact on commercial lines. However, recent McKinsey analysis found that administrative costs for greenfield insurers are, on average, half those of incumbents—sometimes even less.¹ Their cost leadership is partially due to a monoline focus and the absence of legacy IT systems and processes, as well as digital-by-design

Exhibit 3 Commercial lines insurtechs focus on digital distribution and core insurance capabilities.

Share of insurtechs in database

● <10% ● 10–20% ● >20%

Number of insurtechs as percent of total in the database



Source: McKinsey Panorama Insurtech database

products. While these results are primarily related to personal lines, the impact on commercial lines, starting within the SME segment, will become as significant over time.

Developing a plan of action

When the fintech movement started in financial services, the banks that adapted quickly to meet the challenge formulated a strategy in three phases—understand, engage, and act. Commercial insurers may follow a similar approach to determine the best way to partner with insurtechs (Exhibit 4).

A. Understand. While some of the larger insurers and reinsurers have made progress across all three stages of engagement, many insurers are currently in this phase. Commercial executives must become more familiar with the evolution of the insurtech ecosystem, gain an understanding of the research in insurtech databases or publications, and participate in insurtech accelerator programs, which are run by a third party. Other insurers have launched hackathons with insurtechs. Zurich, for example, held a two-day “Insurhack” event that focused on software innovation. It offered €75,000 in cash prizes to participants in challenges focused on areas such as open data and everyday insurance.²

B. Engage. This phase involves interacting with players in the insurtech ecosystem to seek out partnerships or inspiration. Commercial insurers can conduct more formal scouting, partner with insurtechs to develop proof-of-concept solutions, or launch incubator programs. Incumbents have launched incubator programs to provide a springboard to promising insurtechs. Most global commercial insurers have established similar incubator programs.

C. Act. Commercial executives can use their firsthand knowledge of the opportunities to partner with insurtechs to determine whether to invest in, collaborate with, or adopt an insurtech approach, or to wait and see. A few large multinational primary insurers and reinsurers are also actively investing and seeding opportunities in the insurtech space using a multitude of interaction models, ranging from investments to partnerships to reinsurance support.

Many insurers have launched venture capital funds in the insurtech space. AXA Venture Partners, for instance, has \$450 million in funding and invests in enterprise software and technologies, AI, and cybersecurity.³ Munich Re has made investments in excess of \$68 million in insurtech, especially focused on getting access to the IoT ecosystems. Its leaders view the investments as long-term partnerships where they bring not just money to the insurtech but also domain expertise, clients, and brand.⁴

Exhibit 4 Insurance incumbents have started following three phases of digitization.

	A. Understand	B. Engage	C. Act
Goal	Understand what is going on and gain awareness of the value at stake	Engage with insurtech community to seek inspiration and investigate partnerships	Acquire or invest into insurtech and adopt an “insurtech style” of working
Actions	<ul style="list-style-type: none"> • Participate in insurtech accelerator programs • Launch insurtech hackathons 	<ul style="list-style-type: none"> • Partner with insurtech to develop PoC • Launch an insurtech incubator 	<ul style="list-style-type: none"> • Wait and see • Direct investments • Partnerships • Establish a VC fund • Adopt an insurtech way of working • Become an ecosystem orchestrator

Source: McKinsey analysis

Since the insurtech space is changing rapidly, approaching the “understand” and “engage” phases as ongoing efforts rather than one-off activities can ensure that executives stay up to date on the latest developments.

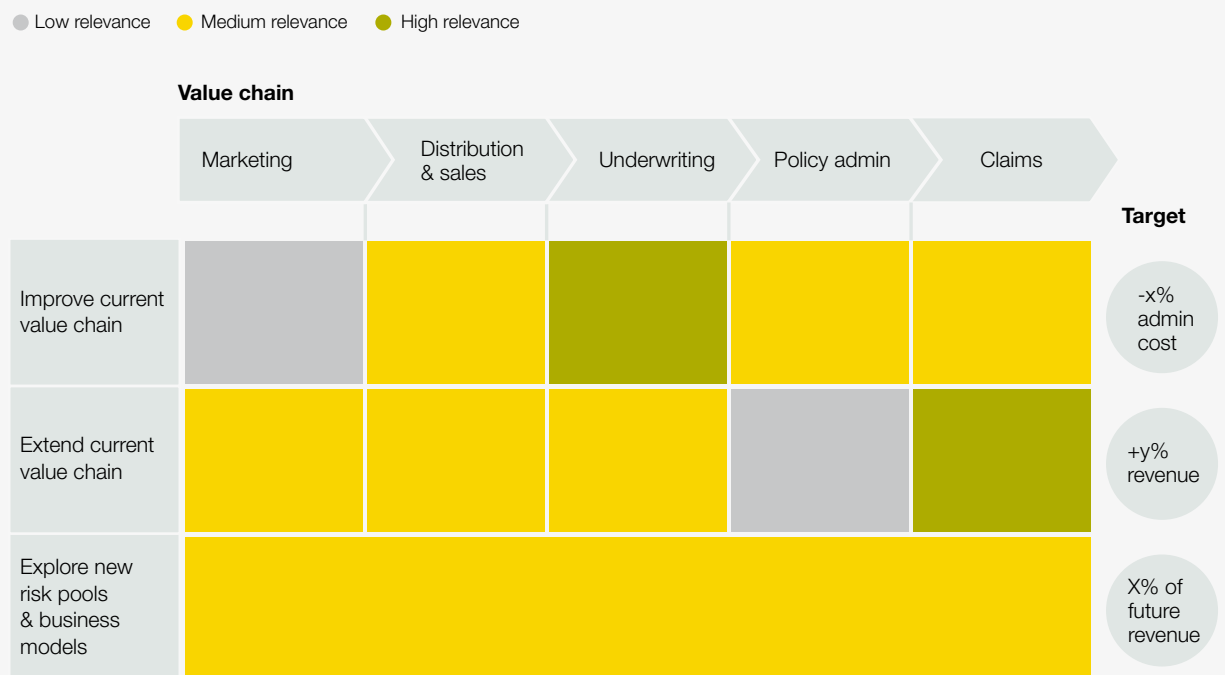
Identifying insurtech partners

Finding the right insurtechs with which to engage requires a structured approach. Executives should consider several parameters when evaluating an insurtech for a more formal arrangement (Exhibit 5):

Placement along the insurance value chain. Insurtechs have emerged at each step of the value chain, from marketing and sales to administration and claims.

Degree of innovation. The analysis should include activities from improving the current value chain (such as through the introduction of advanced analytics or artificial triaging of quotes), extending the current value chain (such as by providing adjacent services for risk prevention and mitigation), and exploring completely new risk pools and business models (such as through ecosystems).⁵

Exhibit 5 Prioritizing insurtech engagement based on value chain, degree of innovation, and strategic fit.



Strategic relevance and value for the company. This measure seeks to determine the importance of the innovation across the insurance value chain. Relevance and value can vary by function and client segment. For example, insurers seeking to extend the value chain may focus on claims, which allows broadening capabilities and enhancing service levels to insureds. Other insurers may seek to rebuild the end-to-end value chain with new, digital-based business models—for instance, Blackboard in the United States.



Insurtechs are entering the commercial lines space: many of these start-ups will fail, and only a few will succeed. The most important impact of commercial lines insurtechs is that they provide a source of inspiration for the incumbent commercial lines insurers and reinsurers and a way to leapfrog into digital.

Commercial insurers that are able to find the right insurtechs to engage with could improve margins, expand their client base, and extend their services. Forging such partnerships may allow them to relieve cost pressures and counter eroding margins once new technologies mature. To reap these benefits, commercial insurers must manage their partnerships effectively and expand IT capabilities to implement the solutions provided by insurtechs. These moves will require investment to understand and engage with insurtechs, define the right business models, and build flexible architecture that will allow insurtech solutions to integrate into IT core systems. The payoff could include not only increased digitization and new ways of generating value but also a stronger competitive position in the coming years, as disruptive models become mainstream. ■

¹ Tonia Freysoldt, Sylvain Johansson, Christine Korwin-Szymanowska, Björn Münstermann, and Ulrike Vogelgesang, “Evolving insurance cost structures,” April 2018, McKinsey.com.

² Held in Germany, Insurhack is a two-day “hackathon” challenge for coders.

³ “AXA Strategic Ventures rebrands as AXA Venture Partners,” AXA Venture Partners, April 10, 2018, axavp.com.

⁴ “Driving digital transformation,” Munich Re Investor Day, November 21, 2017, munichre.com.

⁵ Tanguy Catlin, Johannes-Tobias Lorenz, Jahnavi Nandan, Shirish Sharma, and Andreas Waschto, “Insurance beyond digital: The rise of ecosystems and platforms,” January 2018, McKinsey.com.

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