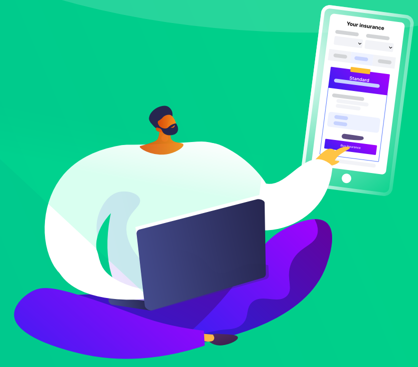
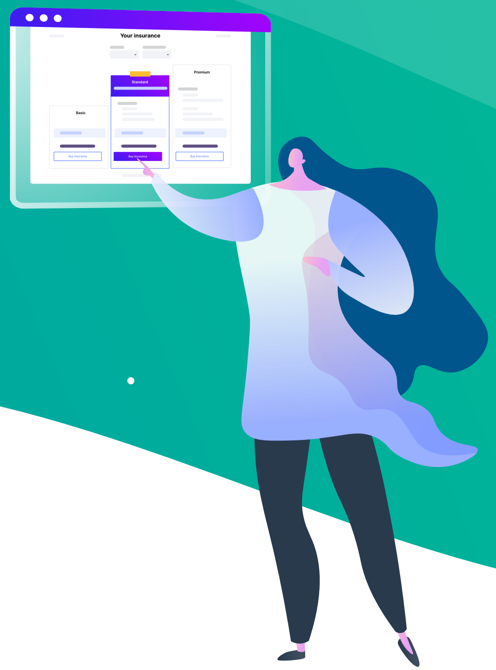


Embedded Insurance Index

Is embedded insurance going digital?

Part I



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Introduction:
Is embedded insurance going digital?

The year 2020 ushered in rapid transformations across all areas of life. The COVID-19 pandemic has exerted a toll on all industries, and insurance was no exception. For years, insurance agents have claimed that insurance will never fully go digital. This proved to be a self-fulfilling prophecy since the major industry players have run outdated, often suboptimal digital strategies. What the COVID-19 outbreak has shown us, however, is that customers have no problem dealing with insurance companies digitally. In fact, they are already used to handling far more complex and expensive online transactions.

These customer preferences had a slower impact in insurance than it did in most other markets due to insurance's lower churn rate compared to other businesses. Yet 2020 has still given us a remarkable increase in digital interactions with insurance providers, especially with regards to sales. Last year alone, digital adoption in Europe has grown from an average of 23% to 31% - an increase of 35%.[1] Despite its low digital adoption rate, insurance could not escape the wave of digitalisation that hit other industries.

This significant and sustainable change is not only about how customers are interacting with insurers. It is also about the ways they interact with banks, retail stores, brokers, bike shops and unions. For carriers who use these companies as third-party insurance distributors, the move to digital sales represents a new standard. If customers are now increasingly interacting digitally with partners that supply their everyday needs, then the insurance products offered through these third-party distributors need to go digital in order to remain relevant.

With this growing demand comes a need for a digital infrastructure that will enable companies to sell these embedded insurance products. Insurers should be ready to face this challenge. However, there is little information available about the state of these insurance distribution partnerships. It may be difficult, then, for insurance carriers and distributors to understand the current market and how to meet changing customer expectations.

1) Europe's digital migration during COVID-19: Getting past the broad trends and averages - McKinsey, 2020

We put together this report precisely because of the lack of research on third-party insurance sales and embedded insurance. Non-direct sales channels accounted for 34% of total European insurance sales in 2018 and are growing year by year. Globally, this figure reached 43% of total insurance distribution.[2] With this report, and the many to follow, we aim to shed some light on this enormous and rapidly changing segment of the insurance industry.

In the report, we focus on partners that resell insurance without bearing the risk and what their needs, demands and expectations are from risk carriers today. The report will give you an understanding of what is required to successfully sell embedded insurance as well as the major challenges to be addressed.

The report is based on a larger study where we surveyed 41 insurance distribution partners in Europe about their needs and expectations when it comes to insurance carriers and the infrastructure they provide. It is supplemented by insights of the specialists at Penni.io, who have many years of experience working with third-party insurance sales. We hope you will enjoy this read, our thoughts and the data we highlight, and we welcome any feedback you may have for future publications.

Happy reading!

Esben Toftdahl Nielsen
Co-Founder & Chief Commercial Officer Penni.io

2) 2019 Global Insurance Pools trends and forecasts: Distribution - McKinsey, 2020

Embedded insurance: An Opportunity Insurers Cannot Afford to Miss

By: Simon Bentholm, Head of Customer Success and Francesco Cocozza, Business Analyst

For more than 50 years, those who work in the insurance sector have been hearing about the promises of partner distribution. Under this model, insurance companies and their partners join forces to sell insurance products to the partner's customers. In theory, these partnerships result in a win-win-win situation that simultaneously benefits the insurer, the distribution partner and the consumer.

In brief, partner distribution promises:

- Lower cost for customer acquisition and marketing
- Higher penetration via convenience
- Improved trust, loyalty and retention
- Greater availability of data
- Increased profitability and higher revenue

These benefits apply whether we are talking about commercial insurance, personal insurance or life insurance products.

With all these benefits up for grabs, who would not want to enter into a distribution partnership? Especially when you consider some of the cases that have been disclosed, including Axis Bank seeing a 30% increase in fee-based income in 2011 after teaming up with Max Life insurance, as well as the State Bank of India increasing almost all of its customer lifetime value metrics once it started offering insurance products under a bancassurance model.

Bancassurance non-life GWP alone has grown by a CAGR of 5.3% between 2012 and 2019 while the rest of the market grew by only 2.0%, after many years of stagnant growth.[3] This resurgence of interest in cross-selling insurance can be seen in the rising price of exclusive agreements between insurers and banks over the past few years (see Figure 1[4]).

These are significant numbers and the trend is set to continue. Estimates predict that "fully embedded" insurance distributed through partner channels will generate $140 billion in GWP by 2030 in P&C alone. That is 24% of the market share, compared to the 2% of the current market share.[5]

Although insurers can expect large gains from partnerships, it is far from certain that every single partnership will be a successful one, especially when catering to digital customer channels. Many have attempted, and some have even managed, to lay a substantial foundation for digital sales and transform their business models. Yet very few have managed to establish successful digital partnerships and realize the full potential of this distribution model.

To understand why this is the case, we worked with the Copenhagen Business School and the Open Insurance Initiative to conduct the first global survey of the state of digital partnerships in embedded insurance. The survey sheds light on the current

3) European bancassurance: Impact of COVID-19 and the next normal - McKinsey, 2020
4) Digitization and Strategy: Bancassurance Trends and Best Practices in 2019 - RGA, 2019
5) Simon Torrance (2020) using OECD, McKinsey and SwissRe Institute as main sources

challenges and opportunities of digital insurance distribution from the partners' point of view. The survey was given to distribution partners that currently offer insurance alongside their core product. We received responses from 41 companies across 13 countries, including the United States, a number of European countries, India, Canada and Chile. More than 50% of the respondents reported distributing more than 1 million euros of insurance policies per year. The most represented industry of ancillary insurance distributors is, unsurprisingly, banking and other financial services providers, accounting for 39.5% of the total respondents.

The questions in the survey cover topics such as incentives for working with insurance distribution, what the results have been and what pitfalls they have faced. We have combined quantitative and qualitative questions in order to get deeper insights into the partners' situation. And finally, we have included the professionals' experience with many cases of third-party insurance sales. It is our hope that our results can help give the insurance industry a greater understanding of what it takes to build a successful partnership distribution model.

Overview of major bancassurance partnerships 2010-2019

Insurer	Year	Bank	Value	Term	Region
Zurich	2011	Satander	$1.6b	25 years	Latin America
Allianz	2012	HSBC	$100m	10 years	Asia
AXA	2014	mBank	$154m	10 years	Europe
AIA	2014	Citibank	$800m	15 years	Asia
Manulife	2016	DBS	$1.2b	15 years	Asia
Chubb	2018	DBS	$500m	15 years	Asia
Chubb	2018	Citibanamex	$500m	*non-life only	Mexico
Prudential	2018	Standard Charter	$?	Renewed in Asia (2014) and new expansion to Africa (2018)	
Prudential	2019	United Overseas Bank	$1.15b	15 years (renewal)	Asia

RGA

Figure 1: Distribution agreements between insurers and banks. Insurers are ready to pay generously for exclusive access to a bank's customer base. Reworked from Digitization and Strategy: Bancassurance Trends and Best Practices in 2019 - RGA, 2019.

Unlocking Value with Insurance Partnerships

First and foremost, distribution partnerships are a cost-effective way of increasing sales and revenue on both sides of the table. The insurer gets privileged access to a new market-within-a-market through the distributor's customer base. This provides a touchpoint with high proximity to the end-customers without having to invest in marketing. Meanwhile, the distribution partner gets to raise its margins by cross-selling a relevant product, without having to develop that product. This is consistent with the way distribution partners responded to our survey. As Figure 2 shows, the extra revenue from insurance sales is a leading motivation for 68.2% of respondents.

Note, however, that customer retention ranks just as high (68.2%), followed closely by customer service (54.5%). In other words, partners do not engage in insurance distribution solely to increase their direct revenue. Distribution partners actually rate customer retention as equally motivating when deciding to cross-sell insurance. It has been proven time and time again that the more entangled the customer is with

What is your primary motivation for having an insurance proposition for your customers? (multiple answers)

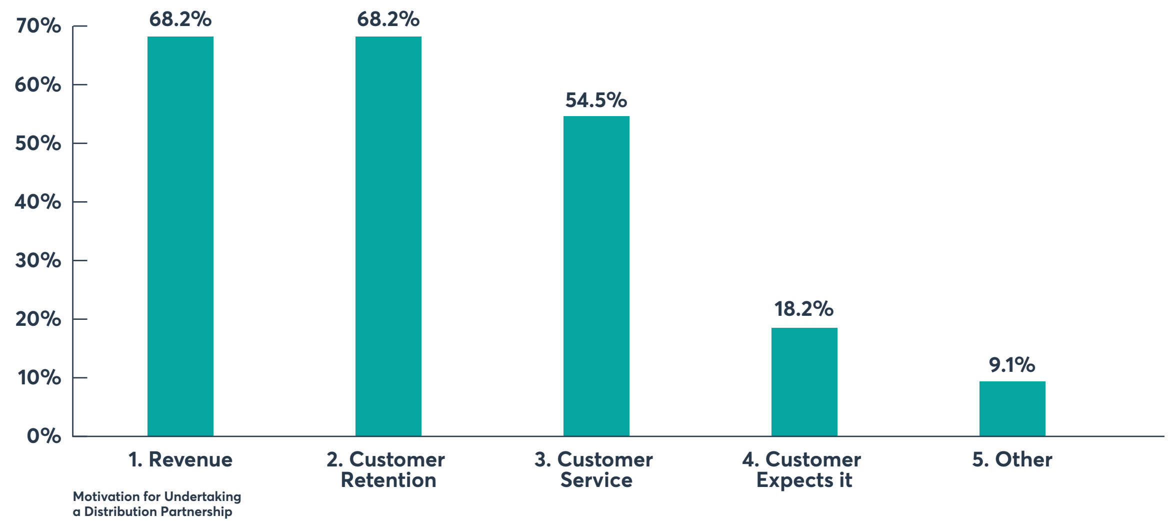


Figure 2: The primary motivations for adopting insurance distribution. 'Revenue' and 'Customer Retention' rank highest, showing that partners have a clear expectation of the benefits of cross-selling insurance.

the partner, the higher the retention. It represents another win-win situation for the partnership: higher retention means higher Customer Lifetime Value (CLV) for both sides.

Customers' willingness to purchase insurance online from non-insurance companies is becoming increasingly evident. Accenture consumer research found that "40% would consider buying insurance from a car dealer, for instance, while 30% might choose a retailer or supermarket, and 29% would consider online service providers".[6] Our data sheds further light on this growing customer trend. 68.7% of the traffic to a car insurance solution offered by one of our service providers was generated by Google searches and unsolicited exploration of the website. When the insurance product is optimally embedded into a distributor's digital platform, the customers will look for the insurance product on the distributor's website without any marketing nudge.

One of our partners took the product synergy in customer retention one step further by offering their core subscription for free for the first year, on the condition that the customer purchases the insurance product. Combining the insurance with the core product produced a higher CLV and created a convenient bundle for the customer. The insurer, meanwhile, benefited from increased sales thanks to a combined product they could not have offered on their own.

6) The future of insurance distribution: New models for a digital customer - Accenture, 2017

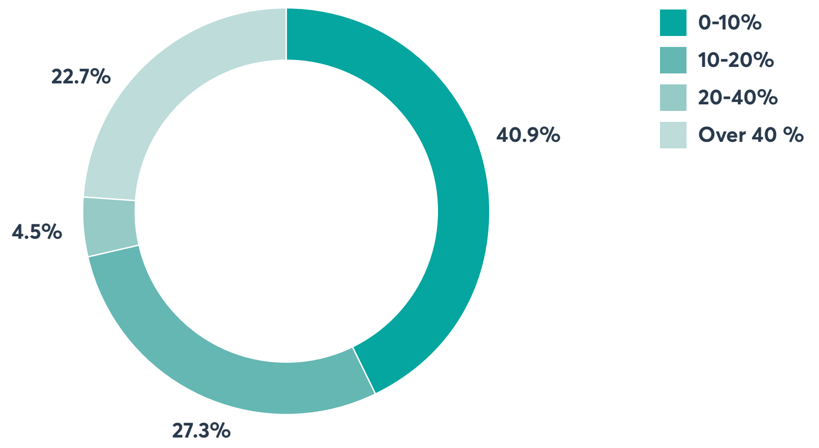
Partnership Performance in Practice: Have Expectations Been Met?

Understanding the main drivers encouraging distribution partners to work with insurance companies is important. But if embedded insurance is to create a sustainable business model, it needs to meet these partners' expectations.

The principal driver is the increase in revenue. Based on Figure 3, we can see that the average reported share of the distribution partners' total revenue from insurance sales is 17.9%. For the distribution partners, having almost one fifth of revenue coming from insurance sales represents a substantial addition to their core business. Even if we exclude financial service providers, which are in a particularly privileged position when it comes to insurance distribution, the average revenue increase created by embedding insurance is still 14.6%.

This means that even non-finance companies like auto dealers and e-commerce retailers are extracting a noticeable share of value from cross-selling insurance.

What percentage of your company's revenue comes from selling insurance?



Percentage of Distribution Revenue Coming from Insurance Sales

Figure 3: Percentage of distribution partner's revenue generated from insurance sales. More than half of partners reported that more than 10% of their revenue comes from sales of insurance.

The other main driver for participating in insurance distribution is increasing customer retention, closely followed by customer service. Since most of these partnerships are quite recent and customer retention takes several years to measure accurately, we decided that asking our respondents about improvements to customer satisfaction would serve as a suitable proxy.

Our survey shows that most distribution partners think their current insurance offering is adding to their customer satisfaction, with 93% saying they saw at least a moderate improvement and almost half of the distribution partners reporting that it has resulted in a considerable or higher improvement (see Figure 4). Moreover, none of the distributors reported that cross-selling insurance had no positive effect on their customer satisfaction. This makes an important difference, since 31.8% of distributors did not even mention revenue as one of their primary motivations for entering into partnerships with insurers.

Please rate how much your customer satifaction improves due to having an insurance proposition

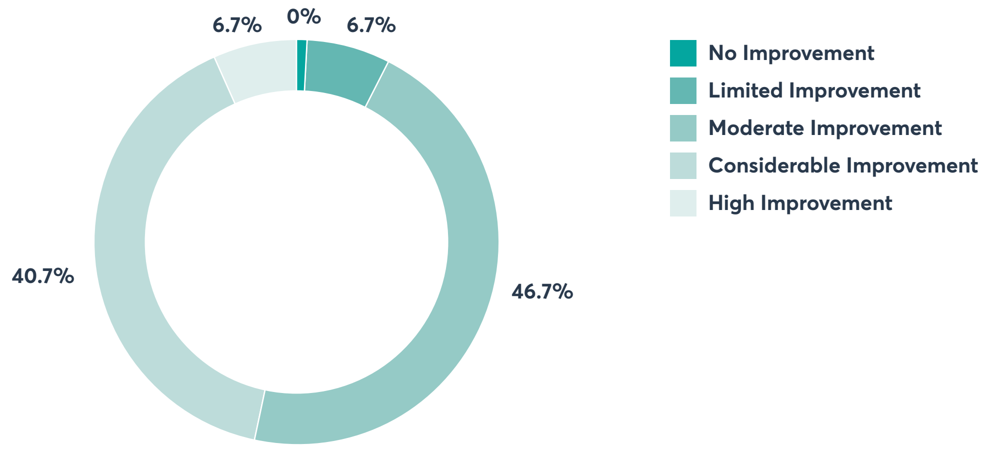


Figure 4: Impact on customer satisfaction as the result of an insurance proposition. Every partner reports that an insurance proposition improves customer satisfaction.

Performing statistical analyses on the survey data revealed that the increase in customer satisfaction and the share of revenue from insurance sales are positively, although not significantly, correlated (a 30% correlation). It may seem obvious, but this highlights the fact that those who manage to best serve their customers' interests also manage to increase their revenue the most. Likewise, the insurers who serve their distribution partner the best will also get more revenue.

Our direct experience confirms third-party insurance distribution's potential for improving both revenue and customer satisfaction. One company that distributed insurance solutions alongside its core product was primarily using a call centre to underwrite insurance contracts to its customer base. They also offered an early "digital" distribution solution to redirect their customers to the insurance carrier's domain. It was a suboptimal solution, not designed specifically for insurance sales, and it created lots of friction in the purchasing process, what we call "conversion killers." When the distribution partner embeded a specially designed widget for insurance calculations directly on their own website, digital insurance sales tripled. At the same time, customer satisfaction for their insurance proposition increased so much that they started to use the insurance product as a core component of their marketing campaigns.

The results we have presented up to this point indicate only upsides to insurance distribution partnerships. However, not everything is optimal. Even if distribution partners do benefit from entering into partnerships, many of them were still dissatisfied. Even when reporting a large revenue increase and prolonged customer retention, many distribution partners were not happy with the performance of the digital insurance proposition offered to their customers. On average, the partners reported being less than somewhat satisfied, but a high percentage (18.2%) expressed not being satisfied, as can be seen in Figure 5.

Figure 5 also shows the reported partner satisfaction with the insurer's support for their digital insurance proposition. The average level of satisfaction with the insurer's support is even lower than the rate of satisfaction for the proposition itself, with 50% of respondents indicating they are not satisfied or only slightly satisfied. On its own, this measure shows us that partnerships may struggle when it comes to support and communication, and that

insurers should make a greater effort to ensure that expectations and goals are aligned, as well as making sure the right digital offerings are present.

Our correlation analysis of these two measures reveals another important piece of information. Performance and support satisfaction have a significant correlation (36%) with each other. They tend to move together and it is not difficult to see why. If the insurer has not developed adequate digital competence, the level of support they will provide to the partner and the performance of their digital insurance solutions will both tend to leave their distribution partners dissatisfied.

This shows us that insurance companies might have a gap to fill between the digital solutions they can offer their partners and the digital solutions those partners are expecting to provide their customers. Insurance companies and brokers who can adequately facilitate their distribution partners' digital business models will have greater opportunities for attracting the most profitable partners over the next few years. On the opposite side, insurers who fail to keep pace with the expectations of distribution partners risk losing them to more innovative insurance carriers. We can already see this threat at play in the market. Insurance companies that invest heavily in digital distribution boast almost 20% more sales growth than their peers[7].

7) Bancassurance: It's time to go digital - McKinsey, 2019

How satisfied are distribution partners with their companies digital insurance proposition?

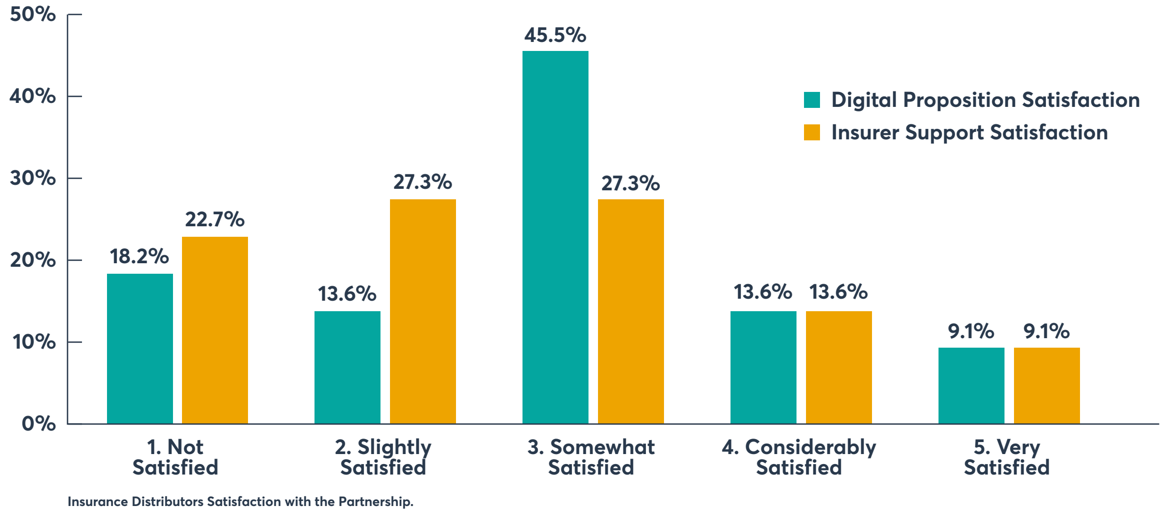


Figure 5: Satisfaction with digital insurance proposition and insurer support. Many distribution partners are dissatisfied with their digital insurance proposition and the support they receive from insurers.

What Keeps Potential Partners from Going into Insurance Distribution?

Most people within the insurance sector and their current partners are aware of the benefits we have mentioned in this article, and many have entered into partnerships because of them. However, digital partner distribution is far from the main mode of distribution and has a tendency to fade as partnerships move from decision to execution. There must, therefore, either be a lack of knowledge about the benefits, or obstacles to becoming an insurance distribution partner. In the previous section, we listed several benefits of entering in insurance distribution partnerships. Now, we will take a look at the obstacles. Our survey offers some insights on the reasons insurers and partners miss out on digitally distributed partner sales.

Standard economic theory teaches us that, when we want to know why companies do not enter a profitable market, we must first ask ourselves whether there are barriers to entry. In the survey, we asked companies about the difficulties of establishing a partnership offering. In Figure 6, we can see that the majority of

Please rate how difficult it has been to establish a digital insurance proposition

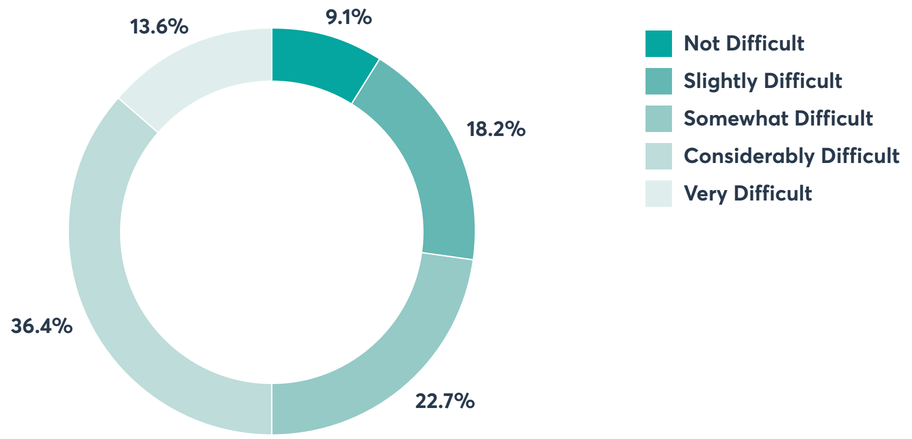


Figure 6: Difficulty of establishing a digital insurance proposition. Many partners have considerable difficulty getting the proposition off the ground.

partners rated establishing the partnership itself "somewhat difficult" or higher, with more than 13.6% even saying it was very difficult. While more than 25% did not encounter major problems, it is nevertheless clear that the establishing process is the first big challenge for the partnership.

We then asked about the obstacles that made establishing the partnership so difficult. This question was open, with some of the most representative answers being:

- "Few digital competencies in the insurance companies"
- "Prioritisation, cost, lack of clear benefit"
- "Underwriting process. Legacy systems. Regulatory requirements."
- "Regulatory burden, low level of digitalisation of the insurers, long implementation"

Our favorite is the following: "Creating a flexible and scalable distribution model requires integrations and that insurers stop 'fencing' distribution partners. Insurers are holding back on tech improvement and empowerment. Basic customer-centricity needs to be applied. Distributors must be able to make the best customer journey possible and thereby conversion."

Legacy systems and the lack of digital competence on the insurer's side were the most frequently cited barriers. The regulatory burden, which one partner described as "unclear," placed third.

Furthermore, we asked in two separate questions whether the insurance carrier provided an API solution when establishing the digital solution with the partner and how long it took to establish the digital solution. Figure 7 shows the distribution of the time it took to establish the insurance offering, based on whether the API was provided or not. The establishment time varies considerably. When the insurer provided the API, 45.5% of the partnerships were established in under 6 months, with an average completion time of 6.9 months. Without the API, however, only 9.1% of the establishments were completed within the 6-month timeframe, taking an average of 9.5 months. When the insurer was not ready to provide an API solution, a staggering 90.9% of the digital propositions took 6 months or more to go live, while none were below the ideal "Under 1 month" goal. Our data shows a strong and significant correlation (50%) between API provision and initial time to establishment.

In summary, the answers to our survey point in the same direction. Despite all the benefits they bring, embedded digital solutions are still not one of the main distribution channels for insurance because of several barriers, primarily the lack of digital competence and the presence of legacy systems. On the insurance side, clearly, but also from the distribution partners.

The manager of one of the biggest insurance companies in the world told us that his company and one of their partner banks had a total of 47 legacy systems. The bank had 21, while the insurer had 26. When they started to discuss embedding insurance products in the bank's digital solutions, they did not know where to start with the integration. When faced with such a big challenge, the idea of establishing an insurance digital proposition becomes daunting, despite the clear benefits it would provide.

How long did it take to establish the digital insurance for your customers?

Did your insurance carrier provide an API solution that helped your company in establishing the digital insurance proposition?

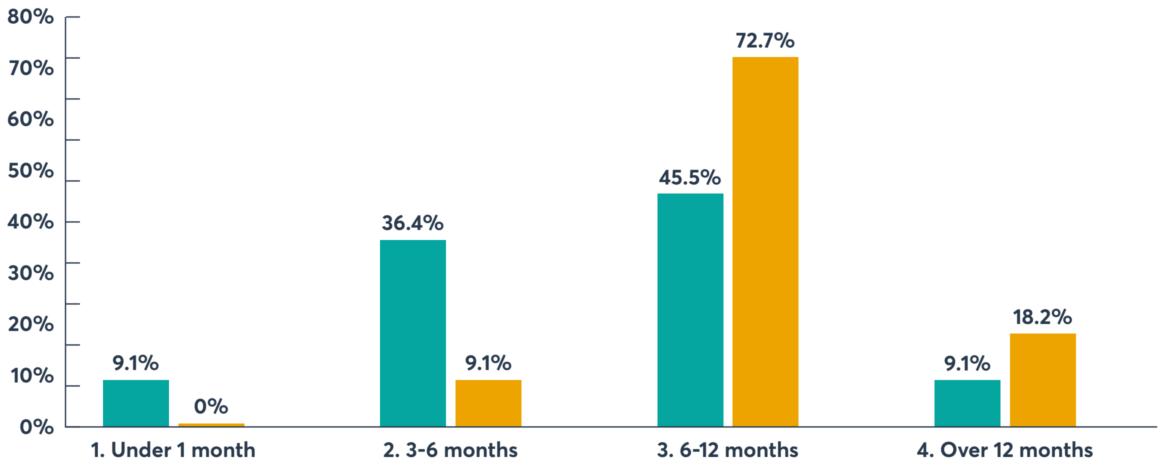


Figure 7: Time to establish a digital insurance proposition, depending on API provision. The difference derived from having an API provided by the insurer is clear and hard to miss.

Conclusion

Prospective distribution partners can expect significant upsides if they choose to go ahead and enter into partnership with an insurer. The upside for the partners includes not only a palpable increase in revenue in the short run, but also a more complete offering to customers that increases retention and consequently customer lifetime value. The insurers, meanwhile, get preferential access to new customers and can piggyback on the distribution partner's marketing efforts.

Partnerships are on the rise but they are far from ubiquitous. With such clear benefits to all parties involved, one has to wonder why that is the case. Our survey shows that partners face difficult obstacles to overcome - obstacles that center around the insurer's ability to swiftly and easily provide a technological solution that enables partnership sales. In other words, partners that choose not to pull the trigger on digital insurance sales are hesitating because they fear it could be too cumbersome.

It is no secret that the insurance industry has been slow to adopt digital innovations. The companies that do so will be the first to have access to a market opportunity that is ripe for the taking.

In the next EII-report, we will continue exploring the way distribution partners view digital insurance solutions. We will analyse their views on how the new digital possibilities could be used to increase the likelihood of a partnership's success and to finally realize the huge opportunity represented.

A special thanks to our survey partners

Open Insurance

CBS

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Appendix:
A Note on Correlations

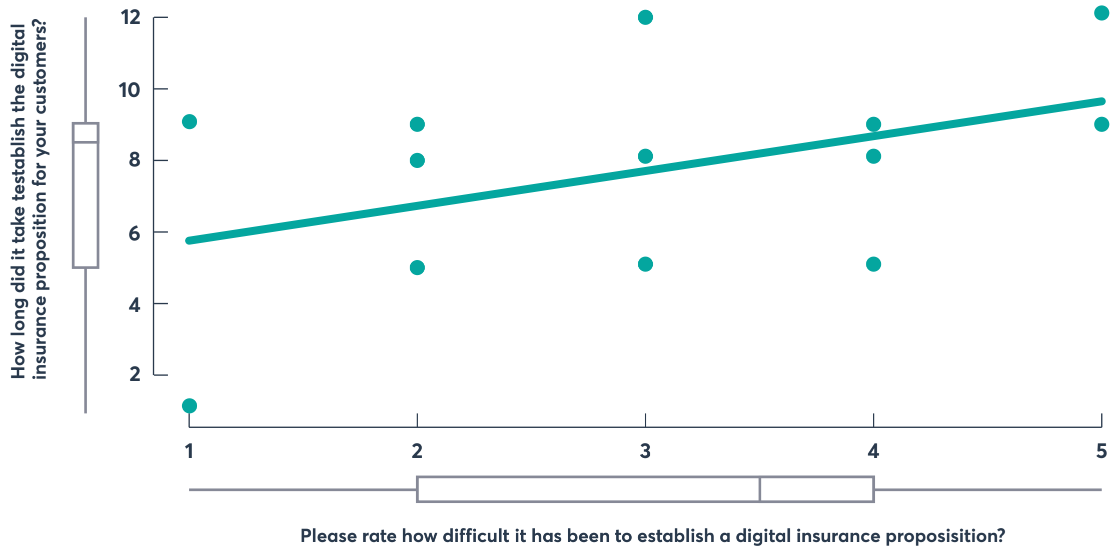
We mention correlations in several places in this report. In the interest of clarity, this section will simplify and explain what we mean by this concept.

A correlation is the measure of the strength and direction of a linear relationship between a pair of variables. In other words, it represents the degree to which two variables move together, or influence each other. Correlations move on a scale between -100% and 100%, depending on the direction of the relationship. It is said to be significant when it is possible to test, given the data available, that the relationship cannot be attributed to chance.

For instance, if variable x and variable y are correlated to each other by 50%, this means that when x increases by 1, y will increase by 0.5 on average. The opposite is also true. You can see how the correlation looks like for two of the questions from our survey, which have a correlation of 44%.

Correlation does not help us understand causality, meaning that we do not know whether x is influencing y, or y is influencing x. It simply shows us that they tend to move together.

Example of correlation between two variables - time and difficulty in establishment have a positive correlation of 44%



In some cases, however, it is possible to ascertain the direction of the relationship. For instance, the correlation between the initial API provision from the insurer and the time of establishment can only go one way.

Correlation is a useful concept because, unlike causality, it can be calculated for a vast set of variables. We are able to analyse the ways several variables influence each other at the same time. When analysing the responses to our survey, we converted all the answers to numerical values and used this property to calculate what is called a correlation matrix.

The correlation matrix is nothing more than a convenient way to summarise the set of correlations in a dataset. Here is the correlation matrix from our survey. The names used for the variables are not always intuitive, but it should be possible to spot the correlations we have mentioned in our report. You can read it just by looking at the intersection of the vertical and horizontal lines. Each intersection represents the correlation between those two variables. Spoiler alert: from the correlations you see here, you may be able to ascertain what we will be discussing in the next installment of our report!

The Correlation Matrix on the Survey Answers

	idd difficult	obstac score	time	difficult	plug play	custom made	ongoing cost	idd challenge	motiv score	idd	perform satisf	easy insur	premium	easy main	cust satisf	revenue share	upfront cost	integrat score	supp satisfaction	api provided
obstac score	0.52																			
time	0.53	0.58																		
difficult	0.58	0.5	0.44																	
plug play	0.46	0.23	0.5	0.59																
custom made	0.26	0.43	0.48	0.28	0.25															
ongoing cost	0.23	0.55	0.38	0.54	0.3	0.41														
idd challenge	0.2	0.09	-0.28	0.11	-0.01	0.03	-0.13													
motiv score	0.51	0.26	-0.01	0.34	0.23	0.37	0.29	0.14												
idd	-0.04	0.23	-0.25	0.16	-0.21	0.12	-0.02	0.07	0.35											
perform satisf	-0.53	-0.13	-0.38	-0.6	-0.57	0.19	-0.18	0.02	-0.08	0.32										
easy insur	-0.6	-0.34	-0.19	-0.38	-0.2	0.13	-0.24	-0.1	-0.12	0.31	0.65									
premium	-0.08	0.17	0.1	0.3	-0.06	0.12	0.04	0.12	0.02	0.41	0.12	0.28								
easy main	-0.08	0.23	0.37	0.18	-0.08	0.03	0.02	0	-0.47	0.08	0.08	0.3	0.52							
cust satisf	0.29	0.07	0.3	-0.08	0.18	0.14	0.14	-0.06	0.14	-0.16	-0.09	-0.03	-0.25	-0.35						
revenue share	-0.23	0.08	0.23	-0.3	-0.03	0.36	0.37	-0.47	0.01	-0.03	0.32	0.27	-0.09	-0.09	0.28					
upfront cost	0.04	0.14	0.03	0.04	-0.07	0.06	0.36	-0.45	0.17	0.1	-0.07	-0.15	-0.16	-0.11	0.15	0.46				
integrat score	-0.16	-0.3	-0.14	-0.34	-0.25	-0.05	-0.29	-0.33	0.12	-0.14	0.2	-0.01	-0.02	-0.24	-0.23	-0.07	0.03			
supp satisf	-0.42	-0.33	-0.59	-0.52	-0.24	-0.37	-0.22	0.12	-0.15	-0.07	0.36	0.19	-0.45	-0.4	-0.02	-0.07	-0.06	0.26		
api provided	-0.1	-0.21	-0.5	-0.02	-0.21	-0.02	0.1	0.28	0.42	0.3	0.22	0.1	0.05	-0.43	0.17	-0.11	0.05	0.26	0.41	
solution exln	0.04	0.05	-0.35	-0.08	-0.15	-0.12	0.02	0.27	0.24	0.26	0.19	0.1	0.04	-0.08	-0.05	-0.16	0.13	0.14	0.39	0.56