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How insurance and financial-services firms facing disruption can innovate and thrive

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EXECUTIVE SUMMARY

In an era of disruption, financial-services firms — and insurance companies in particular — need a shift in their approach to strategy. Developing and implementing a successful strategy in a nonlinear, fast-moving world can be easier than you think — if you focus in an active, iterative way on three core elements:

Portfolio: Which of your businesses deserve funding — and which don't

Innovation: How well your organization is set up for experimentation and success in new ventures

Stewardship: How you direct resources toward your most important capabilities, to steer the business into the future

Your whole approach to strategy should focus on these three elements — and nothing else. Forget traditional notions of strategic planning. Out with the slavish adherence to operating models and organizational design. Ignore the relentless pressures to upgrade every platform and system. Put all your strategic activity in service to those three elements: portfolio, innovation, and stewardship.

Resist thinking of strategy in terms of governance and top-down control. Instead, think of yourself and your top team as innovative stewards of the right mix of business lines, equipping the organization with what it needs to deliver profitably. Simplify your thinking in this way, and the rest — including how you deal with technological disruption — will fall into place.

The only good strategy …

… is one that's implemented. If a strategy can't be put in place and maintained, it's not worth the trouble and expense of putting it together. Companies must ensure that strategy and implementation stay aligned as facts on the ground change.

This has become a matter of urgency for the financial-services industry, and for the insurance sector in particular. One symptom of this is the statements we hear over and over from executives:

> *We're concerned about disruption. If we don't reposition ourselves soon, it will be too late to react.*
>
> *We need to get closer to our customers.*
>
> *We need to move faster and with more agility.*
>
> *We need to figure out digital and innovation.*
>
> *We need to move to the cloud.*
>
> *We're not spending in the right places, and we might need to spend less overall.*
>
> *We're trying to be good at everything, and that's just not realistic.*

All these statements are reasonable, and all have strategic implications. But they don't get to the heart of the issue that is vexing financial-services firms. The problem is not that the world has changed; it's been changing for many years. The problem is that the map is muddled: There are too many options, they involve too many uncertainties, and worst of all, they aren't distinctive enough. Because they seem to apply to all companies equally, they aren't highly suited to any.

In short, decision makers in insurance and banking are overwhelmed by a high noise-to-signal ratio in their assessment of challenges and opportunities. They continue to make many methodical strategic plans, and execute most or all of them, because they aren't sure what to give up. Yet they also know that the world is moving too fast for this approach.

Their situation is made more complex by the nonlinear nature of business today. Small issues lead to big headaches. Minor resources turn out to have major impact. Straight-line projections turn out to be inaccurate. Plans that feel right don't lead to success. These are all symptoms of nonlinear trends — forces internal and external that accelerate or slow down in unexpected ways and that therefore prove unpredictable. The business structures, practices, and supporting mechanisms built for more straightforward, predictable times just don't work in the age of disruption.

Yet it's not obvious how to reform or replace those old strategic approaches. Financial-services companies — and insurers in particular — are huge enterprises subject to more constraints than most. They must deal with heavy regulation, the obligation to support products sold half a century ago, and a culture generally more attuned to compliance than innovation.

To create and execute strategy in today's fast-moving, volatile environment, companies need a focused approach that will let them quickly develop new organizational muscles and reflexes. We're not suggesting companies discard their best practices wholesale. But they do need to think differently about the structures and mechanisms they rely on to develop and carry out strategy.

Crafting a streamlined strategy

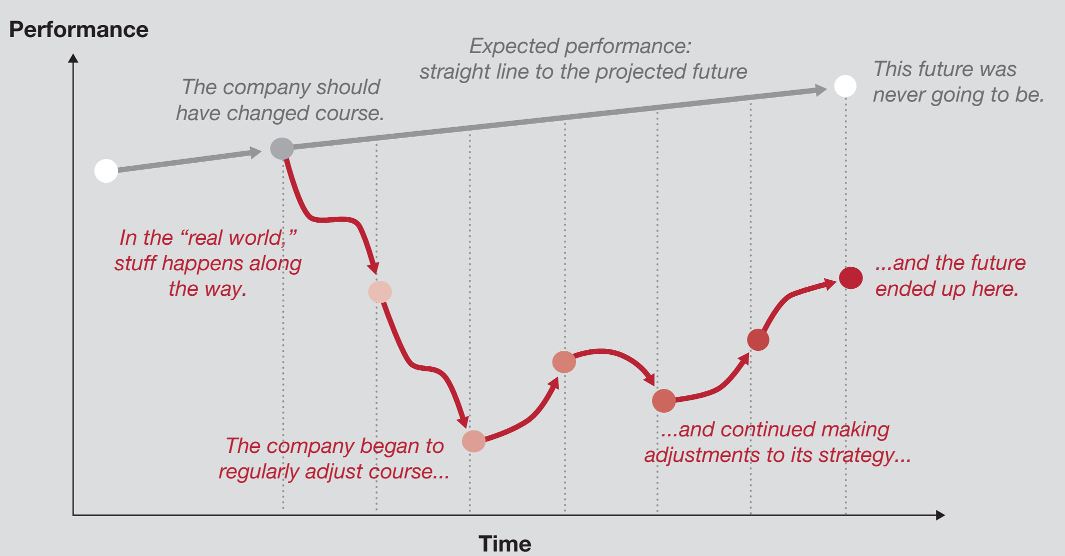
Fool's errand: sending a novice off in search of something that can't be found or is pointless; for example, dispatching an apprentice to the store for a bucket of striped paint.

In our 2018 article in *strategy+business*, "The Insurance Industry Needs an Intervention," we explained why many financial-services firms aren't getting the results they need. Indeed, if you're a leader of an established insurance company, you've probably already found that the traditional levers for executing strategy — textbook moves such as fine-tuning marketing programs, updating products, enhancing customer-service systems, and beefing up information technology — are not well-suited to the challenges you face. The source of your problem is, more likely than not, in the way these interventions fit together. As you manage each of the "trees" of the organizational interventions you have in mind, you lose sight of the "forest": the main thing you're trying to accomplish.

In essence, strategy is figuring out where to apply limited resources in order to capitalize on opportunities. But determining where to apply those resources — to answer the questions "What businesses are we in?" and "What capabilities do we need to compete effectively?" — has become a moving target. In a nonlinear world, a good strategy is not one based on a straight line to some supposed future — a future that likely will never come to pass. A good strategy adapts to ever-changing facts on the ground (*see Exhibit*).

EXHIBIT

A good strategy adapts to the continual change of a nonlinear world



Source: PwC's Strategy&

Think of the real world as a game of gin rummy: Every time you draw a new card you need to optimize your hand. As facts on the ground change, you adjust your awareness of them and your sense of the whole. You can do that only if you are willing to play a limited number of cards, a few that represent the whole system you're trying to manage — and play them well.

In other words, this type of adaptive success requires a streamlined, focused approach to strategy. You will need a clear idea of the businesses you are in, the brands you own, the way you're organized (including whom you partner with and how you structure your financial and legal entities), and how you distribute your products and services, all fitting coherently together.

When you streamline your strategy, you reconsider the structures of your enterprise: the mechanisms, practices, and relationships through which you distribute, sell, operate, and manage. These structures must not only fit together to advance strategy but must do so without distracting or diverting your focus, or otherwise wasting time. You can't adapt to 21st-century conditions without simplifying your 20th-century structures. Cut away the weeds and bramble; reduce the noise and confusion.

You don't just streamline because of rapid change and disruption. Your goal is to set your company apart from others. If you chase every trend that comes along, your strategy will probably look much the same as your competitors'. When you aren't disciplined in streamlining your strategy, you fall into old habits, continue with the same projects, and renew your budgets year after year. Your future resembles your past, and your costs remain just as high. Instead of executing strategy this way and acting the same way your competitors do, focus on what sets you apart from them. Focus in particular on the three elements of a differentiated strategy: your portfolio, your capacity for innovation, and your stewardship.

"You don't just streamline because of rapid change and disruption. Your goal is to set your company apart from others."

Portfolio. Executives often address strategic planning and their portfolio of businesses as two separate issues, giving short shrift to the latter. In theory, strategic planning is fine; but as boxer Mike Tyson famously noted, “Everyone has a plan till they get punched in the mouth.” In practice, strategic planning is often geared toward traditional, ingrained spending habits. Businesses — other than those that are hemorrhaging red ink — keep getting funding simply because they exist.

But why not approach strategy with a zero-based mind-set? Find ways to shutter the businesses you should no longer be in and shift scarce resources away from those that are subscale (too small to compete effectively). To reinforce the importance of being flexible and adaptable, shift your focus away from strategic planning and toward managing the portfolio: Invest in the businesses that will give you the capabilities you need to realize your strategy.

“The tried-and-true processes and practices by which many leaders govern — annual budgeting, cost-benefit analyses, project gating — are no longer reliable for putting the money where it needs to go.”

Innovation. In an unpredictable, nonlinear world, better ideas come from having more ideas. Playwright and political activist George Bernard Shaw, who observed that “imagination is the beginning of creation,” also said, “A life spent making mistakes is not only more honorable, but more useful than a life spent doing nothing.” Creating a culture that fosters new ideas and that encourages trial and error and rapid course correction will likely succeed over continuing one that plans everything out and expects predictability.

Stewardship. In our conversations with company executives, we discovered that many have a de facto strategy: to keep doing what they’ve been doing, only better. The reasons for this vary, but the most common is institutionalized planning processes, which tend to entrench habitual spending; pay lip service to longer-term, off-cycle investments; and discourage ideas that require change.

The tried-and-true processes and practices by which many leaders govern — annual budgeting, cost-benefit analyses, project gating — are no longer reliable for putting the money where it needs to go. They’re legacy approaches, designed for manufacturing or production efficiency, rather than for innovation, customer focus, and speed. In addition, many of the challenges that companies face today, such as creating a new product or revamping the customer experience, require a cross-functional and cross-product response. That is hard to achieve with traditional — especially siloed — organizational structures and operating models.

Governance implies oversight and maintenance, leading by reinforcing established ways. Instead of governing, steer toward your desired future. An ethic of stewardship — the conscious allocation of resources, including executive time and attention, to your most important capabilities — will help you steer in new directions and find new means of operation.

Let’s take a deeper look at these three elements and how they interconnect.

Think portfolio

Consider the portfolio on three levels: which businesses you should keep or exit, which operating model you should follow, and which capabilities make you stand out in the eyes of your customers and distributors.

Which businesses? Scale has become an increasingly important condition for success, in the near and long term. We define scale as the sheer heft or technological might to deliver your products and services at a level of efficiency and effectiveness that rivals the market's best players. In many industries, technology enables a rapid trajectory from startup to market leader, making the winner-take-all effect much more common. Scale should therefore be a foremost consideration in deciding which businesses you should keep.

Many companies don't have the basic portfolio they need for their strategy. Even leaders who understand the value of making portfolio adjustments tend to think first of buying, when selling is sometimes the better move. They also tend not to think about how the maturity of their business and its prospects should affect their decision making. For example, there's no point in fully integrating a business you might sell off or close down. It may be smarter to starve it for short-term profit or invest in it to get the best sale price. And if the timing for a deal isn't right, the lessons you learned while making this decision can still influence your other strategies.

What kinds of portfolio decisions should leaders contemplate? For starters, they should consider spinning off product lines that no longer serve the company strategically or practically, that represent a steady drain on resources, or that entail onerous capital requirements or regulatory constraints. That money can be put to better use funding a more core investment, initiative, or activity. You might invest in a new business to gain scale, enhance distribution, or diversify further. You might consider outsourcing certain key functions if doing so would improve economics or give your company access to better capabilities. Finally, there's partnering — through an equity investment or joint venture — to create or gain access to capabilities that are not available through acquisition or that would be too difficult to build organically.

Which operating model? The notion of core capabilities is relatively simple. Understand what you're good at, leverage it, and win in the marketplace. However, if you're not good at it, or if you can't do it better than your competitors, look to a third party. There are many well-known examples of companies that outsource their IT, call centers, investment management, claims settlement, or underwriting. Perhaps a joint venture is the way to get the capabilities you need.

Consider other aspects of your operating model. Do you have the right legal entity and capital structure in place? Are you sharing the functions you've built internally to optimize scale, quality, and control? Does your organizational design fit your purpose?

Which capabilities? How are you leveraging the things you're good at into marketable capabilities? We're thinking of such capabilities as enabling customers to view their accounts; get needed information; and manage transactions as they want, when they want, and through the channel they want. Also, evaluate your ability to understand your customers: who they are and what their behaviors and preferences are in shopping and transacting. You may also need to improve how you hire and cultivate the right employees to build, expand, and hone these capabilities.

Today, an integral element of any company's strategy is its ability to adapt rapidly. Your capabilities are only as good as your ability to keep them sharp and up to date. Although disruption hasn't hit the insurance world as hard as it has other industries, insurers are hardly insulated from it.

Finally, having the right capabilities is often about acquiring them, which could mean buying up potential threats in markets you've dominated. Take, for example, Sun Life's acquisition of Maxwell Health, an absence management software company. Together, these companies have created a carrier-distributed technology platform that offers services and features including payroll, human resources management, online enrollment, administrative dashboards, and mobile apps. Or consider the deal in which Reinsurance Group of America (RGA) acquired LOGiQ3 Group, which enabled RGA's innovation and digital business unit to ramp up its technology, consulting, and outsourcing services for life insurance and reinsurance enterprises. Both examples illustrate how companies are making acquisitions to venture into new adjacent areas that not only promise added value to clients but are potentially disruptive.

"Your creative energy and IT budget should go into developing more comprehensive, more distinctive digitally enabled capabilities that will make you stand out and position you to compete."

Think innovation

Every business needs discipline in how it's organized: in its business models, processes, organizational design, IT infrastructure, data management, and so on. Every company also needs rock-solid professionals to manage these organizational elements. But this discipline can come at the expense of innovation.

Often, these well-meaning architects of organizational design issue standards and rules that make components too expensive, too complex to maintain, and ill-suited for anything but a static environment. Executives often get dragged into or paralyzed by decisions about pruning the trees instead of strengthening the forest.

For example, you will gain no competitive advantage if you limit your IT choices to vendors of immediate solutions. These lead you to "table stakes" systems — systems that fulfill your immediate business needs but don't set you apart from competitors. Nor should you devote energy to enhancing these relatively limited systems. Instead, your creative energy and IT budget should go into developing more comprehensive, more distinctive digitally enabled capabilities that will make you stand out and position you to compete.

Why are table stakes systems so similar? Because financial-services companies are generally similar in their operating models, technological capabilities, operational capabilities, and even strategies. Every insurer needs a claims system, policy system, and financial system. Every company must be able to serve customers where they want to be served; provide value to its distributors; have the right technology in place to support better decision making; operate at scale with competitive economics; and maintain security and control. You may need to invest in these systems, but you should manage them either for differentiation — making them part of your unique, strategically relevant capabilities system — or for cost, gaining the functionality you need with as little money, time, and attention as possible.

In the end, one thing becomes painfully clear. All too often, the strategic activities in your company — deliberation, prioritization, project formulation, and funding approval — are devoted to these table stakes activities. They inevitably drain money, time, and attention from the significant innovations you need to make, in the areas where your enterprise can set itself apart from competitors. If you have the opportunity to reduce these draining activities or cast them aside, don't wring your hands. Think of these cuts as the inevitable measures you have to make to become truly competitive.

Focus on speed and flexibility. In times of rapid change, companies need to move quickly, using agile work processes, to compete. Speed is important in the insurance sector, whether you are starting a greenfield business with a simple product, as Atlanta-based Haven Insurance Group did with its online term life-insurance sales system; enhancing customer experience, as Idea Bank did with branches on commuter trains; or distinguishing your offerings with new services, as some companies are doing with financial and health wellness programs that lower insurance rates.

Flexibility is also important. You need to focus continually on the specific capabilities they have defined to meet market needs in real time. This imperative has profound implications on your stewardship: on annual planning and prioritization, how you approve and fund specific initiatives, and even the ways in which you deploy your workforce.

Some large companies, for instance, are tapping freelancers to fill intermittent or specialized needs. Some are providing digital training to employees and introducing more agile, less hierarchical structures. In this form-follows-function approach, companies can deploy ad hoc teams for single-purpose projects, and long-standing teams can employ agile work methods and self-governance to meet evolving needs.

Set your organization up for innovation. Bet on experiments that will generate new ways of doing things that are likely to solve problems or create opportunities. In fintech and insurtech, companies are toying with innovations in discrete segments in the value chain, such as robo-advice, personalized insurance, and automated underwriting. New medical advances such as predictive medicine and wearable devices, and health improvements such as decreasing morbidity and mortality risk, present opportunities for innovation in other parts of the value chain. These new solutions can be hatched in a number of ways. Some leading companies have formed an innovation arm. Others are investing in startups, which gives them ready access to new ideas about how to operate. Still others are creating "tiger teams" or pilot programs to test new ideas or approaches.

Think of your business model and the way the business is organized as you would think of a modern-day patent series, with each new entry building on a previous innovation already in place. Because the basic elements of the financial-services ecosystem are heavily regulated and well established, innovation — and indeed disruption — can happen only within the basic structure of the existing ecosystem. Those areas of the ecosystem are increasingly well supported by technology; plug-and-play systems, such as cloud-based software environments, are already available. The upshot: Innovate only in areas where you can have impact.

Think stewardship

Many business leaders seem to practice management by maintenance. They solve problems that come up in the most expedient way, not by marshalling their company's scarce resources — its people, technologies, financial capital, and management attention — in a way that steers the business toward the future. Instead of thinking of yourself as a maintainer of the business or a facilitator of the governance of the enterprise, consider yourself a steward.

Stewardship refers to a managerial approach in which you continually direct resources, including your own time and attention, toward your most important capabilities, the ones that will make or break your strategy. You thus steer the business into the future. This is a more apt way to think about how you organize your enterprise. It's forward-thinking; it suggests driving innovation in a way that *governance* does not. As a steward of the strategy, you are in charge of mobilizing, prioritizing, funding, and executing. Through these efforts, you define and build your most important capabilities, now and in the future.

Leaders need to be able to discard best practices or policies that obstruct or hinder innovation. They need license to pursue new ways of working and to bend the rules when justified. The concept of stewardship suggests this is not only OK but desirable.

For example, it's important to let silos intersect or overlap, because you need to give precedence to getting the right people and the right expertise on teams without requiring a Herculean effort. Digitizing the customer experience requires coordination across products, customer segments, and functions. Sales and distribution are probably better organized from the customer perspective than by product or geography, as they often still are. Yet none of these necessarily calls for deconstructing the org chart.

At the same time, a stewardship approach could also lead you to stick with the status quo. Maybe one or more of your businesses is a cash cow that requires only a modest investment to stay the course. Perhaps in a new market or product area, the threat of disruption isn't high because of barriers to entry such as capital or regulatory requirements. Sometimes there is no first-mover advantage; or, like the dinosaurs, you don't see the meteor coming, and even if you did, you probably couldn't prepare for it.

“Leaders need license to pursue new ways of working and to bend the rules when justified. The concept of stewardship suggests this is not only OK but desirable.”

Balance your IT dollars. Given technology's outsized role in the platforms that power financial-services companies, determining how to fund IT for the short and long term may be among your most difficult decisions. The executives we talk to generally have a firm understanding of technology's trajectory and how customer needs are evolving. They've thought through potential strategies that would position their key assets for capability and versatility. But they tend to go astray in separating day-to-day incremental improvements from long-term strategic moves. They shortchange the platforms and systems that will enable their strategy — say, great customer interaction mixed with a high-service model for distributors and the best information money can buy.

All the technologies and platforms that run the business — for example, those that handle data, data integration, analytics, and related innovations — must be funded at reasonable levels for the foreseeable future. These are table stakes that enable every strategy at expected levels of market performance, so they must be part of the planning and funding model. But funding only the status quo will not advance you. Surprisingly, some companies behave this way, pretending to adopt the latest customer-experience approach without a tangible commitment to establishing the supply lines needed to create that capability.

A short-term focus can be insidious. Companies spend a huge chunk of their IT investment on business-as-usual tweaks or minor improvements to eliminate workarounds or keep up with compliance requests. Then, as systems and platforms age and the patchwork fixes build up, the technologies become so tangled that they can no longer support the business strategically. They can no longer help it grow and improve service or efficiency, let alone become more profitable. This problem even has a name: technical debt.

A longer-term view gives companies the flexibility they need to build the most urgent capabilities on an ongoing basis to respond to the typically fine-grain, customer-driven demands.

Tie your blueprints and road maps to the strategy. These tools delineate the capabilities and actions required to achieve your vision. Blueprints define the functions and business capabilities needed to make the strategy happen, including how departments and people must interact. Road maps outline how a plan might unfold, noting the broad steps and their prerequisites, and spelling out alternative routes if the sequence of actions changes.

Together, blueprints and road maps convey at a high level what it will take to get something done, roughly how long it will take, and what the interdependencies are. They formalize the need to maintain technology that supports the capabilities. They also help set a rational spending level, based on the capabilities' relative urgency and importance to the business and other stakeholders, including regulators.

Invest in platforms and partners for the long term. Products, customer expectations, and technologies may change rapidly. Regulations, however, do not. In financial services and insurance, with their heavily prescribed processes, regulated product design, and mandated reporting requirements, the value chain resists rapid change.

This gives you an opportunity to set a time horizon for your strategic capabilities investments, determining how long they are expected to operate. In other words, you can invest rapidly, leapfrogging your competitors' capabilities. But once the new system is in place, you can move more slowly, knowing that you are keeping up with your industry.

Base all decisions about strategic investment on a considered view of the time horizon. This affects IT systems such as enterprise resource planning or cloud development, as well as strategic partnerships such as joint ventures or outsourcing relationships. For example, fundamental technology platforms — the call center platform; core policy- and claims-processing systems; assets for storing, analyzing, and modeling data; HR systems; financial reporting systems — can have a fairly long shelf life.

“This time-horizon approach is so logical that it should become standing best practice in the industry. Unfortunately, it conflicts with some of the so-called best practices in project funding and project management.”

Once you have a rational acquisition and replacement strategy established for these major components, don’t let them stagnate. Rather, set up agile teams to modify and improve functionality as needs evolve. These standing agile teams can get more skilled at what they do and thus can keep in sync with the business’s ongoing and high-priority needs. Supporting applications and platforms can be continually developed: Iterate them to incorporate innovative change and to deliver products and services to the market with increasing speed, while still treating them as long-term assets and aspects of your core capability.

This time-horizon approach is so logical that it should become standing best practice in the industry. Unfortunately, it conflicts with some of the so-called best practices in project funding and project management that companies have zealously adopted in recent decades. Those practices came with unintended consequences: overhead bloat; inadequate skill building because teams are organized for one-time use, which also drives up costs; and a bias against funding projects that lack an immediate payoff, such as future-building platforms. Ultimately, some of these practices only encouraged more technical debt. Generally speaking, they were designed for yesterday’s challenges, many of them for a slow-changing environment. And yet companies continue to follow them, despite the fact that they can grow stale and outlive their usefulness. (See Bruce Brodie, “Best practices in insurance and beyond: It’s time to stop looking backward,” PwC US, 2017.) Now there is an opportunity to change them.

Focus on essential strategic assets. The old project-based approach favored whatever short-term needs seemed urgent and important. Instead, by establishing strategic platforms, companies can make tactical, short-term service or efficiency improvements and support the ability to build long-term assets and capability. A scaled agile framework, such as Agile/SAFe, used for lean enterprises, core systems, and applications, can help simplify annual planning, funding, and gating processes while enhancing the long-term view of controls and security for platforms.

Companies need to be able to uphold their promises to customers and remain viable — while also playing the cards in hand in real time. A stewardship approach lets you make rational choices about your operating model — choices such as large-scale automation or AI as part of your digital transformation — informed by an understanding of the many customer journeys you serve (including college funding and retirement investments) and the critical moments of specific customer interactions.

Achieving efficiencies, making more informed decisions through analytics, getting closer to the customer — there’s no either/or in these actions.

Does your strategy have a shot?

In today's fast-moving business environment, leaders are constantly bombarded with calls to update, upgrade, and optimize everything, including product design, analytics, and customer service and technology platforms. Cutting back on high-profile initiatives whose value may have withered can be seen as impolitic. If you don't follow every best practice that your competitors have, the implication is you could be sabotaging competitive advantage.

Banking and insurance are not immune to disruption, so keeping abreast of change is critical. Moreover, your major areas of capability in financial services are circumscribed by customer needs, product life cycles, distribution requirements, and regulation. There's simply less opportunity to set your company apart.

But it's easy to lose sight of a basic truth: There's no payoff in fine-tuning capabilities that won't differentiate your company. Strategic success requires a streamlined response. Companies need to focus their energy, attention, and resources on the things that will give them a competitive advantage. Leaders need to focus on the business portfolio to be sure investments are being directed to the businesses that will deliver the essential capabilities. Instead of worrying about table stakes business models, processes, infrastructure, and systems, concentrate on how well the organization is set up for innovation. Rather than managing by maintenance, think about stewardship — about steering the business toward the future.

This means having a longer-term view that properly establishes the platforms essential to supporting the strategy. In that way, you can prioritize the most urgent capabilities on a continual basis to fulfill more short-term market demands.

To determine whether your strategy has a shot at being implemented, ask yourself (and other members of your top management team) these questions:

- Do you have the scale and resources to support all the businesses you are in?
- Can you articulate your strategy in a way that sets you apart to customers and distributors?
- Are you directing scarce resources in the right places to create those capabilities that will set you apart?
- Are the strategic technology platforms in place that will let you build that differentiation?

If you didn't answer "yes" to all four questions, you need to change your approach to strategy. Remember, as facts on the ground change, you need to keep strategy sharp and implementation aligned. You can do that only if you are willing to play a limited number of cards and play them well.

Strategy&

Strategy& is a global strategy consulting business uniquely positioned to help deliver your best future: one that is built on differentiation from the inside out and tailored exactly to you. As part of PwC, every day we're building the winning systems that are at the heart of growth. We combine our powerful foresight with this tangible know-how, technology, and scale to help you create a better, more transformative strategy from day one.

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