10 – Insurer Strategic Management

**1 – Strategic Management Process**

**Objective**: Summarize the stages in the strategic management process

The strategic management process is critical to any organization’s success. Effective strategic management is especially important for insurer because they must distinguish themselves in a highly regulated business where products may not widely vary. Organizations can be successful in the long term if they have effective strategies that efficiently deploy resources. Therefore, the heart of any successful business strategy is the alignment between the internal resources of the organization and external factors. This alignment allows an organization to create a sustainable competitive advantage.

**The strategic management process involves three interdependent stages:**

* **Strategy formulation – creating a plan**
* **Strategy implementation – putting the plan into action**
* **Strategy evaluation – monitoring the results to determine whether the plan works as envisioned**

**Strategy Formulation**

Strategy formulation depends on an organization’s mission or value statements. Throughout the strategic management process, the statements should serve as a focal point for the organization’s management and board of directors.

* Mission and Vision Statement – A mission statement is a broad expression of an entity’s purpose or goals which reflecting the entity’s character and spirit. It specifies the products or services the organization provides, its stakeholders, and what is important to the organization. **For insurers, mission statements frequently mention financial strength, customer service, and integrity**. The mission statement may also include, or be accompanied by, vision or value statements that provide additional information about company values or principles important to the organization, such as integrity, honesty, customer focus, flexibility, and compassion.

**Strategy Formulation Steps**

**Considering the organization’s mission and vision statement, board members and senior level executives develop strategies through a three-step process.**  Although business theorists differ over the labeling and numbering of the steps (and some divide individual steps into more than one), strategy formulation has these basic components:

* **Analysis of external and internal environments**
* **Development of long-term strategies and organizational goals**
* **Determination of strategy at different organizational levels**

**The first step of strategy formulation involves an internal analysis of the organization and an analysis of external factors including competitors, current and prospective customer’s needs, the current and anticipated economy and government regulations**. Typically, a SWOT analysis may enable executives to **determine how receptive the market would be to its products and services and its competitive position within the market**. Opportunities can be categorized as those the “can” or those that “should” be pursued. With this approach, the framework for strategic plan begins to emerge.

**The second step in the process involves development of long-term strategies and organizational goals to support the mission statement within the framework developed during the analysis step. Goals should reflect an understanding of its identity, customers, and purpose.**  Companies establish these goals to set priorities or direction for the organization, to establish a measurement of success, and to align its people and actions.

Normally, the Chief Executive Officer (CEO) and executive officers will develop these strategies and goals, often with input from the board and operational-level managers. Then this group of management will develop short-term financial objectives that are aligned with long-term strategies and goals.

**The third step is to determine strategies at different levels of the organization. This involves agreement on more specific action and delegation of responsibilities to achieve long-term strategies and goals. These strategies are based on an organization’s core competencies, the competitive nature of the business, the potential customer base, and other factors.** This step on the strategic management process involves formulating the “who”, “what”, and “when” responsibilities.

**Strategy Implementation**

The second stage of strategic management process is strategy implementation, also called strategy execution. Strategy implementation is the process of making strategies work. In relation to the strategy formulation, this stage is more difficult to complete and requires more time.

**The first consideration and crucial component of strategy implementation is designing the structure of the organization**. The most appropriate organizational structure for a company will be determined by its strategic goals. In a single-business company, a functional structure might be most suitable, with departments defined by the operation they perform (such as Claims, Underwriting, and Marketing and sales). **A diversified company (one that is categorized by geographic regions and has departmental operations within each region) is more likely to use a multidivisional structure to organize its operations and to segregate each division into separate profit centers**.

**Other possible structures organize company operations by region or by type of product or customer**. Such as commercial, marine and personal lines. This way the expertise and resources required for specific customers is concentrated within the related department. This approach supports a differentiation strategy, which the company seeks to provide unique products for specific market segments.

Structure can also determine the reporting relationships or the company’s level of vertical differentiation, which is the extent to which an organization is stratified from its lowest to highest level. Some companies are tall organizations, with many levels between functional-level positions and executive-level positions. Conversely, a flat organization has fewer levels from the top of the organization to the bottom. When following a cost leadership strategy, a flat organization helps to eliminate costs related to maintaining multiple reporting relationships within the company.

Companies should also decide what degree of centralization is needed to operate efficiency and to meet organizational goals. The degree of centralization determines whether authority is maintained at top levels or is delegated throughout headquarters, into regions, or even to the local level. For example, some insurers retain underwriting authority at the headquarters level, while others extend it to local offices or to managing general agents.

Ultimately, the entire organization is responsible for successful strategy implementation. However, the plans for implementation begin with a filtering down process, where organizational goals are communicated by top management.

Strategy Implementation Steps

Mid-level managers are typically responsible for strategy implementation an may follow these five steps:

* Create a documented roadmap of the specific processes, tasks, and responsibilities necessary to disseminate the corporate strategies throughout the organization.
* Communicate information regarding the strategies clearly, frequently, and completely throughout the organization.
* Assign specific responsibilities, tasks, authority, and accountability throughout the organization
* Allocate adequate resources for successful implementation. Resources include finances, staff, training, time, equipment, data, and technology
* Manage variances between the goals and the mid-year results; make necessary adjustments to achieve the goal.

**Strategy Evaluation**

**Strategy evaluation, also called strategic control, provides a method for measuring a strategy’s success**. Control mechanisms allow management at each level to gauge the progress of the integration of established strategies into the organization’s activities and toward achieving the goals that have been set. **The control process has 4 steps**:

* **Establish Standards** (example, setting a combined ratio of under 100)
* **Create and apply measurements** (example, compiling all premium, expense, and loss date required to develop a combined ratio figure, as well as determining a format to report the data)
* **Compare actual results to standards** (inherent part of this process is or managers to communicate the importance of meeting this standard. The reports would then be used in comparing actual results to establish standard of a combined ration under 100. If the standard has not been met, managers need to determine the reason and implement changes)
* **Evaluate and implement corrective actions if goals are not met** – depending on the results of this comparison, corrective actions might involve training initiative for employees, strengthening communications with producers, examining marketing activities, or taking other corrective actions. If the goal has been met, management should reward and recognize all employees involved to provide motivation to achieve future goals.

Theses are categories of organizational controls that may be used to monitor goals

*Financial controls* – in the insurance industry, loss ratios, expense ratios, and combined ratios are financial controls typically used to evaluate overall corporate performance. They also measure the performance of business units, regional offices, and individual books of business. Other financial controls include stock price, return on investment formulas, cost/benefits analysis, or budget measurements.

*Operational or process control* – these include processes to monitor work flow, production processes, and customer service. In an insurance claims department, such controls could include the average cost of settlement, average case load per adjuster, or file turnover rates for individual adjusters.

*Human or behavior controls* – This category includes rules, policies, and procedures that provide operating guidelines for employees within an organization, including measurement of individual performance.

As a result of evaluation, strategic plans may be reformed, and/or the manner in which they are implemented may need to be adjusted. The evaluation may indicate that results are off target in ways that cannot be addressed through moderate adjustments. Or it may reveal that the plan’s concepts were not completely connected in the implementation state, which requires an adjustment to the implementation approach.

**2 – The Five Forces and SWOT Methods of Analyzing the Environment**

**Objective:** Explain how the Five Forces and SWOT methods can be used to analyze the environment in which an insurer operates.

An insurer’s success depends on its ability to analyze changing environmental factors and influences and to formulate sound business strategies based on its analysis.

Insurers rely on the strategic management process to achieve long-term goals. Strategy formulation is a crucial component of the strategic management process and involves the interrelated steps of analysis of external and internal environments, development of long-term strategies and organizational goals, and determination of strategy at different levels.

**In the first step of the process, managers consider factors in both the general environment and the task environment. The general environment affects all businesses regardless of the specific industry in which they operate, and includes demographic sociocultural, legal, technological, economic, and global factors.** *The task environment, which includes an organization’s customers, competitors, and suppliers, describes the environmental factors specific to the industry in which the organization operates*. The task environment for an insurance company might include customers, competitors, suppliers, reinsurance providers and regulators.

Many methods can be used to analyze the environment in which an organization operates. Two commonly used methods are the Five Forces Model and SWOT analysis.

**The Five Forces Model**

**The widely used Five Forces Mode**l, developed by Harvard Business School professor Michael E Porter, **deals with the external task, or competitive, environment and is often used to analyze customers, competitors, and suppliers**. Porter describes 5 forces that drive competition:

* **Threat of new entrants**
* **Threat of substitute products of services**
* **Bargaining power of buyers**
* **Bargaining power of suppliers**
* **Rivalry among existing firms**

**By analyzing these forces and their effect on the organization, managers can better understand their company’s position in the industry. This increased understanding allows management to construct strategies that build a competitive advantage**.

**Threat of New Entrants**

The threat of new entrants in a market is one force that drives competition, although the strength of this force depends on how difficult it is for outsiders to enter the market. Barriers to entry include economies of scale, which contribute to lower overall costs by decreasing the unit costs of products as volume increases. Such as homeowner’s policies through technology. The standardized nature of personal insurance policies allows some insurer to use automated processes to issue large numbers of policies with relatively low overhead costs. These insurers have lower expenses than insurers relying on more labor-intensive processes, allowing them to charge lower premiums and thus raise barriers to entry for this market segment.

Insurers can also raise barriers to entry by offering unique products or services through the establishment of leadership in certain distribution methods (long term relationship with producers or creating an online direct application system known for its ease of use) or by having established advertising or group marketing programs. The ability for one insurer to access distribution channels in a marketing system can crate barriers to entry for others and pose a competitive disadvantage for new entrants. For insurance products, the insurance distribution system and channel can be important components for the overall marketing plan.

State statute and regulatory policy can act a s a barrier to entry if they deter potential entrants from considering the highly regulated insurance industry. Regulatory requirements within a given jurisdiction can also discourage insurers from entering certain states. (Example, Massachusetts once discouraged new entrants to the personal auto market with state made rates and restrictions on distribution)

**Threat of Substitute Products or Services**

A second force that drives competition is the threat of substitute products or services. This threat arises when products that are capable of performing the same function as those from another industry become widely available. This threat makes it difficult for any one seller to substantially increase prices and tends to hold down profits for all participants in the original industry.

The threat of substitute products or services to the insurance industry has been limited thus far but remains an important force for insurers to consider. One example of such a threat is alternative risk transfer mechanisms including self-insured retention, formation of captive insurance companies, catastrophe bonds, and finite risk transfer.

**Bargaining Power of Buyers**

When buyers have significant power, they can increase competition within an industry and demand lower prices. This force affects the insurance industry, principally in the personal insurance market, in which customers have exerted great pressure on insurers to lower prices and increase availability. The bargaining power of buyers is the reason that many government-sponsored or mandated residual market plans were created. Auto assigned risk plans and property insurance plans (particularly those serving coastal markets) were create where the market would not support eh prices needed for insurers to voluntarily offer coverage. Further, the bargaining power of buyers led to the explosive growth in the number of coastal property insurance plans and wind pools as property owners would not, or could not, pay rates sought by the private market.

When formulating strategy, companies should consider customer buying power. In some cases, insurers might decide not to enter markets where they feel pressure from buyer groups would inhibit their ability to be profitable.

**Bargaining Power of Suppliers**

In some industries, suppliers can exert power over companies by increasing prices, restricting supply, or varying product quality.

In the insurance industry, reinsurers are a supplier to primary insurers. Without access to reinsurance many insurers would lack sufficient capacity to write certain types and amounts of insurance. Reinsurers are in a position to control the price and amount of capacity they provide depending on the market conditions. For example, in periods when large losses occur, such as multiple hurricanes, reinsurance capacity may shrink. Insurers may also underestimate anticipated loss amounts from such events. Such uncertainty in the marketplace generally results in tighter capacity, rising rates, and more restrictive terms.

Another example of bargaining power of suppliers is the power exerted by auto manufacturers to mandate use of original equipment manufacturer (OEM) parts for auto physical damage repairs. Physical damage loss costs increase for insurers.

**Rivalry Among Existing Firms**

Rivalry is reflected in pricing wars, aggressive advertising campaigns, and increased emphasis on customer service. Competitors are constantly striving to be at the top of their industry and to outperform other companies. Example, Geico v Progressive rivalry among personal lines auto insurers

A high level of competition can be expected in industries having many companies, little product differentiation, or high exit costs. All of these characteristics are present in the insurance industry, making the market strongly competitive. While some insurers can use economies of scale to gain a competitive edge, the individual market share of insurers at the top of the market is still relatively small compared to that of other industries. No single insurer has enough market share to dominate to overall property-casualty market.

**SWOT Analysis**

**SWOT analysis, or situational analysis, is another method used to analyze the competitive environment. SWOT (Strengths, Weaknesses, Opportunities, and Threats) analysis allows organizations to consider both the general environment and the task environment**. This method was devised by Albert S Humphrey, a business scholar and management consultant who specialized in business planning and changes.

**Strengths and Weaknesses**

**Identifying internal strengths and weaknesses involves consideration of financial, physical, human, and organizational assets**. Managers use SWOT analysis to determine the current state of their companies. **These are some of the asset management considers:**

* **Managerial expertise**
* **Available product lines**
* **Skill levels and competencies of staff**
* **Current strategies**
* **Customer loyalty**
* **Growth levels**
* **Organizational structure**
* **Distribution channels**

It would be a strength if any organization has an executive training program that is considered an industry standard. If a company is having financial difficulty or is experiencing unfocused growth, it would be a weakness. In an insurance operation, an insurer that had been cutting prices to gain market share might identify loss of premium volume as a substantial weakness when an unanticipated rise in losses is projected as part of the SWOT analysis. Unfavorable loss results cause financial constraints.

The first step in the process of evaluation of business strategies should be to complete a current analysis. The current analysis can then be used to examine the insurer’s business strategies, placing emphasis on any issue that have prompted the current evaluation. Strategies can then be evaluated to determine whether they are appropriate in guiding the insurer to meets its goals and objective.

**Opportunities and Threats**

Managers determine potential opportunities or threats by analyzing he external environment, including both general and task environment factors.

One way to achieve this is through trend analysis, which identifies patterns related to specific factors in the past and then projects those patterns into the future to determine potential threats or opportunities. Insurers might determine opportunities and threats through trend analysis. Opportunities might be presented by new markets, possible acquisition targets, or a reduction in competition, while threats might include new competitors, an increase in competition levels, economic downturns, or changes in customer preferences.

SWOT Analysis Table:

|  |  |
| --- | --- |
| Strengths | Weaknesses |
| **Internal**: **List assets, competencies, or attributes that enhance competitiveness**  Prioritize based on the quality of the strength and the relative importance of the strength | **List lacking assets, competencies, or attributes that diminish competitiveness.**  Prioritize based on the seriousness of the weakness and the relative importance of the weakness |
| Opportunities | Threats |
| **External**: Lists **conditions that could be exploited to create a competitive advantage**  Prioritize based on the potential of exploiting the opportunities | **List conditions that diminish competitive advantage**  Prioritize based on the seriousness of probability of occurrence |
| *Note Strengths that can be compared with opportunities as areas of competitive advantage* | *Note weaknesses that can be paired with threats as risks to be avoided* |

The approach varies based on each company’s needs. A company should not only identify strengths, weaknesses, opportunities, and threats, but should also thoroughly analyze how they affects its strategic plan.

Once the SWOT analysis has been completed, managers can develop strategies that position the company to gain a competitive advantage by leveraging organizational strengths and offsetting or reducing weaknesses. The company should also find ways to capitalize on identified opportunities and to neutralize existing threats.

**3 – Determining Strategy at different Organizational Levels**

**Objective**: Explain how strategies are developed at the corporate, business, functional, and operational levels

Strategic plans encompass a variety of organizational activities. Because organizations vary widely, every organization requires its own approach. Strategies can be categorized based on the level at which they are carried out within an organization, how they relate to the development stage of the organization, and how they align with the organization’s overall business approach.

Strategies at all levels should be aligned to support the organizations overall mission and vision. On any given date, insurance professionals may participate in implementing multiple strategies simultaneously.

**These are the most prevalent types of organizational strategies:**

* **Corporate-level strategy represents the highest level for a diversified organization. It determines the types and potential profitability of business or activities the organization will undertake.**
* **Business-level strategy may be implemented by a single operation or, in the case of a diversified corporation, a strategic business unit (SBU). Managers develop strategies at this level to support the corporate-level strategy, to be competitive, and to respond to changes in the external environment.**
* **Functional-level strategy is carried out by individual departments performing specific organizational function, such as marketing or underwriting**
* **Operational-level strategy relates to a department’s narrowly defined day-to-day business activities. Operational strategies include workflows and production processes**

**Corporate-Level Strategy**

At the corporate level, the CEO and the executive team determine the business in which the company will be involved, allocate organizational resources properly, and incorporate strategies at all company levels to maximize profits. Corporate-level strategies are relatively long term, established for five-year period and beyond.

Competitive advantage is reinforced when each department or unit in an organization creates value for the customer. In insurance operations, the marketing, underwriting, claims customer service, and other departments must align to build value and to support corporate-level strategy in a continuous chain. This alignment can also provide additional advantages in the form of reduced operating expenses or increased differentiation of products and services through the interaction of various departments, such as marketing and underwriting.

Three generic corporate-level strategies are available for companies in a growth mode:

* Single business
* Vertical integration
* Diversification

**Concentration on a Single Business**

Based on a business environmental assessment, a company might determine that the best corporate-level strategy is to pursue is concentration on a single business. By concentrating its efforts and resources on one industry, product, or market, a company can build distinctive competencies and gain a competitive advantage. Many property-casualty insurers pursue a single-business strategy, even though they write many types of insurance.

Concentrating on a single business, however, has some potential disadvantages. Most are related to missing opportunities to build a competitive advantage through either vertical integration or diversification into related areas.

**Vertical Integration**

**A vertical integration strategy can be either backward or forward. If an organization produces inputs for processing (such as an insurer printing policy forms-in-house instead of purchasing them from a printing supplies), it is backward integration. When an organization sells its product directly to the customer rather than through a wholesaler, it is called forward integration**. Direct writer insurers are an example of forward integration being put to use.

*When a company is pursuing a vertical integration strategy, it either produces its own inputs or disposes of its own inputs. Backward integration occurs when an organization produces inputs for processing. Forward integration occurs when an organization sells its product directly to the customer.*

Companies choose vertical integration to decrease expense or increase efficiency. However, vertical integration could have an opposite effect due to a lack of expertise or the cost of resources in different states of the production process.

**Diversification**

Diversification for the property-casualty insurance industry can be advantageous. Because the industry is affected by the weather cycles, diversifying into lines of insurance or financial products that are unaffected by the weather can help smooth the demand for both financial and human resources. Because the insurance underwriting cycles does not coincide with the general business cycles, some insurer may benefit from diversification into non-insurance business to offset lower insurer profits during troughs in the insurance profit cycle.

**Related diversification allows companies to gain economies of scope by sharing resources, such as the same distribution system or research and development facilities. Expanding its operations into areas that are similar to its existing operations.**  Example; an insurer may also provide life or health insurance and thus utilize its existing technology and agency system to grow its business while spreading risk. Another benefit of related diversification is the ability to leverage fixed expenses with additional revenues for diversified operations, resulting in lower unit cost for each product or service offered. Example, insurers may enter into third-party administration of claims as some of their customers choose alternative risk financing approaches instead of traditional insurance. This allows the insurers to obtain additional revenue from their existing technology platforms, claim expertise, and other internal resources.

**Unrelated diversification strategy (also referred to as conglomerate diversification) involves acquiring companies that have not relationship to the existing business operations and is riskier than related diversification.** The negative aspects of unrelated diversification include additional costs of coordinating the divergent businesses, a loss of synergy among business units, and diminishing returns from any economies of scale or scope. Companies that have succeeded with an unrelated diversification strategy excel at making the right types of acquisitions. These companies have also developed strong structure and control mechanisms to offset some of the difficulties stemming from managing an extensive and varied group of profit centers.

**Decline Mode Strategies**

**All of the strategies discussed to this point involve companies operating in growing markets. However, some companies might not be growing, might be encountering substantial marketplace obstacles, or might have numerous internal weaknesses and external threats. The problems that these companies encounter could include decreasing profits, loss of market share, or changing economic conditions.** When a company is operating in a market in which demand for its products or services is decreasing, it is in a decline mode and its strategic options are different than those of companies in a growth mode.

**Corporate-level strategies for such companies are defensive. In the worst-case scenario, the company might determine that the only option is bankruptcy or liquidation. In bankruptcy, companies seek court protection from creditor to reorganize and improve their financial standing**.

**Business-Level Strategy**

Business-level strategies are developed at the business or division level by managers who are responsible for supporting the stated corporate-level strategy. These managers must find ways for their business units to be competitive and to respond to changes in the external environment. Business-level management also budgets for needed resources and coordinates the functional-level strategy within the division. The time from for business-level strategies, sometimes referred to as tactical strategies, is 3-5 years in most organizations. There are three business-level strategies:

* Cost Leadership
* Differentiation
* Focus

**Cost Leadership**

**Cost leadership enables a company to charge a lower price for its products or services. It involves eliminating costs in every aspect of the operations, from product development and design to distribution and delivery**. However, cost leadership involves more than just charging the lowest price in the industry. Even when prices for similar products are comparable, the cost leader can earn higher overall profits than its competitors because of its lower costs. Cost leadership can also better withstand prolonged price wars.

One requirement of a cost leadership strategy is that most products or services must be fairly standardized. Introducing varied types of products increases expenses and erodes any cost leadership advantages, so costs leaders do not tend to be first movers within an industry.

For insurers, price cutting might be limited by regulatory constraints. Insurer must closely examine the three components of an insurance rate (allowances for loss payments, expenses, and profit) to determine where const can be reduced. When evaluating how to decrease costs, insures can consider reducing acquisition expenses by lowering producers’ commissions, using direct writer system for some or all of their marketing, or exploring alternative distribution channels.

**Loss expenses can be reduced by streamlining claim adjusting processes, managing litigation expenses, or implementing cost containment practices, such as negotiation of repair or medical reimbursement rates with vendors. Underwriting expenses can be reduced by using expert computer systems or standardizing underwriting guidelines**. Technology can automate processes, improve interaction among departments, and speed policy processing times.

**Differentiation**

A Successful differentiation strategy requires products and services that customers perceive as distinctive and that are difficult for rivals to imitate. Companies using this strategy must accurately determine the needs and preferences of their customers, or revenue and market share will be lost. Market share will also be lost if competitors can match or improve upon the product’s unique features.

Insurers employing this strategy may choose to differentiate products or services to gain market share and to establish a competitive advantage. Insurer that offer special programs for commercial or homeowners insurance are examples. When an insurer writes only homeowners or personal auto insurance and targets multiple markets (such as teachers or retired persons) it is following a differentiation strategy.

**Focus**

A focus strategy involves concentrating on a group of customers, a geographic area, or a narrow line of products or services while using a low-cost approach or a differentiation strategy. The tow types of this strategy are focused cost leadership strategy and focused differentiation strategy.

**Focused Cost Leadership Strategy** – a business level strategy through which a company focuses on one group of customers and offers a low price product or service

**Focused differentiation Strategy** – a business-level strategy through which a company focuses on one group of customers and offers unique or customized products that permit it to charge a higher price than that of its competition.

Many insurers follow on of the focus strategies. Niche marketing programs, which offer tailored coverages to specific groups of customers are examples of focused differentiation. Alternatively, an example of a focused cost leadership approach is when an insurer that sells to a specific group of customers, such as retail hardware stores and offers discounted commercial packages or auto policies using standard forms. The use of standard forms is an important factor because any significant level of specialization increases costs and erodes profits.

**Functional-level Strategy**

Functional-level strategies are the plans for managing a particular functional area, such as finance, marketing, underwriting, actuarial, risk control, premium audit, and claims. These strategies establish how functional departments support the organization’s business-level and corporate-level strategies. The time frame for these strategies is short term, usually one year.

Companies build value and competitive advantage through efficiency, quality, customer responsiveness, and innovation. Some combination of these factors must be incorporated into its activities at the functional level for a company to pursue either a cost leadership or differentiation strategy at the business level. Without efficiency and innovation, cost leadership cannot be obtained. Quality and customer responsiveness must be included in the development, production, and marketing function for a company to execute differentiation strategy effectively.

In insurance operations, functional-level strategies specify how the underwriting, claim, actuarial, and other departments advance business-level strategies. For an insurer to be successful at garnering market share using a cost leadership strategy, it must become a highly efficient organization. The information technology department should provide innovative solutions to lower overall production costs and improve the speed of organizational communications, both internally and externally. Likewise, an insurer that is pursuing a differentiation strategy will consider innovations and quality at all functional levels to be critical to providing a distinctive product that meets the customer’s needs.

**Operational-level Strategy**

Operational-level strategies involve daily business processes and workflows, and are implemented at the department level to support the strategies of the functional, business and corporate levels. Example a claim office with a high volume of claims and a functional-level strategy to improve efficiency might decide to obtain more information through the claims reporting process in order to assign eth claim properly and eliminate redundant communications with insureds. A premium auditing department, striving to achieve a functional-level budgeting strategy might use pre-audit screening as an operational-level strategy to make the most effective use of resources or achieve its budget goals

**4 – Strategic Management Case Study**

**Objective**: Given information about an insurer’s business strategies, conduct a SWOT analysis of its strategy

X Insurance Company is a 60-year-old regional mutual insurance company authorized and operating in 8 states. The company is headquartered in PA., but, maintains at least one satellite claims office in each state in which it writes.

X writes only personal lines risks, with auto being the core of its business. Auto customers may be offered coverage in X’s “preferred” auto insurance company, or in its “nonstandard” (high risk) company. The company offers generous discounts for drivers between the ages of 35 and 60 based on the favorable loss ratios of this group. X does not offer a rating discount based on longevity, although long-term households also show consistently favorable loss ratios.

The company’s operations are consistent with core values it established 60 years ago: to protect policyholder assets, to gain customer loyalty, be a good corporate citizen, and to comply with all legal requirements. Throughout its existence, the company has enjoyed a consistently superior financial rating. A conservative investment strategy, favorable underwriting results, and conservative policy growth have allowed X to maintain ample policyholder surplus even in years of high catastrophe losses and lackluster returns on investments. X does not compete based on price, but rather on financial strength and core values.

X uses independent agents to sell its products, and a monthly policyholder magazine accounts for the majority of its advertising. X’s customer-focus philosophy stresses personalized service to gain customer trust and loyalty. X’s website does not provide quotes, direct purchase options, claim reporting, or premium payment options.

Over the past decade, the auto market has changed dramatically. Policyholders demand customer service, yet also want lower premiums. The line between “preferred” and “nonstandard” companies has blurred as the use of credit-based insurance scoring and other tools effective in predicting risk of loss have resulted in more refine pricing and increase use of rating tiers. More sophisticated coverage and rating options means that the insurers are able to rate and compete for segments of business that they may not have in the past.

Some auto insurers invest millions of dollars annually in high-profile advertising. Celebrity spokespersons, mascots, special effects, and humor have led to name recognition for certain companies and remind consumers that they can easily switch companies. Younger consumers tend to seek information from insurer’s websites when shopping for auto insurance, and these shoppers are more likely to seek an auto insurance quote directly from a website or mobile application than older consumers.

**X’s Insurance Company – Goals**

An organization’s goals provide the overall context for what the organization seeks to achieve. X’s goals have remained fairly constant for many years, and it establishes metrics based on these goals annually.

* Maintain financial strength to protect insureds
* Build long-term customer loyalty and maintain high customer satisfaction by meeting customers needs
* Contribute to charitable community efforts through time and financial support
* Comply with legal requirements

**X Insurance Company – Business Strategies**

Based on its goals of financial strength, customer loyalty and satisfaction, and charitable giving. X has develop business strategies to direct its actions:

Financial Strength: Protect our policyholder’s security by maintaining financial strength. We will:

* Increase policyholders’ surplus and maintain our superior financial rating
* Achieve a combined ratio of 98% or less (auto & Homeowners)
* Increase written premium by 5%
* Gain a net increase of auto policy in force by 2%

Customer Focus: we will commit to providing outstanding customer service that our customers deserve and demand, and strive to build long-term relationships. We will:

* Offer quality products, while meeting or exceeding established product delivery goals
* Increase average household longevity by providing consistently superior service
* Achieve 98% customer satisfaction as expressed on post-claim settlement and annual policyholder renewal surveys.

Technology and Data Management: we will provide the best service possible to our agents and policyholders by adopting current and efficient technologies intended to enhance our business. We will

* Safeguard all customer data
* Expand use of data-driven products in the claims settlement process

Corporate Leadership: We will show leadership in the communities in which we operate through organization effort and through the dedication of our employees. We will

* Dedicate our time and financial support to community activities
* Encourage employee participation in community charitable efforts
* Achieve a 50% positive response on recognition of our community efforts as measured by annual policyholder renewal surveys

Issues that Prompted the Evaluation

X has failed to meet is auto insurance written premium and policy growth goal for the past 2 years. X’s new business has declined steadily over the past few years, and retention ratios of existing business have decreased at an even greater pace. After accounting for the impact of the economic downturn it has become clear that the negative trends likely stem from its current business practices.

A survey of X’s agents has revealed that X insureds who were insured under their parent’s policies seem increasingly less likely to stay with X when they establish their own households. Further, many cited dis-satisfaction with claims service as a primary reason for obtaining coverage elsewhere, despite the fact that post-claim surveys continue to show acceptable results.

**Conduct a Current SWOT Analysis**

When determination of strengths and weakness may be based on subjective criteria, the overall process allows for an objective view of the environments in which the organization operates. One method of conducting a SWOT analysis is through a group activity that involves an organization’s managers and is organized by a facilitator.

Brainstorming - Through brainstorming, factors are listed under each of the SWOT headings (Strengths, Weaknesses, Opportunities, Threats). **Strengths can be paired with opportunities as areas of competitive advantage and Weaknesses can be paired with threats as risks to be avoided**

Refining – List items from high importance to lower importance and cluster similar items together

Prioritizing - **Strengths are ordered by quality and relative importance; Weaknesses are ordered by degree to which they affect performance and by their relative importance; Opportunities are ordered by degree and probability of success; Threats are ordered by degree and probability of occurrence**.

The SWOT analysis of X reveals that the company faces a high risk of threat because it has not kept pace with the needs of existing customers or the buying preferences of prospective customers. Customer surveys may be unreliable because they are outdated and fail to ask the right questions. The monthly magazine may have little impact on customer relations or loyalty.

A review of the survey questions asked may reveal whether such surveys need to be revised.

**Determine Business Strategies to Be Evaluated**

The organization’s business strategies are its long-term approach to attaining its goals and objectives. Because an organization’s strategies can be extensive, it is helpful to narrow the focus of the examination by understanding the business issue that has prompted the evaluation. The strategies relevant to the issue can then be targeted for evaluation.

Which business issues have contributed to the failure of X to meet its customer satisfaction and loyalty goals and policy growth target?

Assuming that customers are leaving because they are either dissatisfied with the company’s products, services, or prices, the company may need to reevaluate its customer-focused strategy. This goal seeks to meet the needs of customers but fails to address identification of changes in the marketplace. The company’s business strategies also lack commitment to respond to the changing needs or buying habits of insurance consumers.

**Evaluate Relevant Business Strategies**

**After an organization’s internal and external environments and its business strategies have been examined, the next step is to determine whether a change in course is required to achieve its goals.**

Will the current business strategies for X continue to be the most effective approach toward attaining its goals, or should its business strategies be changed?

X’s current customer-focused strategy will not lead to successful achievement of the company’s growth goals. X has committed to customer satisfaction but has not devised an effective method of determining customer needs and opinions.

If the company revises its customers surveys and establishes additional method of reaching out to current and former customer and agents, it may determine that additional changes are needed as well, such as:

* Redesign its website to add online quote capability or other interactive options
* Expand into a new state as a direct writer
* Implement a pilot program to test new products or coverage options
* Redesign the company magazine to emphasize new developments and to better target second-generation policyholders
* Refocus community involvement efforts on issue more likely to appeal to second generation policyholders and effectively promote those efforts
* Retrain claims staff to improve customer satisfaction.

**SWOT Case Correct Answer**

X company has failed to meet its automobile insurance written premium and policy growth goals for the past 2 years because customer satisfaction goals are not being met and lapse ratios are increasing. A SWOT analysis indicates that X has not adequately identified or kept pace with the changing needs of customers.

Using that information to evaluate its business strategies, X must revise its customer-focused strategy to meet is goals. As a well-capitalized company, X is in a good position to implement changes, including updating technology and implementing pilot marketing programs designed to attract and retain business.

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| --- | --- |
| **Strengths** | **Weaknesses** |
| Strengths are apparent in Co’s financial Stability  Superior financial rating and PHS  Branding based on customer satisfaction  Commitment to charitable efforts  Established monthly communication  Representation by independent agents  Experienced employees | Weaknesses in the types of services that have not been developed  Customer surveys – inadequate  Technology has not kept pace  Claim handling complaints  Inadequate advertising  Lack of new products |
| **Opportunities** | **Threats** |
| Provide potential actions company can take  Generation Y insurance – ability to target younger  Ability to enhance branding through community  Ability to pilot discounts or incentives  Claims staff can be retrained and eval materials updated  Ability to expand into additional states  Ability to pilot direct writing option and internet based partnership options w/independent agents | Threats have surfaced as some are better positioned to meet the needs of your customers  Current business vulnerable to price leaders, advertising efforts and national writers  Agency force may lean towards – recognized brands  Increasing % of customers looking for direct purchase options (internet)  Dissatisfaction with claims process – may damage reputation  Competitors offer more pricing options |

**Strengths can be paired with opportunities as areas of competitive advantage**

**Weaknesses can be paired with threats as risks to be avoided**