5 disruptors that could turn the P&C industry on its head

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Wherever you turn in the business and technology media, the talk is all about the next disruption. In the beginning, there was Google and Amazon. More recently, there's been Facebook and social media platforms. Insurance has managed to sidestep most of these early forces of radical change by doing what it does best: limiting risk and staying the course. But now, with ground-rumbling shifts that can only mean more upheaval of traditional business models across the board, the insurance industry is facing some very real disruptors it can no longer ignore—and in some situations, is actually doing the disrupting itself.

The big five disruptors are agency displacement, monitoring technology, the blurring of financial services, the regulatory environment and demographics. Not only does each of these drivers have a profound impact on the insurance industry at large, but there are very specific implications for the property and casualty insurance sector.

1. Agency Displacement: Is There an Agent in the House?

Since the advent of insurance exchanges, agencies have had to adapt to bringing more value to the insurance process—through service, support and education of the customer—or go out of business. Property and casualty agencies in particular have survived on transactional business—personal auto, home, small life, business owners' policies—that have heretofore been a 'sold and done' affair. The unsettling fact is that the more transactional the insurance product, the more likely that it could end up being sold through an exchange. And if the product can be self-served by the customer, the need for the middleman is eliminated. Therefore, agents and agencies who rely on transactional business are the ones that are most at risk.

The insurance exchange or marketplace is just one of the factors threatening to displace agencies as we know them. But there's a deeper impact to them too, in that they threaten to displace product differentiation. In insurance, we live and die by differentiation—some companies have better service, some have better coverage through their policies, or simply enough variation to suit the needs of multiple customers. You only have to think of the different levels of deductable for casualty to get a sense of how insurance products fit different needs. But with the advent of insurance exchanges, such as Google's insurance marketplace, there's only one factor left over which to compete—and that's price.

So these online marketplaces represent for the industry a race to the bottom in service and in quality—with a reduced role for the agent in helping a customer select the ideally matched product. Liberty Mutual is one carrier trying to stay out of the box everyone else is putting themselves into, by refusing to participate in the exchanges. Perhaps you have seen Liberty Mutual's television ads that speak to how Liberty handles an automobile insurance claim. That is a key differentiator for Liberty Mutual as they eschew the exchanges. Liberty Mutual aside, those that participate in the exchanges will soon be selling "white paint" with not a shade of difference between policies, price being the only determinant.

In a similar vein to exchanges, another huge disruptor is the concept of "Pay-at-the-Pump." In a nutshell, these insurance plans would replace the present system of customer-selected policies with a government program. In this scenario, every car is covered by basic auto insurance when the car is registered and tags are issued, and the state would take the proceeds of a gasoline surtax (up to 50 cents per gallon) to pay for future claims. The idea is that insurance companies would bid competitively to insure blocks of motorists, with states contracting with them on claims handling. Those of us who have been in this business for awhile remember, not fondly, the Joint Underwriting Authorities (JUAs) that tried manage automobile insurance and failed miserably, leaving behind billions of dollars in shortfall.

2. Technology: Telematics, Anyone?

Technology is creating a tremendous opportunity for the insurance industry, while at the same time seriously complicating matters—the perfect definition of a disruptor. By having access to masses of real and factual data on customers, carriers are now able to ascertain the actual risk presented.

By this time, we all know about telematics and how good drivers can lower their premiums through its use. But think about it from the carrier's side. When the insurance company can price to the risk, based on the information they're able to get from the insured's car, it obviates or at least reduces the need for actuaries. Whether it's from a car or a home security system, by getting the actual data from a device connected to the client, insurers can more accurately price their products.

In certain cases, customers with an extremely low risk profile may opt to raise their deductibles very high so that they can pay a lower premium. Companies that carry insureds with low-risk drivers and safely garaged cars are going to take a hit in premiums. By contrast, when it comes to fleets, telematics may help insurers actually raise premiums. Most of us have had encounters on the road with careening, speeding trucks on the highway, or delivery vehicles tearing down a quiet, residential street. Insurance companies will know when commercial vehicles are being driven recklessly, and will be able to price for that risk.

On the homeowners' insurance side, telematics is making waves through big data. At some point in the near future, every piece of property is going to be geocoded. It will no longer be a question of, "For your piece of property and your zip code, you can talk to any of these three agents." Once everything is geocoded, agents will be assigned to a certain territory or number of houses in their market. And when anyone wants to buy a house in that area and needs a homeowner's quote, they can go online and buy their insurance. When the transaction is done, the buyer has his insurance and the agent has his commission.

This cuts two ways. Insurance companies are under pressure to be able to affect that kind of transaction, and this is where the industry is headed, though no one is quite there yet. But it's a huge disruptor for the P&C industry because it will affect commission rates. Millennials, for example, may be very resistant to paying 15% commission on a transaction they researched and completed themselves. This tech trend is consequently also a disruptive threat to agencies as we currently know them.

3. Banks-as-Insurance Companies-as-Banks: A Blurring of Financial Services Boundaries

Another disruptor is being seen in the blurring of boundaries between insurance companies and banks. Here's where the insurance industry is doing some disrupting of its own. While this shift may not affect the P&C industry immediately, it will definitely have ripple effects in the not too distant future. Led by Mutual of Omaha, we now have banks that are carrier owned, selling insurance in retail locations throughout the country. Mutual of Omaha, for example, has started a chain of 40-plus banks. In the past, traditional banks have tried selling insurance, but didn't fully understand that with insurance, the underwriter is taking the risk.

This will be a game changer. With a whole new set of investment products offered by insurance companies, suddenly customers want to get their agent service in brick-and-mortar "banks," rather than having their agent explain it and hand it to them over the kitchen table. With this blurring of financial services, the clear demarcation that existed before between insurance companies and banks and investment brokers is going to disappear.

This will send the industry's distribution channel into a state of flux. Agents' spectrum of offerings will need to be broadened—the monoline carrier that only writes a certain type of coverage will be heavily affected. In order to survive, insurance agents will have to be able to sell all kinds of products, helping customers take care of all their household needs. Commercial carriers will have to become true business partners with their clients—in small businesses, for example, where personal and business affairs are mixed up together, insurance agents will have to be able to manage it all. State Farm is already doing this, but their agents aren't compensated, nor are they specifically trained.

In this sense, the blending of services represents a disruptive threat from within the industry—suddenly there will be highly professionalized agents appearing on the scene who know financial services deeply, versus agents who just sell auto or home insurance.

There will also be a blending of complementary services—for example, personal investment products will eventually have joint agents who will distribute and sell both menus of products under one agency roof. Personal investment advisory firms will be selling a lot more insurance than they do now, and insurance companies will be getting a lot more involved in the security side. In effect, regulatory disruption (see next page) is creating a merger or consolidation of all financial services under one heading.

4. Regulatory Disruption: Another Step Away From Private Enterprise?

Changes in the regulatory landscape pose an enormous disruption to insurance. Take storm coverage for homeowners in hurricane states along the east coast. One customer who lives slightly inland of Ft. Lauderdale, Fla., pays $3100 for homeowners' coverage. If he lived in Iowa, he'd be paying $600; if he were right on the coast his premiums would cost $9500. Government regulators have established state-run "wind pools" to take the business out of the private market, because it was unwilling to provide insurance to homeowners in these areas at any price. So these premiums are very high—and traditional carriers are losing business as a result.

More regulation equals more oversight. Licensing of P&C claims adjustors is another example of regulatory disruption. Company and independent adjusters will have to submit continuing education and all the other certifying processes that agents already have to complete. Education perpetuation for licensed people is going to get harder. There will need to be more professionalism in the agent ranks, and "fly-by-nighters" won't be able to survive. The already complex ins and outs of the industry will become much more complicated, and there will be a regulatory environment that will combine federal and state regulations. In the short run, this will disrupt the industry's distribution channels.

As described above, the trend is toward a blending of agents—people who used to sell only P&C insurance are going to have to sell more types of insurance, like life and financial products. My prediction is that the day of the monoline agent will come to an end. Carriers are pressuring agencies, demanding: "Are you going to bring on a new Life producer?" This gets costly for the agency, and amid this, agents are going to be dealing more with risk management than they have in the past. In a sense, the new regulatory environment is moving the insurance industry away from private enterprise and more toward being a government-type, mega-overarching entity, as evidenced by movements such as ACA and Pay at the Pump.

5. Demographics: Ready or Not, Here Come the Millennials—and Immigrants

No roundup of disruptors to the insurance industry would be complete without addressing the changing demographics in the U.S. The Millennial segment, currently defined as those between age 18 and 34, make up 25% of the population. For the purposes of the insurance industry, the common denominator with Millennials is price. They spend hours online painstakingly looking for the best price, searching for the absolute best deal.

The other side of the demographic disruption is that we're bringing millions of immigrants into the country, including people who do not have a history, understanding or a comfort level with insurance. This will make for big changes. People who only speak their native languages will have a harder time navigating not only what is available to them, but what they need. Insurance companies will have to be able to service this market. On the positive side, this is a whole new subset of people that the insurance industry can educate and sell to.

In the end, in P&C, it's all about customer relations. Despite the technology and all of the other disruptors, the core of the insurance business relies on agents who have a personal relationship with their insured. People may believe that car insurance is car insurance—they're all created equal; but with the blendings and crossovers coming down the pike for insurers, the customer will want to know that there's a person behind all of these products, and that this person can be relied on. Indeed, the bigger the disruption, the greater potential role of the agent. Which gets us full circle back to the question: Can insurance afford to ignore these disruptive factors any longer? My vote is a resounding 'no.'