Insurance Practice

Product innovation: The new imperative for insurers in Asia

Incumbent insurers in Asia find product innovation challenging. Developing products to respond to customer needs, not risks or competitor actions, will be crucial.

This article was a collaborative effort by Vince Han, Alex Kimura, Diego Mattone, Brad Mendelson, and Jason Ralph, representing views from McKinsey's Insurance Practice.

March 2021

By their own admission and despite ongoing efforts, incumbent insurers struggle to produce innovative products. Survey data shows that while 82 percent of executives surveyed said they consider product development a core competency, only 12 percent believe their companies have a process that produces innovative products.[1] In informal interactions, executives also struggled to name products from the industry that they consider truly innovative. Effective product innovation is tied to a deep understanding of customers' emotional and practical needs and wants, paired with the ability to quickly get those products to customers—a departure for many incumbents' default philosophy of aiming to be fast followers. Traditional insurers demonstrate a relative lack of both understanding and ability compared with their digital-native counterparts, and that could be one of the primary factors that accounts for low penetration in Asian markets, ranging from 0.49 percent to 19.97 percent of 2019 GDP at the country level.[2]

The distinctive traits of the Asian insurance market make product innovation more important compared with the industry's traditional approach, which begins with an analysis of risks instead of customer needs and preferences. For instance, some major markets, such as Greater China, have rapidly aging populations and cultures that prioritize the care of children and elderly parents, which can create logistic and financial stresses for the "sandwich generation" of adults taking care of both their parents and their children. Incumbent insurers need to effectively reach and serve these customers while trying to increase insurance penetration. Partnering with digital platforms, particularly super apps—that is, apps that fulfill multiple functions, have a large user base, and mediate a significant portion of online activity for many customers—can help. However, super-app developers measure their success by the frequency of product iterations based on customer insights, and they will therefore expect insurers to develop products more quickly than they are currently prepared to do.

The combination of these pressures is a wake-up call for insurers to put customer-centric product development on the C-suite agenda. Insurance leaders in Asia should focus on developing their customer-insights capabilities, optimizing existing product portfolios, and improving their approaches to product innovation. Insurers that succeed in the region will be those that can use their understanding of customers to bring the right products to market quickly through the most relevant channels.

Slow-moving incumbents in a demanding and culturally diverse region

Incumbent insurers generally spend six to 12 months bringing a new product to market. This pace is partly attributable to factors such as legacy IT and a lack of agility. By contrast, a digitally enabled direct-to-consumer insurer might require two months or less to develop and launch a new product and less time for product changes. While super-app developers can be helpful partners in marketing and distribution reach, they can easily become competitors as well.

For now, while insurers can offer industry-specific expert capabilities, super apps are increasingly important to insurers' commercial sustainability. However, super apps also demand a pace and scale of innovation that can exceed many insurers' current capabilities. One executive of a Chinese super-app developer complained that his insurer partners often struggled to translate customer insights into viable products because they lacked the speed and the ability to change the way they worked. Further complicating the picture, the benefits and features of traditional insurance propositions—that is, the products as well as their supportive services and functionalities that may or may not be visible to the customer—can be challenging to convey in a digital setting, especially to consumers who are less familiar with insurance offerings.

[1] "Understanding the product development process of individual life insurance and annuity companies," Society of Actuaries, December 2017, soa.org.
[2] "World insurance: Riding out the 2020 pandemic storm," Sigma, 2020, Number 4, swissre.com/institute/research.

Finally, the region is home to a significant sandwich generation: one out of seven adults in their 40s and 50s with parents who are 65 or older are also supporting children.[3] A 2019 McKinsey survey showed that adults in mainland China are concerned about retirement planning, building wealth, family protection, and their children's education. As such, insurance products therefore need to address needs across multiple generations.

Creating innovative propositions

The best way to create innovative products is to build innovation into the way an organization functions.[4] Instead of building products to address an extensive set of risks, incumbent insurers should design products in response to specific customer needs and challenges, some of which may not be obvious. This approach also applies to optimizing insurers' existing product portfolios and ancillary services. Finally, insurers should update the product-innovation process so they can stay close to their customers and promptly deliver what customers need. These tasks should be continuous and—especially in light of the COVID-19 crisis—involve a speedy ramp-up of digital capabilities and a virtuous cycle of insight and product generation within the workforce.[5]

Focus on customer insight

Product development in the insurance industry is traditionally built on risks, which requires the application of underwriting rules and standards. Though this approach is rational, it lacks a deep understanding of customer behavior and has produced an industry in which insurers obsess over competitors' actions instead of taking cues from customers. This approach results in commodification and makes insurers more likely to overlook emerging—but significant—risks. Instead, insurers should take a generative approach that prioritizes discovering customer needs first, then responding with propositions. Such an approach has already inspired some insurers to offer insurance as a service, which expands on the traditional insurance offerings.[6]

Customer insight may not be a well-developed discipline for every insurer, but partnerships with companies that have rich and complementary sets of customer data and insights can be valuable. Partnerships with super-app developers, for example, can help insurers observe customers' behaviors and revealed preferences, not only because these apps generate large volumes of data but also because they create and shape new purchasing behaviors. For instance, one insurer partnered with a Chinese social media platform to develop, market, and distribute a protection product. The product launched in time for the Lunar New Year and let customers send digital red packets—traditionally used to exchange monetary gifts—containing insurance benefits. Similarly, an insurer in Japan partnered with an insurtech to address the needs of a population in which more than 30 percent of people are over 60. The result was the successful launch of dementia insurance and associated services.

Even though partnerships can yield rich customer insights, insurers should also continue to use traditional customer-research methods, such as direct observation, focus groups, and interviews. To create the right conditions to gather customer insights and identify evolving and emerging customer needs, every product team and marketing team should have dedicated resources for customer research that use data collected from diverse sources and methods. This task may require modifying the organization and its operating model. One large Chinese insurer, for example, forgoes functional groups and works in business groups headed by product owners.

[3] Irfan Handaru, "Sandwich generation: The power struggle of caring for two-generation," *The People of Asia*, April 5, 2019, thepeopleofasia.com.
[4] For more on committing to innovation, see Daniel Cohen, Brian Quinn, and Erik Roth, "The innovation commitment," *McKinsey Quarterly*, October 2019, McKinsey.com.
[5] For more on innovation during a crisis such as the COVID-19 pandemic, see Jordan Bar Am, Laura Furstenthal, Felicitas Jorge, and Erik Roth, "Innovation in a crisis: Why it is more critical than ever," June 17, 2020, McKinsey.com.
[6] For more on insurance as a service, see *McKinsey Digital Blog*, "What the new world of insurance could look like," blog entry by Ido Segev and Amy Vickers, August 1, 2017, McKinsey.com.

The ultimate goal for insurers is to know their customers well enough to personalize offerings and messaging to the smallest possible segment so customers feel understood. For example, one Philippines-based insurer responded to the related trends of aging populations and increasing numbers of sandwich-generation adults with a protection product that covers both the account owner and up to three family members. Insurers that refine their understanding of customers and fit their products to their needs will do better than competitors that take the inverse approach.

Optimize existing product portfolios

A lack of regular, rigorous review of the portfolio tends to result in out-of-date products that generate high maintenance costs. This scenario is a significant liability; industry executives indicated in interviews that in a portfolio of 100 products, the top three products often make up about 75 percent of sales, and only about 10 percent of products in the portfolio achieve their new-business targets. Instead, insurers should use customer insights to continuously conduct comprehensive reviews of their product portfolios. Specifically, product teams should first analyze the economics of each product and its odds of success given what they know about current and projected customer needs and preferences. Then they can stress-test and prototype each product individually and the portfolio as a whole. This stress test should at least cover the effects of external factors such as changes in interest rates on product economics and commercial performance.

In addition, the team should review the company's proposition strategy, regularly identifying and assessing market opportunities in evolving market conditions, with a heavy emphasis on how different products can meet disparate customer needs. Such an exercise can produce insights on products that could benefit from being redesigned. This review can also help decision makers evaluate whether market conditions might affect distribution and how they can respond. (For a study of how one Asian insurer reviews its product portfolio, see sidebar, "Annual reviews of an insurance product portfolio.")

Update the product-innovation approach

Innovation should not be a niche activity, and insurers should overhaul their innovation processes—and indeed, their organizations—to focus on customer centricity and agile operations in service to a flowing product pipeline. The CEO should preside over this pipeline—similar to how a tech CEO might approach the role—and work closely with the chief customer officer, the chief data and analytics officer, and major partners such as super-app developers.[7] Although the latter two roles will be relatively new to the industry, they can

[7] For more on chief customer officers, see Chris Davis, Alex Kazaks, and Alfonso Pulido, "Why your company needs a chief customer officer (CCO)," December 29, 2020, McKinsey.com; for more on chief analytics officers, see Brian McCarthy, Chris McShea, and Marcus Roth, "Rebooting analytics leadership: Time to move beyond the math," November 19, 2018, McKinsey.com.

Annual reviews of an insurance product portfolio

One large insurance company operating in Asia reviews its product portfolio once a year. Its product-strategy team works within the actuarial function to initiate this review and first spends a week collecting important data such as annual premium equivalents (APEs) and value of new business (VNB), a proxy for future profitability.[1]

Data in hand, the team spends three weeks on analysis, splitting the portfolio into product groups. The team evaluates each product in a product group and gives detailed explanations of changes in key metrics—such as VNB—for important products. The relevant factors usually include regulation, changes in customer demand, competitive pressure, and the macroeconomic environment.

The team uses its analysis to recommend actions for product groups and individual products. These recommendations are reviewed with the chief actuary, the CFO, and then the rest of the C-suite.

[1] A measure of insurance sales. The APE is calculated by summing the total value of regular or recurring premiums, plus 10 percent of any new single premiums written in a given fiscal year. VNB is the book value of new business an insurer wrote in a given fiscal year.

For instance, different lines of business and product families can be headed by a business group leader who acts as the product manager.

help nurture a culture and product- and customer-focused mindset that uses cycles of creation, testing, and learning to innovate.

To support an effective product-innovation process, insurers would also need a corresponding organizational structure. For instance, different lines of business and product families can be headed by a business group leader who acts as the product manager. This leader would be responsible for pulling together customer, partner, and market insights and responding promptly to new customer and market developments.

The product-innovation organization must have an agile process if it is to respond effectively to customer insights. Cross-functional teams should work together to uncover and act on these insights. And because new products and processes can emerge as responses to market conditions, innovation teams—reporting to product leaders—should work with tech and IT teams to ensure that their companies' tech stacks can minimize time to market. For ambitious insurers, an agile innovation process that releases funding when products reach predefined milestones can help them progress quickly, allocate resources efficiently, and learn from products that fail to thrive or that become irrelevant.[8]

Once products are in the market, insurers should continuously collect consumer-behavior data and use that feedback to test and adjust elements of their approach, most obviously their targeting and pricing. Insurers can also use this approach to test product concepts. Of course, this dynamism depends on each insurer's ability to respond promptly and build on emerging insights as data come in.

Bucking established industry conventions and designing new products with customer needs—instead of risks—in mind will be Asian insurers' next big challenge. This challenge is also an opportunity that promises to be fulfilling for the insurers that get it right. The key is to get started.

[8] For more on agile organizations and processes, see Daniel Brosseau, Sherina Ebrahim, Christopher Handscomb, and Shail Thaker, "The journey to an agile organization," May 10, 2019, McKinsey.com.

Vince Han is an associate partner in McKinsey's Shanghai office; **Alex Kimura** is a partner in the Singapore office; **Diego Mattone** is a partner in the Zurich office; **Brad Mendelson** is a senior partner in the Hong Kong office; and **Jason Ralph** is an associate partner in the Minneapolis office.

Contact

To connect with someone on this topic in your region, please contact:

Americas

Kweilin Ellingrud
Senior partner, Minneapolis
Kweilin_Ellingrud@McKinsey.com

Brian Quinn
Partner, Chicago
Brian_Quinn@McKinsey.com

Jason Ralph
Associate partner, Minneapolis
Jason_Ralph@McKinsey.com

Asia

Vince Han
Associate partner, Shanghai
Vince_Han@McKinsey.com

Alex Kimura
Partner, Singapore
Alex_Kimura@McKinsey.com

Brad Mendelson
Senior partner, Hong Kong
Brad_Mendelson@McKinsey.com

Europe

Diego Mattone
Partner, Zurich
Diego_Mattone@McKinsey.com

Further insights

McKinsey's Insurance Practice publishes on issues of interest to industry executives. Our recent articles include:

The growth chessboard: How leaders fuel profitable growth in insurance

Insurance strategy in Asia: Using programmatic M&A during the pandemic

Reimagine insurance: Five keys to innovation

China insurance: How insurers can improve customer experience where it matters