

SME insurance in Australia – A market ripe for change



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Executive summary

The Small and Medium Enterprise (SME) sector is growing in importance. Employing over 70% of the Australian workforce, the sector is becoming an important target customer base for a range of services providers, from banks to telecommunications companies to utility providers. And the insurance sector is not immune. It too is seeking to better understand how to service this large and growing customer base.

In response, McKinsey & Company launched a survey of SME businesses in 2017 aimed at better understanding the insurance buying characteristics of this segment of the economy, the McKinsey Australia Small Commercial Insurance Consumer Survey. The Survey points to an Australian SME insurance market that is ripe for sizeable change. Nearly three-quarters of small business owners are dissatisfied with, or are not loyal to their insurance provider. However, they are not aware of, or actively pursuing better options – only 19% of small business owners switch provider each year. This suggests there could be significant rewards for insurers who are able to better meet the needs of small business owners. While it might require adopting entirely new business models, the potential gains are significant.

Australia's small business sector (comprising companies with fewer than 250 employees) is sizable, consisting of over two million businesses. These account for nearly 70% of all employment in the economy and almost 40% of the country's GDP¹. Currently, the SME insurance market accounts for an estimated A\$9.4 billion in general insurance premiums.² However, a recent report by the Insurance Council of Australia found that some 13% of these companies are not insured, and 1.9% report being underinsured.³

Reasons reported for lack of insurance or underinsurance include being too busy to arrange insurance, price levels being too high, and a lack of awareness of risk exposures.⁴ Though rates of no insurance or underinsurance are commonly understated, if even just the reported 13% gap of uninsured companies could be closed it would be worth A\$1.4 billion in new premiums.

Similar to other markets, the McKinsey Australia Small Commercial Insurance Consumer Survey found the SME market in Australia is far from homogenous however, making it challenging for insurers to serve it. Indeed, the variety of niches and different risk profiles makes it difficult for insurers to build efficient, at-scale business models. SME niches vary in at least three important ways:

- Size: organisations range from sole-proprietors to larger SMEs with fewer than 250 employees
- Industry: from solicitors to plumbers, each profession requires a very distinct set of products
- Attitudes and behaviours: with such diversity, price sensitivity, need for advice, willingness to self-serve and dependency on brokers varies substantially across SMEs

1 Australian Bureau of Statistics (www.abs.gov.au).

2 McKinsey Global Insurance Pools Insurance Database, 2017.

3 Compares to estimated 15% non-insurance rate in the UK. FCA 2015

4 Non-insurance In the Small to Medium Sized Enterprise Sector, July 2015, Insurance Council of Australia.

The McKinsey Australia Small Commercial Insurance Consumer Survey

This report covers the market for commercial insurance for small and medium enterprises (SMEs) in Australia. SMEs are defined as business entities registered in Australia with fewer than 250 employees, according to the definition used by the Australian Bureau of Statistics.

The report is based on the findings of the McKinsey Small Commercial Insurance Consumer Survey, conducted in January 2017 by McKinsey & Company. The Survey is part of a series of McKinsey & Company surveys and research efforts related to SME insurance conducted across a number of geographies.

The McKinsey Small Commercial Insurance Consumer Survey is an online survey of more than 400 Australian small business decision-makers who have direct responsibility for buying insurance. The surveyed population includes a diverse mix of companies by product mix, industry, size, region and brand of insurance product used. Sole proprietorships (one employee), small enterprises (two-10 employees) and medium enterprises (11-249 employees) are all represented in the sample. Industries represented include professional and business services, industrial and construction, retail and consumer, technology and telecommunications, travel and transportation, and finance, amongst others.

The variation in attitudes and behaviours underscores the need for insurers to define a distinctive value proposition for the diverse SME segments. Our Survey has revealed four groups of customers who exhibit similar attitudes and behaviours: 1) convenience seekers; 2) online DIYers; 3) expert seekers; and 4) bargain hunters. Based on the results of the Survey, the first two segments likely comprise around 63% of the premium value of the market, and are the 'value play'. The other two segments make up the remainder of the market, and are the 'volume plays' for insurers.

Understanding how to reach each segment successfully requires a more nuanced grasp of what drives insurance purchasing decisions for small business owners, as follows:

- Brand awareness, availability of information, and strength of brand equity are the key factors in the consideration set
- Price changes are the main trigger for the decision to switch provider, but low prices are much less important in driving loyalty
- Online channels are gaining importance, but brokers still have a significant influence on the market
- Industry expertise and the ability to build a trust-based relationship with customers significantly drive customer loyalty.

Success in this market may not be easy; the needs of the customers vary so widely that few players will be able to serve them all. The winners will be those that apply a sharp customer segmentation, demonstrate a deep understanding of their customers' needs, and find a cost-efficient way to serve the diverse segments.

Success will also require building distinct capabilities for the SME segment that straddle the border between personal lines and commercial lines. Some capabilities will be universal – in particular, those around standardisation, automation and cost-efficient customisation – others will differ by customer segments. For example, a proposition for the volume segment may be to boost marketing efforts and investment in direct distribution channels, while value players may invest more in the broker channel to ensure brokers have the latest digital tools for managing customers.

Insurers will need to learn from the best consumer-oriented institutions how to build their brand, and how to communicate the right emotional message, at the right time and via the right avenues. Digital innovations, data and analytics, and the ease of doing business will be critical to the new operating models. Price competitiveness will continue to be important and traditional elements of the proposition such as product, service, and claims experience should remain strong.

1. A market ripe for change

As of early 2015, there were 2.1 million private sector businesses in Australia, of which 99.8% were SME companies with 1-249 employees (of which almost 98% of were small businesses with 1-19 employees). The SME segment represented A\$608 billion of value to the Australian economy, representing 38% of Australia's GDP. Likewise, close to 70% of private sector employment in Australia - some 7.2 million people – work for SMEs.⁵

While SMEs account for a significant share of the Australian economy, many are underinsured. This under-insurance gap represents a potential A\$1.4 billion in additional premiums for insurers able to attract and better serve SMEs.⁶

Many SMEs are not insured or under-insured

In a recent survey performed by the Insurance Council of Australia, 12.8% of SMEs explicitly reported not having insurance.⁷ This compares to reported non insurance rates in the United Kingdom of around 15%, and in New Zealand of around 30%.⁸ For SMEs that do have insurance, the survey found that almost 2% actively report being inadequately insured (i.e. that they are insured, but not to adequate levels), with a significant number reporting particular underinsurance in business asset insurance, with reported underinsurance of the order of 20%. However, closing the reported ~13% non-insurance gap could be worth up to A\$1.4 billion in additional premiums.⁹

Reasons reported by business owners for not having insurance or being underinsured include feeling too busy to arrange insurance, price levels being too high, feeling as if they could never be adequately insured, and a perception that the risk was either too low or insurance just wasn't worth having.¹⁰ Those carriers that can create new value propositions and platforms to reach these SMEs are the ones who stand to capture this opportunity.

Dissatisfaction does not make SMEs switch insurers

As revealed in the McKinsey Australia Small Commercial Insurance Consumer Survey, roughly three-quarters of SMEs are potentially at risk of switching to another insurance provider. Nearly half are 'shoppers', and hence do not automatically renew their policies with their current insurers, but rather search for alternative quotes from different providers. Just over a quarter of customers are 'passive loyalists': they are dissatisfied with their insurers but do not look for alternatives as they find the process of finding new providers, and switching, too inconvenient.¹¹ Taken together, these two customer clusters are therefore good targets for an insurer that can provide better-suited products and services. Further, just 27% of SME clients are 'active loyalists', who are satisfied with their current insurers and true advocates of their brands; recommendations stemming from such loyalists are a key driver of winning new business.

5 Australian Bureau of Statistics (www.abs.gov.au).

6 Non-insurance In the Small to Medium Sized Enterprise Sector, July 2015, Insurance Council of Australia.

7 Non-insurance In the Small to Medium Sized Enterprise Sector, July 2015, Insurance Council of Australia.

8 SME Insurance, 2015, YouGov.

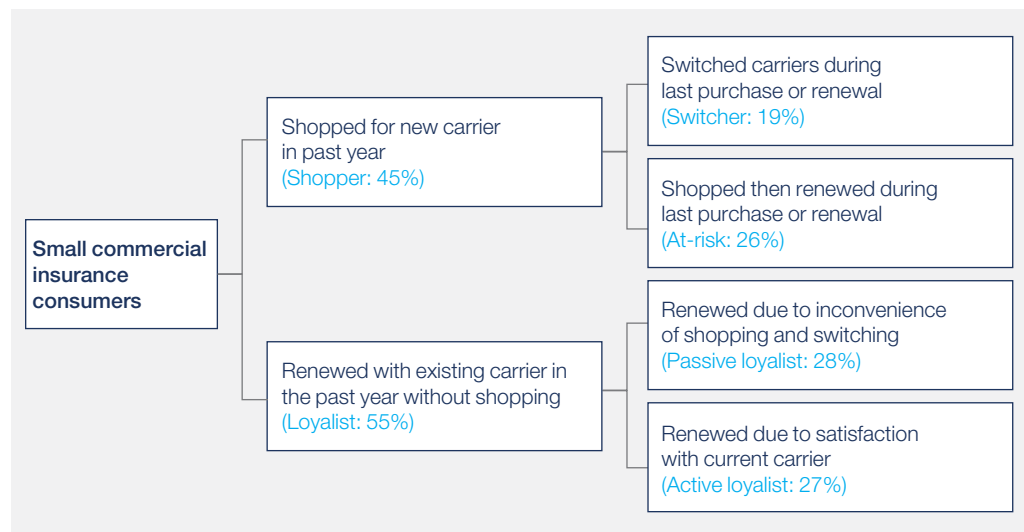
9 McKinsey Global Insurance Pools Insurance Database, 2017 based on estimated size of SME insurance premium pool in Australia of A\$9.4 billion.

10 Non-insurance In the Small to Medium Sized Enterprise Sector, July 2015, Insurance Council of Australia.

11 McKinsey Australia Small Commercial Insurance Consumer Survey, 2017, n=405.

More telling still, the Survey results showed that only 19% of the small business owners who search for better quotes end up making the switch. This low churn rate points to the lack of suitable and convenient alternatives and limited brand differentiation. These trends also closely align with those found in other markets including in the United Kingdom, and further indicate a real market opportunity may exist for new offerings and insurer business models that can deliver better value to SMEs.

Exhibit 1 – Only 27% of customers are active loyalists¹²



A A\$1.4 billion shortfall

Australia’s SME insurance market grew at a rate of 2.5% a year from 2011 to 2015, slightly slower than SME output growth of 2.9% over the same period. However, this represents only a small part of the story in missing premiums. Insurers can do more to deploy the right models and strategies to fully capture the potential of the SME market in Australia. Historically, focus has been placed on serving larger players with high service requirements and advice needs. Premiums for smaller businesses are typically much smaller than those paid by large companies, making it challenging to serve smaller SMEs in a way which is economical. Going after other, smaller SMEs, which are much higher in quantity, has to date been seen as not cost-effective, leading to significant gaps in coverage in the market.

The market opportunity for insurers to better serve SME insurance customers is significant. The question is, how can insurers best address this potential market opportunity? Digitisation, better segmentation, and new operating models, which will be discussed in more detail, are critical to solving this puzzle.

¹² McKinsey Australia Small Commercial Insurance Consumer Survey, 2017.

2. No single market: A myriad of micro-niches characterises the Australian SME sector

SMEs form a highly contrasted congregation of businesses. According to the Survey, SMEs differ markedly in size – from extremes of one person sole-trader businesses to relatively large, multi-centre businesses with fewer than 250 employees; they can be sole proprietorships or partnerships, they can be private companies or publicly-listed companies. They operate across a range of industry sectors, from those with standard risks (e.g. small convenience stores) to industries with highly specialised risks (e.g. suppliers in the aviation sector), leading to a significant variety of risk profiles and exposures which insurers need to understand.

In addition to these differences in risk exposures and resulting premiums, the diverging sizes of SME businesses will likely lead to varying degrees of risk management capabilities, risk purchasing sophistication and risk transfer appetite – all making the process of buying insurance hugely inconsistent across clients. Bigger SMEs will likely have a dedicated risk manager dealing with the business’s insurance program (often the finance director), as well as a dedicated broker advising on the policies needed. At the opposite end of the spectrum, sole owners or SMEs with under 10 employees are usually more focused on growing their business, and insurance is low on their list of priorities. In these businesses, the founder is usually the person dealing with insurance, but is often busy elsewhere. In addition, as the sums insured by SMEs vary from a few thousand dollars to tens of thousands, the insurers’ business economics for serving these businesses demands very different operating models.

Exhibit 2 – 2015 SME breakout by size, employment and industry value added¹³

Business size		No. of businesses (million)	Total employees (million)	Industry value added (A\$ billion)
Small	Non-employing	1.28		
	1-4 employees	0.58	4.76	1,086
	5-19 employees	0.20		
Medium	20-249 employees	0.05	2.50	696
Total		2.12	7.26	1,782

SME owners show different behaviours towards their insurers

Business activity and scale are the most easily understood differences between SMEs; however, they are not always the most significant. In fact one of the biggest areas of difference uncovered in the Survey was in attitudes and behaviours around purchasing insurance. The Survey found that SMEs respond quite differently to price sensitivity, to advice requirements, to disposition towards self-service, and in the degree to which brokers support the risk purchasing process.

Notwithstanding these differences, our Survey has identified four clusters of SME businesses, grouped by their consistency of attitudes and behaviours:

- Convenience seekers: this segment depends almost exclusively on brokers** to source the best policy price; and right coverage and claim services. They are willing to pay more for a better proposition and services, and they exhibit low affinity to online channels. In addition, they are loyal to their insurers’ brands. This segment has a higher proportional share of enterprises comprising 20 to 250 employees, and accounts for 29% of volume and 45% of the value of all SME businesses surveyed.





¹³ Australian Bureau of Statistics (www.abs.gov.au).

- Online DIYers: this segment is comfortable with purchasing insurance online, and generally has standardised product needs.** These customers can readily be found across all sized SMEs. They are comfortable with the idea of purchasing insurance products for their businesses online and have expressed a strong inclination to do so. They are also very interested in being able to manage their insurance policy online. Not overly price sensitive, this segment is willing to pay a bit more to have these features.

They are largely interested in standard insurance coverage and products. The segment accounts for 23% of volume and 18% of premium value of the Survey respondents.

- Expert seekers: this segment needs tailored products** and expects not only solid insurer expertise and reputation, but also a high level of customer service. They express a high level of confidence in their ability to navigate a variety of insurance options and select the right coverage their business needs. This segment has a higher-than-average proportion of sole proprietors and shows high levels of loyalty. The segment accounts for 27% of volume and 21% of premium value of respondents.
- Uninvolved bargain hunters: this segment is the most price-sensitive,** and does not generally have a need for extra coverage or tailored offerings. It has a balanced representation of both broker intermediation and direct purchase. The segment accounts for 21% of the volume and 16% of the premium value of respondents.

Exhibit 3 – Four SME Clusters¹⁴

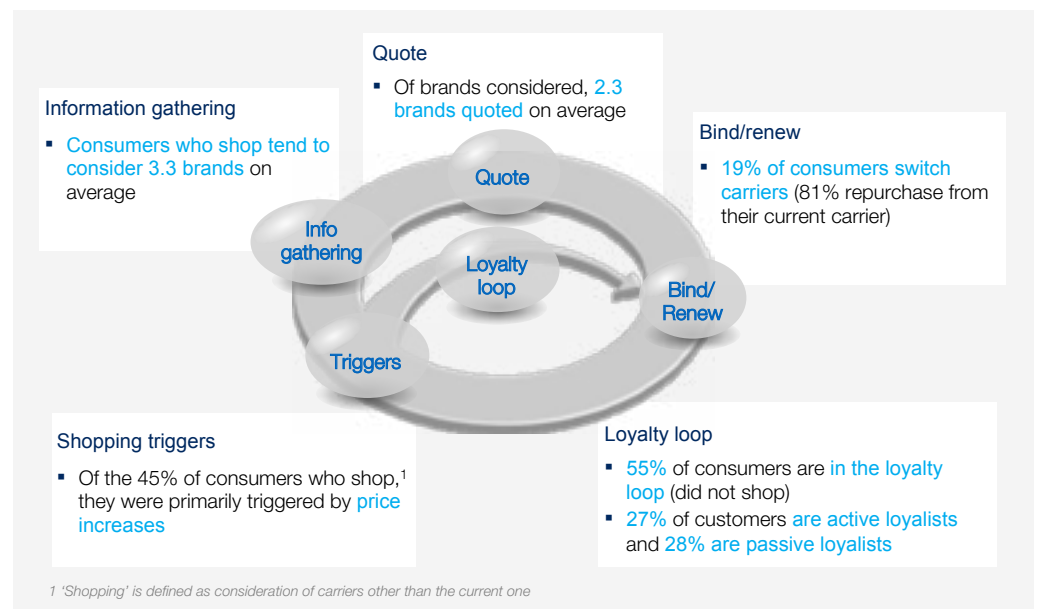
	The convenience seeker	The online DIYer	The expert seeker	The uninvolved bargain hunter
				
Typical Segment Characteristics	"I am very dependent on my broker to identify and recommend the best insurance products for my specific needs."	"It's important for me to be able to manage my insurance online. Standard insurance products are typically fine for my business."	"Custom-tailored insurance products are important to me. I am confident I can select the specific coverage that I need. I stick with a good provider."	"The most important thing when I consider which insurer to go with is price. I want my insurance as affordable as possible."
Median premium	~ A\$2,500	~ A\$800	~ A\$1,000	~ A\$600
Volume	29%	23%	27%	21%
Sole proprietors	6%	12%	17%	17%
Medium-sized (21-249 employees)	50%	54%	42%	51%
Share, broker intermediated	77%	58%	5%	23%
Share, buying online	1%	53%	33%	31%
Share, switchers	19%	23%	12%	28%
Share, active loyalists	32%	17%	33%	28%

14 McKinsey Australia Small Commercial Insurance Consumer Survey, 2017, n=405.

3. Understanding the SME decision-making processes

The process small business owners follow when purchasing insurance is fairly simple: information gathering, quotes searches, and provider selection. However, our research shows that SMEs do not necessarily follow these steps in a linear fashion. Instead, they regularly seek new information, reconsider prior decisions, and can change insurers even after connecting. They follow this disjointed approach because they constantly receive signals which, depending on where they are at in the process, may trigger a fresh decision journey, or change their thinking about a process already under way. On occasion, SME owners finish the cycle and then enter a loyalty loop, i.e. they stop considering other insurers and renew with their existing provider. On other occasions they do not automatically renew but become a 'shopper', re-entering the information-gathering phase. In a nutshell, SME decision-makers constantly 'learn' by adding or dropping brands and including the results of searches and experience into their decision-making process.

Exhibit 4 – The customer decision journey in commercial insurance¹⁵



The triggers that influence the SME decision-making process occur at a range of touchpoints. These include traditional advertising, online research (including insurer websites, social media and aggregator sites), brand recognition, recommendations from others, previous experience, brokers and trade associations. The relative importance of each of these triggers may vary, depending on the consumer's stage in the decision-making journey. After buying insurance, a consumer's loyalty will be shaped by elements such as security, trust, service and expertise.

The Survey we conducted illustrates four key areas that carriers and brokers should consider:

- **The consideration set and the importance of the Halo effect:** SMEs tend to get quotes from well-established players.
- **Price:** While price is important in the purchase process or in triggering a change of insurer, it is less important when it comes to loyalty.

¹⁵ McKinsey Australia Small Commercial Insurance Consumer Survey, 2017, n=405.

- **Distribution and digital:** Online channels are becoming increasingly relevant. They dominate the information gathering phase and are increasingly being used to retrieve quotes, but are still less utilised during the purchase phase, or are even available as options to purchase. Brokers remain a key influencer during the purchase phase.
- **Loyalty:** SMEs differ in their loyalty across segments; historically higher loyalty has correlated to segments requiring higher levels of service or tailored products.

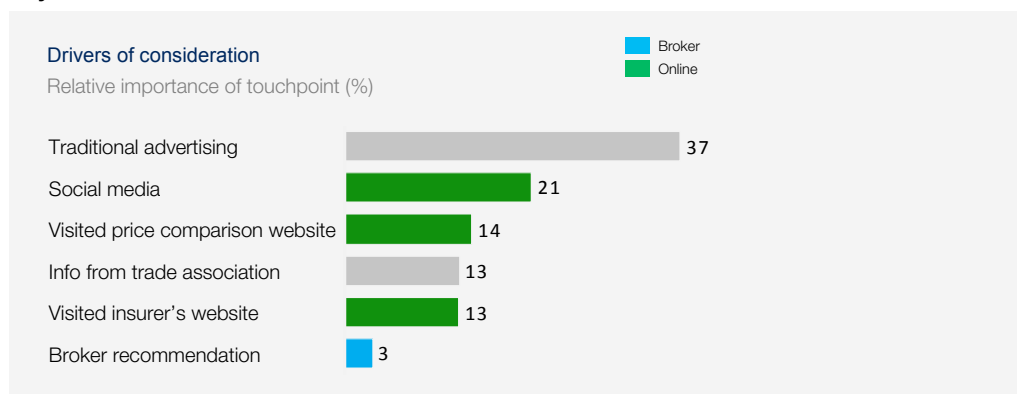
Falling into the consideration set: the Halo effect

The Survey found that small business owners generally consider three or four brands during the insurance purchasing process, and obtain quotes from two or three. At this stage, they will assess each short-listed brand according to the criteria of most importance to them. The critical question for insurers, therefore, is to understand how to position themselves in this limited set of brands that makes up the consideration set. There are some key strategic ways to do this.

The results of the Survey show that the first key strategic approach continues to be through traditional advertising. However, it is becoming increasingly important to complement this approach by using the latest digital marketing research techniques to assess questions such as: What emotional messages appeal to your target segments? How to best allocate the marketing budget to different media to ensure optimal impact? How to deliver a relevant experience that is ‘mass-customised’ but specific to the needs of an SME?

The second most reported driver of consideration for Australian SMEs was seeing an insurer mentioned in social media, emphasising the importance of effectively leveraging this rapidly expanding channel for reaching potential customers. Price comparison websites are the third largest driver of getting insurers into the consideration set, followed by information coming from trade associations, and finally, visiting the insurance company’s website. Broker recommendations are reported as less important for getting an insurer into the consideration set, but are highly important later, during the purchase decision.

Exhibit 5 – Traditional advertising, social media, and price comparison websites are key drivers of which insurers are considered¹⁶



¹⁶ McKinsey Australia Small Commercial Insurance Consumer Survey, 2017.

Price as the primary trigger for shopping and switching

When do SMEs start shopping around? As noted, our findings indicate the most common trigger is a price increase, either suddenly or gradually over time. Price changes matter, even if they are small; over 20% of SMEs that shop around were prompted to do so by prices that went up gradually, and 15% start to consider switching when the price rise is under 5%. When the price increase reaches 10%, over 65% of SMEs that shop around will consider switching.

The next most important shopping triggers are when a company expands into new products and services, or new geographies and locations that require insurance cover the business didn't already have. Cross-selling and making it easy for customers to add new products are two key ways insurers can prevent customers from switching in these scenarios.

Finally, SMEs reported that changes in their financial situation, and receiving recommendations from colleagues from similar businesses, as the next most likely events to trigger shopping for different or new insurance.

Exhibit 6 – Shopping and switching are most likely to be triggered by price increases and SME expansion into new products or locations¹⁷

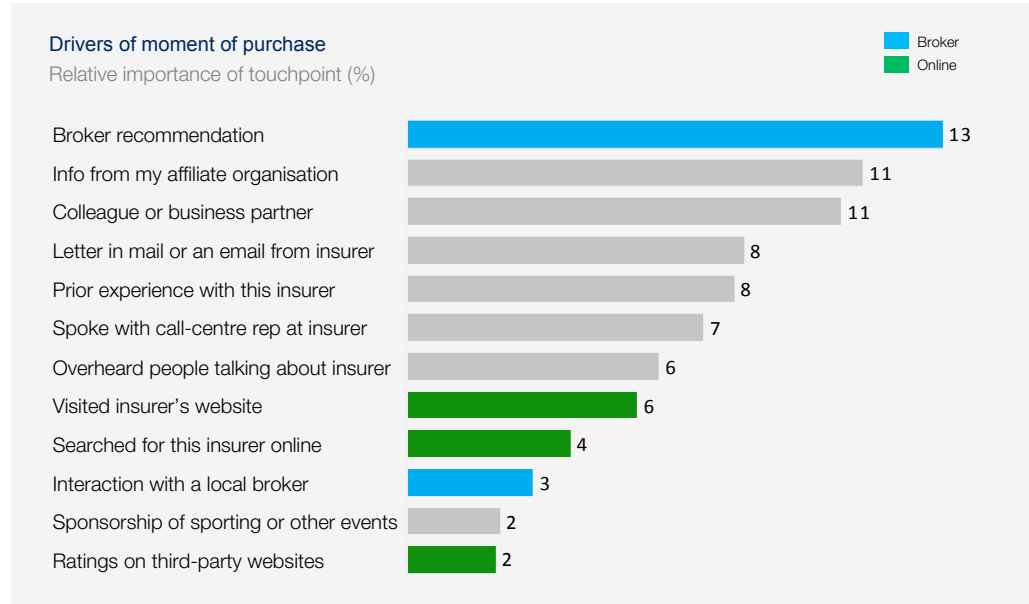


Price may be a critical factor, but it is not enough to win

Having entered the consideration set, insurers should consider their pricing strategy. As indicated from the Survey results, price is still by far the most important factor in purchasing, and at this stage of the process the relative importance of other brand elements drops significantly. Indeed, and perhaps unfortunately for some insurers, this means that the cheapest quote does not always win. Brokers – for those who use them – have the greatest influence at this stage, followed by recommendations from business partners and colleagues. Insurers therefore need to both ensure that brokers understand their value propositions, and sustain their reputations so that people recommend the carrier to SME peers.

¹⁷ McKinsey Australia Small Commercial Insurance Consumer Survey, 2017.

Exhibit 7 – Brokers and recommendations from other influencers are immensely influential¹⁸

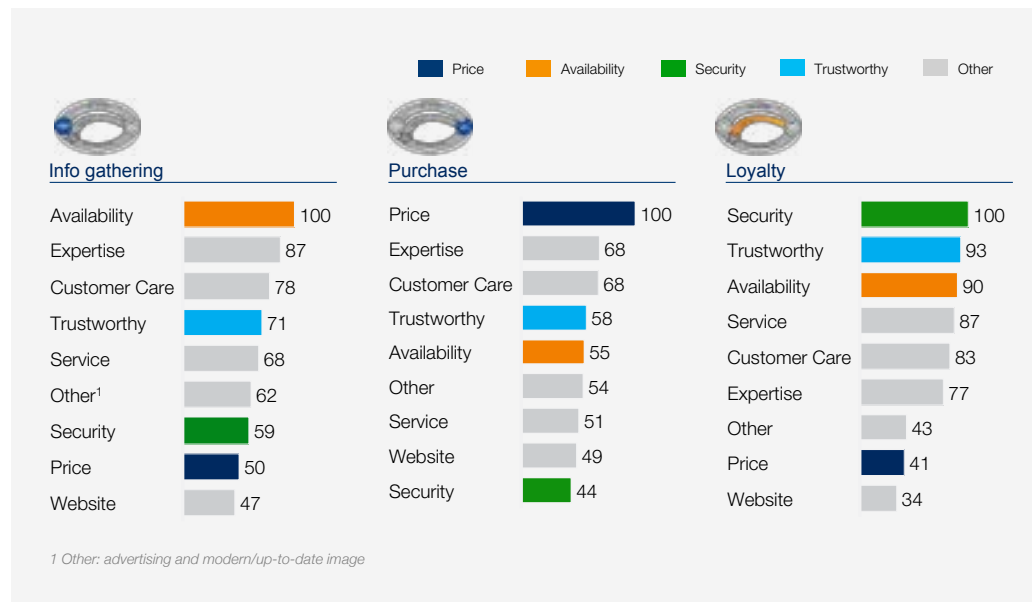


Although price is important at the purchase moment, it is far less important at the information gathering phase, and does not impact on the loyalty loop. To be top of the prospective customer's mind, it is critical for an insurer to ensure a high level of information availability exists about an insurer's value proposition to potential SMEs.

The next most important factors noted by respondents are expertise and customer care (87% and 78% of respondents responded that these were of relative importance, respectively). These are less important at the purchase phase, but return with more influence in establishing loyalty. The loyalty phase is dominated by a customer's sense of security and trust with their insurer, as well as continued ease of access to information about their policies. As such, the importance of building a reputation of taking excellent care of your business customers, and following through promptly on all commitments in order to build loyalty, cannot be overstated.

¹⁸ McKinsey Australia Small Commercial Insurance Consumer Survey, 2017.

Exhibit 8 – Different brand equity attributes drive success at different stages¹⁹



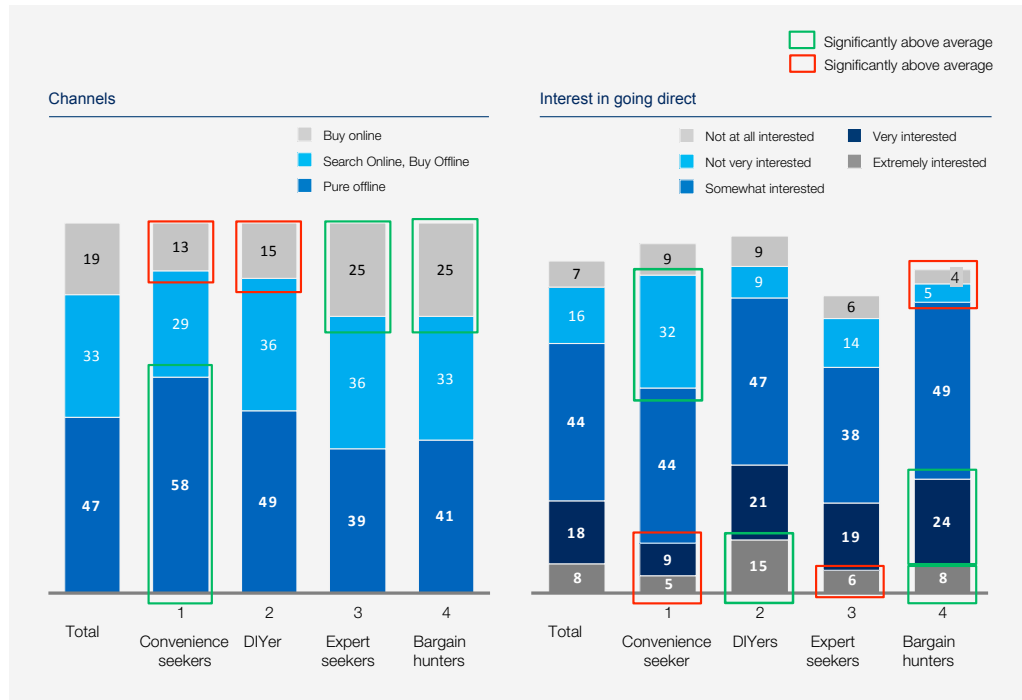
The digital channel is growing in popularity, and opens the door to lower-cost service delivery

Over 60% of SMEs surveyed use the online channel to research or find quotes for insurance. Larger Australian SMEs were found to be even heavier users of online channels than were sole proprietors and those with fewer than 11 employees. This means effective, powerful, and easy to navigate insurer websites and digital options are critical. Social media was the second most reported factor in getting an insurer into the mind of a consumer.

Online and digital channels present a new opportunity to insurers. These channels can do much to solve the level-of-service/cost-of-service tradeoff. New digital tools, which will be discussed in further detail later in this report, can streamline and simplify the process of providing information, quotes, purchase options and policy management abilities, reducing the cost of reaching the consumer on these points.

¹⁹ McKinsey Australia Small Commercial Insurance Consumer Survey, 2017, n=405.

Exhibit 9 – Segments differ on current channel use as well as in their interest in direct²⁰



The importance of loyalty and its variance across SME size and sector

The Survey results suggested that loyalty is generally low in the Australian SME commercial insurance market. This begs the question: what does it take to get loyalty right? When it comes to building loyalty for a brand, price simply isn't very important; loyalty is typically driven by emotional attributes around security, trust, and expertise. Customers who stick with their insurers trust them to keep promises, and are reassured that their businesses and livelihoods are well-protected in the case of a loss.

Loyal customers also often perceive their providers as experts in their specific industry. However, service-related elements, such as ease of doing business, customer experience, and responsiveness are also relevant. Questions to address here include: How can insurers provide their customers with these relevant and reassuring messages? And how can they show depth of expertise in the small business owner's industry?

Active loyalty varies by size of the SME according to Survey responses. While sole proprietors have the highest level of passive loyalty, they come in lower on the active loyalty ranking than their larger peers. SMEs with two to 10 employees exhibit the greatest degree of active loyalty at 31%; SMEs with more than 11 employees ranked second at 27%. Further, our research revealed a high degree of variability in loyalty levels across sectors. The finance sector led substantially in active loyalty at 45%, and in overall loyalty at 63%. Travel and transportation had the lowest level of active loyalists at a mere 10%, yet had the highest level of passive loyalists at 50%¹⁹. Understanding these variations in loyalty tendencies can help an insurer carefully craft retention strategies for their various SME customers.

²⁰ McKinsey Australia Small Commercial Insurance Consumer Survey, 2017.

Exhibit 10 – SME loyalty by size²¹

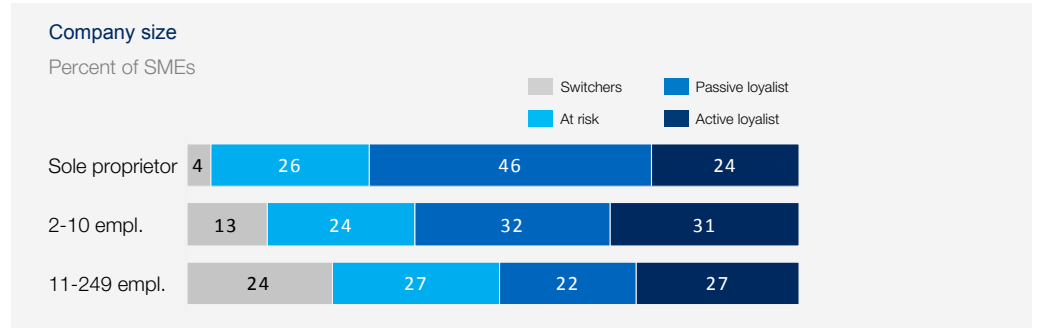
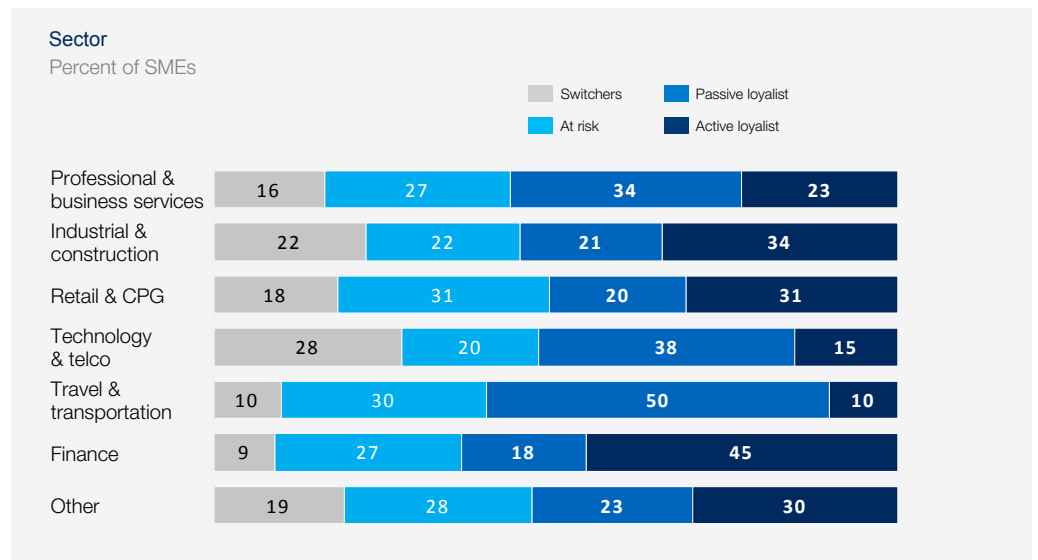


Exhibit 11 – SME loyalty by sector²²



21 McKinsey Australia Small Commercial Insurance Consumer Survey, 2017, n=405.

22 McKinsey Australia Small Commercial Insurance Consumer Survey, 2017, n=405.

4. What will it take to win in Australian SME insurance?

It is clear that understanding the potential opportunity in the Australian SME market requires a re-think of where to compete, what to offer, and how to operate. A single strategy to serve the market is unlikely to truly deliver emerging customer needs. Similarly, current insurer and broker go-to-market models may not work, as many are already struggling to deliver the level of service that SMEs demand at the premiums they are willing to pay. New, cost-effective models, including digitally-enabled models, should be considered in order to succeed.

Choose your approach: value versus volume

In a diverse market, providers should not try to be 'all things to all customers'. To thrive, insurers need to take a narrower focus and pick specific areas in which to deliver targeted propositions, with a sustainable and cost-effective operating model. The four SME customer segments are the starting point for such targeting decisions, but even these categories are too broad for a precise strategy. Winners will be those who select clusters of customers within the segments, grouped by industry or size, and develop specific value propositions and operating models to meet their needs. Insurers should select granular sub-segments targeting specific SME needs, based on their ability to create value for the customer.

That being said, the SME market highlights a classic trade-off that every insurer will need to resolve: volume versus value. Based on the Survey results, three of the four segments – online DIYers, expert seekers, and bargain hunters – taken together make up 71% of volume, but only 55% of value. The remaining segment – convenience seekers – make up only 29% of volume but account for the remaining 45% of value. This is because premiums for larger businesses in the convenience seekers segment are substantially higher than those for the remaining segments. Insurers will therefore need to develop distinct propositions for the value and volume segments. Digitisation, applied well, could help in addressing both opportunities for those insurers choosing to do so.

Leveraging capabilities across personal and commercial lines

Once an insurer has chosen where to compete, it will then need to build an attractive proposition based on its customers' needs, as well as its own capabilities and operating model. Winning value propositions will be those that show a deep understanding of the target customers' needs, while delivering a cost-efficient model to serve them. This will mean building distinct SME capabilities that cut across the characteristics of both personal lines and commercial lines insurance. Some of these capabilities will be tailored towards a new, professionalised SME business model (particularly focused around standardized / modular products that leverage increased automation and cost-efficient customisation). Others will differ by customer segments, in particular where client interactions are concerned.

For example, a proposition for 'volume insurers' may involve boosting marketing efforts to develop brand awareness around security, trust, or expertise, as well as investing in direct distribution channels and self-service capabilities.

'Value insurers', in contrast, may invest more in the skilled agent/broker channel to build and maintain customer relationships and increase loyalty, whilst still leveraging new digital capabilities to manage clients in a more streamlined and cost-effective way.

Based on an analysis of the Survey results winning propositions will likely need to take the following into account:

- **Tailored value propositions, services and customer experience:** SMEs generally expect insurers to demonstrate a solid understanding of their business and cover all their insurance needs. That will entail a much more segmented approach to customer propositions, with bundled products for specific micro-niches. Simplifying and reducing costs stemming from the underwriting process will also be critical. Digital tools can help in developing an optimised client experience, opening the door for personalisation, package comparisons, and easily accessible advice.
- **Consumer approach in brand building:** SMEs' choices and considerations go well beyond price when it comes to selecting their insurer and staying loyal to them. Insurers should invest in creating strong and well-recognised brands, built around both emotional (e.g. security, trust) and tangible (e.g. industry expertise, service) elements of brand equities. They should then organise to deliver efficiently against these promises.
- **Set-up in digital capabilities:** To be successful going forward, insurers will need to develop a digital environment and operating model. First, to master digital marketing capabilities and promote their brand and products. Second, to personalise and enhance the customer experience at each phase of the journey. Third, to serve efficiently a fragmented market of niches at scale through automated and lower-cost digitised processes.
- **Advanced analytics:** Capabilities such as external data aggregation and data mining, and pricing sensitivity modelling will allow insurers to increase pricing sophistication. These will also be able to predict client churn and identify ways to mitigate this risk. Finally, algorithms/analytics will provide automated advice (e.g. with the use of robo-advice, chat-bots) and raise customer awareness of risk exposures and risk transfer options. Sophisticated data analytics can also assist in enhancing cross-sell opportunities to personal lines customers where they are identified as also being business owners.
- **Ecosystems of partners:** Insurers should review the way they consider the SME market in order to increase their market awareness, third-party recommendations, and access to capabilities and risk coverage. They have to create new distribution and affinity channels to access cohorts of customers through trusted relationships (e.g. with banks and trade associations). Partnerships with specialist insurers may allow them to grow their product portfolios and offer clients broader sets of products to better match their needs.

There will still be space for other players in the market who can deliver their propositions:

- **Brokers** will continue to add value by providing expert advice to their clients, and can bring value to insurers by managing operational complexity, distribution cost exposure and first-level client support. Digital tools can also assist them in managing their work and can lower costs.
- **Bancassurers** have a privileged relationship with SMEs and need to combine this with a long-term insurance vision and providing adequate service levels.
- **Aggregators** and professional websites provide market knowledge and ratings based on user experience.

Winners in the SME market will be those who can master the traditional capabilities of commercial lines competitors (client relationships, product expertise, risk selection and underwriting, claims service, reinsurance) and deliver them to the market with the agility and consumer-orientation of personal lines' insurers (through digital access, customer experience, mass personalisation, simplicity, speed, cost efficiency). Insurers will need to find new ways of targeting customers and meeting their needs. Building new digital capabilities will be a critical ingredient for success in this market.

Conclusion

The Australian SME insurance market is at an inflection point: it is large and growing, customer behaviour is signalling a need for change, and technology is becoming ever more readily available and more powerful. Industry participants as well as new entrants can at any point seize this opportunity. Incumbent insurers who are willing to look at this market with a fresh perspective, carefully choose their segments to compete, overhaul their approach to target SME customers, and fundamentally upgrade their operating models have good prospects for improving market position – but the change is significant.

Indeed, competition will be tough: personal lines insurers are well positioned to address the SME customer opportunity; they have already put digital, data and analytics to work to create new models; and commercial lines insurers are often less technologically sophisticated, but have a deeper understanding of SME customer risks. New entrants, on the other hand, will not only more fully leverage technology and new approaches, but will also be free of the baggage of legacy books and operating models.

Traditional models must therefore evolve quickly. The boundaries between brokers, insurers and other market participants will increasingly blur, and different winning models should emerge. Insurers should leverage new technology and ideas to optimise their operating models for both the value play and the volume play.

SME insurers certainly face challenges as they seek to better serve their customers. Those that adapt will thrive while those that stick to old models risk being left behind. The time for action is now.

About this report – methodological note

This report covers the market for commercial insurance for small and medium enterprises (SMEs) in Australia. SMEs are defined as business entities registered in Australia with fewer than 250 employees, according to the definition used by the Australian Bureau of Statistics.

This report is based on the findings of the McKinsey Australia Small Commercial Insurance Consumer Survey conducted in January 2017, and other research conducted by McKinsey & Company.

This report is part of a series of McKinsey & Company surveys and research efforts related to SME insurance conducted across a number of geographies.

The McKinsey Australia Small Commercial Insurance Consumer Survey is an online survey of more than 400 Australian small business decision-makers with direct responsibility for buying insurance. The surveyed population includes a diverse mix of companies by product mix, industry, size, region and brand of insurance product used. Sole proprietorships (one employee), small enterprises (two-10 employees) and medium enterprises (11-249 employees) are all represented in the sample. Industries represented include professional and business services, industrial and construction, retail and consumer, technology and telecommunications, travel and transportation, and finance amongst others.

The McKinsey Australia Small Commercial Insurance Consumer Survey is focused on understanding the needs of SMEs in Australia with respect to commercial insurance and their underlying motivation at each stage of their decision journey when buying commercial insurance for their enterprise. It examines the key 'triggers' to which buyers of SME commercial insurance in Australia react, 'key drivers' that result in the response, and 'touchpoints' that are most effective for influencing the customer at each stage.

The Survey investigates how decision-makers in SMEs choose their insurance and their preferences in terms of products, channel and brands; and the various segments of customers that exist in the market for commercial lines insurance for SMEs in Australia today. In addition, the Survey looks at how various brands have performed across these dimensions.

This Survey was designed as a guided quantitative survey administered online. It was completed by commercial insurance decision-makers selected through panel screening.

Various types of analytical techniques have been used to draw findings from the Survey, including but not restricted to, relevance analysis (through correlations), consumer decision-journey modelling (through step-wise logistic regressions), clustering, and factorial analysis.

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