

# The New Insurance CXO

By Marek Jakubik

One of my long-standing observations is the insurance business culture undervalues operations and IT. To be fair, this bias seems pervasive throughout all economic sectors. In all industries, managers and executives overwhelmingly associate corporate glamour with deal-making, buying, or selling. Mergers, acquisitions, new product campaigns, and major restructuring are not only easier to explain than redesigning customer service or transforming product development but also offer much quicker gratification. In most insurance companies, there seems to be a clear hierarchy: strategy and finance on top, sales and marketing in the middle, operations and IT at the bottom. Yet it is the ones held in the lowest esteem—operations and IT—that offer the biggest chance of improving carriers' fortunes.

The evidence already is visible as some of the most forward-looking companies in the U.S. and Europe have been marching quietly toward new standards in operational innovation. Yes, not just operational excellence but an iterative process of improvement supported by a new culture capable of steadily generating new ways of streamlining and improving key business processes.

Some, such as the French AXA, are adopting strategies and practices well tested by manufacturers. In 2002, AXA hired Claude Brunet, previously chairman and CEO of Ford France Automobiles, where he successfully implemented a number of improvement programs. As AXA's management board member and chairman of AXA Technology Services, Brunet has become responsible for a comprehensive program of process improvement. In the first two years, Brunet says in an interview with *The McKinsey Quarterly*, AXA eliminated €1.3 billion (\$1.5 billion) from its expenses; however, cutting costs was only part of the challenge. An equal effort was directed at improving effectiveness and quality.

Brunet relied on approaches adapted from manufacturing: Six Sigma, cost-modeling analysis, and internal benchmarking. In effect, AXA was reusing more than 30 years of manufacturing experience by applying proven tools and methodologies. AXA does believe by targeting the processes of differentiation, improving those processes, and managing them for results, it will create a sustainable competitive advantage.

## **Closer to Home**

Progressive Insurance has set an early example of using operational innovation to create a competitive advantage. Progressive didn't achieve its success through acquisitions, clever marketing, or a flood of new products. Instead, it fostered a new culture directed toward inventing and deploying new, smarter ways of doing work. In the '80s, Progressive was focused on segment-based, finely tuned underwriting and pricing. To maintain its competitive position, in the '90s it built a superior claims service followed by a capability of competitive quoting. A steady stream of innovative improvements produced a simple result: lower prices and better service without sacrificing the margins. And, of course, another key point—none of the Progressive pioneering efforts would have happened without innovative use of IT.

The Progressive story is a prelude. It heralds the arrival of the next strategic battleground for insurers: a focus on operational innovation coupled with IT. This makes sense only if you consider the following three points.

One, in most lines, and especially in large volume or regulated, the insurance product has become a mass-market commodity. Insurance companies have difficulty with differentiating themselves and convincing customers it makes sense to deal with them rather than their competitor. Opportunities for breakthrough innovation are very limited.

Two, most insurance processes are not just dependent on IT but deeply embedded in the information systems (and those that are not will be). More and more often the only people in your company who really understand the working of processes are the systems analysts.

Three, information systems are for carriers what factories are for manufacturers. They are their biggest, most valuable nonhuman assets. They also are their biggest, underused levers.

## **How to Play the Game**

To make their companies newly competitive, CEOs, CFOs, and boards of directors will have to master the game of operational innovation. And for that game, they will need a new player: the chief process officer. This new role will be a challenge but also an opportunity for many ambitious CIOs.

The executive search firm Egon Zehnder International recently reported the results of a survey dedicated to the future role of the CIO in the financial services industry. EZI concluded future CIOs would tend to be change-oriented business drivers who also will direct the redesign of organizational structures. The study projected the classical interpretation of the CIO role no longer will exist in a few years' time.

According to the EZI report, "The CIO of the future will be the CEFO, or chief efficiency officer. Along with the IT organization, he will also be responsible for an operational or business unit within which IT plays a significant part. To this end, CIOs will have to actively change both their leadership role and their traditional field of responsibility." (The chief efficiency officer is another name for what I call the CPO.)

The preparation for such a transition already is well under way. EZI outlined three prerequisites for CIO-to-CPO/ CEFO development:

- CIO at the executive board level,
- centralized IT, and
- combining responsibilities for IT with responsibility for business operations.

As an industry, insurance has been relatively aggressive in promoting CIOs to the executive level. For example, it has a notably higher proportion of management/board-level CIOs today than banks.

It also is interesting to note from the ease-of-transition perspective, midsize carriers have a distinct advantage over their large peers. While centralization still is the principal challenge facing large-carrier CIOs, IT at tier-two insurers already is almost uniformly centralized.

On the other hand, combining IT and business responsibility in insurance still is a rare exception.

### **Two Down, One to Go**

So, let's say the first and second prerequisites are being addressed and focus on the challenges of taking the final step. As I see it, two issues will stand out:

- organizational and cultural barriers, and
- the CIO's readiness.

Cultural barriers stem from the fact very few senior executives understand operations. They tend to focus on strategies, marketing, financials, and regulatory issues while prac-

tically ignoring operations. As author and reengineering consultant Michael Hammer wrote: "An insurance CEO once quipped that managers work hard at operations so they can be promoted to the executive level, where they can stop worrying about operations." Let me re-quip: Very few of the insurance executives I've met ever got their hands dirty in operations. As a consequence, very few of them look to operations for competitive advantage.

The other obstacle on the road to operational innovation is simple: Nobody owns it. Occasionally but only implicitly ownership is assigned to the CIO. Such an occasion always is related to a major system implementation when an organization has no choice but to tackle the processes that often cross interdepartmental boundaries.

How do CIOs do in those circumstances? On the whole, and judging by the popular opinion, rather poorly.

Of course, this should not be surprising. What would you expect from a system where responsibility is implicit, accountability undefined, capabilities haphazard, and tools mostly nonexistent? I say give those CIOs who succeeded despite all this a medal!

Seriously, though, what should an insurance executive convinced operational innovation is worth pursuing do? Two key things are: Choose the right strategy, and find a leader.

Operational innovation is by its nature disruptive for an organization. The right choices have to be made to focus on those processes that bring the highest strategic value. It may mean processes that increase customer retention, reduce claims expenses, or reduce time to market. No organization can attack them all at once. It took Progressive about a decade to build its current machinery. And it hasn't stopped. Progressive continuously is adding and improving—a very important cultural element common to companies that mastered operationally driven innovation.

As to a leader, I've already dropped a hint. First and foremost, insurers should look to their CIOs. Many of them display the key competencies required for the CPO job: They demonstrate a high level of leadership, they are customer and market oriented, they have a firm understanding of processes and technology, they are tena-

cious, they can think and act outside the box, and they have strong strategic aptitude. If on top of these traits a CIO shows strong business acumen and has proven to be result oriented—you have a winner!

Of course, the risks are high. The individual and organizational talents required to transform a company so it thinks and acts in holistic terms across all units and to drive far-reaching change requires skills, commitment, and full support at the executive and board level. However, that also means those who succeed will enjoy a sustainable advantage for many years. (How many years do you think it would take your company to emulate Progressive?) Moreover, the operational innovation is based on incremental change, both in an operational and cultural sense. Once a company reaches a new level, it also is better prepared to move to the next.

Companies in other industries have practiced the operational innovation evolution for more than 20 years. Many have mastered it. Is it time for insurance companies to follow their path?

Speaking with McKinsey, AXA's Brunet thinks so: "If you want to innovate, you must always do so in a cost-effective, predictable way, and for that you must master your processes. Excellent manufacturers know how to do this. We will, too."

2-Column Text

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