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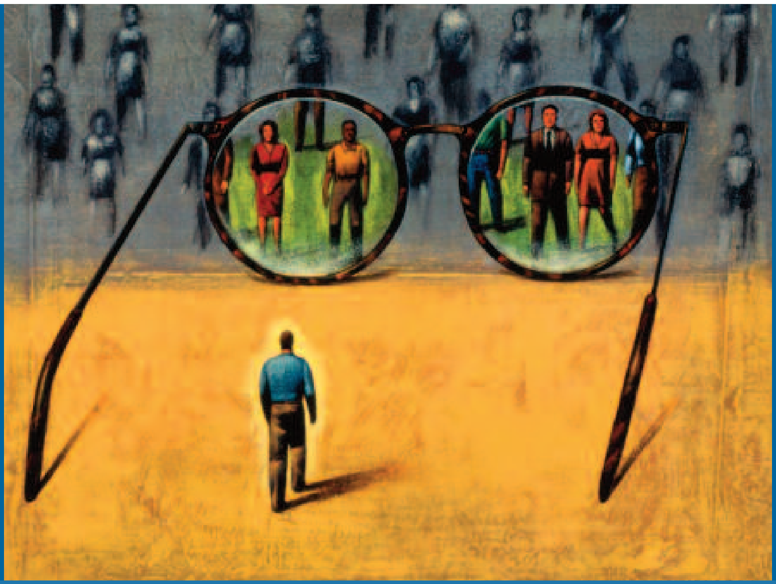

Beyond Price: The Rise of Customer-Centric Marketing in Insurance

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Contents

Introduction

Over the past decade, U.S. auto insurers have increased their marketing expenditure 15 percent each year. Spending totaled almost $6 billion in 2011 alone. A simple logic propelled this marketing "arms race." As one carrier increased its level of spend to gain customer awareness, others responded in kind to keep up.

But the equation omits a true reckoning of how *effective* the spending is. The explosion in marketing spend has had no measurable impact on industry premiums, which have remained stagnant. And more than half of the marketing dollars spent in the last 10 years came from carriers that *did not gain share*. Clearly, in their eagerness for top-of-mind consideration, auto insurers are missing something crucial about what their customers need, how they shop and how they make decisions.

The disconnection of escalating marketing expenditure and the realities of consumer behavior raises fundamental questions for senior leaders of auto insurance carriers, as evidenced by the findings of recent McKinsey research:

- **Marketing spend in auto insurance is targeted disproportionately at the 30 percent of auto insurance buyers who are most price-sensitive and least loyal.** Why have insurers aimed so much marketing firepower at this one segment? What determines whether the other 70 percent will remain loyal or shop around? How can insurers reach this majority and motivate them to switch?
- **Consolidation of market share at the top of the industry appears set to accelerate, as shoppers typically consider only four or five brands as they begin their shopping journey.** What sustainable options and mod-

els exist for insurers outside of the top five? What alternatives exist for insurers unwilling or unable to compete in the current spend-for-consideration model?

- **Digital and social media channels influence 40 percent of consumer decisions made during the consideration phase.** Can auto insurers – especially those outside the top five – use digital channels to influence shoppers during the active evaluation phase in the consumer journey?
- **Car insurance retention hovers around 90 percent, yet virtually all marketing spend is focused on acquisition.** Given escalating acquisition costs, and the fact that strength of loyalty within a carrier's policyholder base varies significantly, how do carriers find the right level of marketing spend and the optimal balance between attracting new customers and holding onto their valued policyholders?

The answers to these questions will differ for individual insurers, based on their current position and business model. But they are questions that all insurers should address as they adapt to changes in how customers evaluate and purchase an auto insurance policy.

This report is based on the results of McKinsey's 2012 U.S. Auto Insurance Buyer Survey and numerous interviews with marketing executives. It highlights new research on auto consumer needs and behaviors, and describes the core marketing capabilities that will define industry leaders for years to come.

Beyond Price: Changing Insurance Shoppers

In 2011, the personal lines insurance industry spent nearly $6 billion on marketing, more than three times what they spent in 2002 (Exhibit 1, page 6). Auto insurers have vaulted up the list of advertisers in corporate America (Exhibit 2, page 6). But the results of these investments have been mixed at best. While marketing spend has increased by a robust 15 percent per year, industry premium growth has been stagnant. In the last decade, $19 billion, more than half the total marketing spend for the entire industry, came from carriers that did not gain share.[1]

For a small number of individual carriers the marketing arms race has yielded gains in market share. These winners are likely to continue to thrive in the current marketing paradigm. But the industry as a whole is treading water; some carriers are spending heavily for broad brand recognition and have little to show for it.

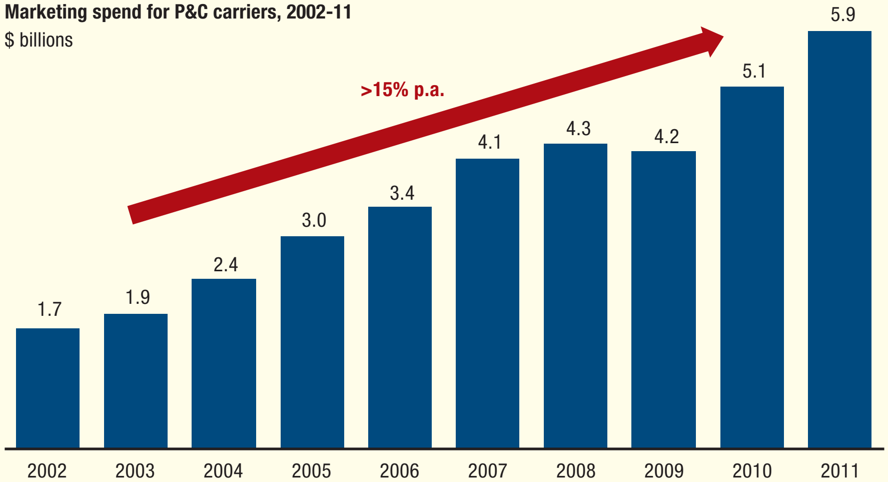
Why has insurance advertising not been more effective? The answer appears to be that most advertising is based on an overly simplified view of the insurance consumer. For a percentage of insurance shoppers, saving money on their policy is indeed of paramount importance – but they are by no means the majority. The number of customer segments, and the

[1] This breakdown for marketing spend mainly reflects the failure of these companies to attract enough customers; to a limited degree it also reflects efforts by some large carriers to lower exposure in certain states.

Exhibit 1

Marketing spend for U.S. personal lines insurers has increased dramatically

Marketing spend for P&C carriers, 2002-11
$ billions



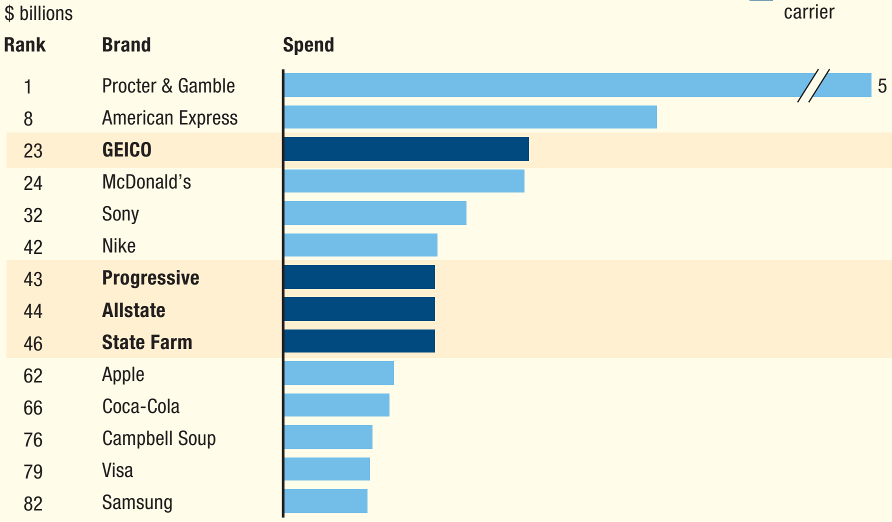
Source: SNL Financial

Exhibit 2

GEICO spends more on advertising than McDonald's, Nike or Coca-Cola

2011 ranking based on U.S. advertising spend, selected brands from top 100
$ billions

P&C insurance carrier



Source: AdAge

range of motivations that drive decision-making within each, are much greater and more complex than has been assumed. To maximize return on their marketing investments, insurers will first need to develop a more sophisticated understanding of customer segments and how consumer needs shape their shopping behaviors. New approaches based on those insights can then be designed.

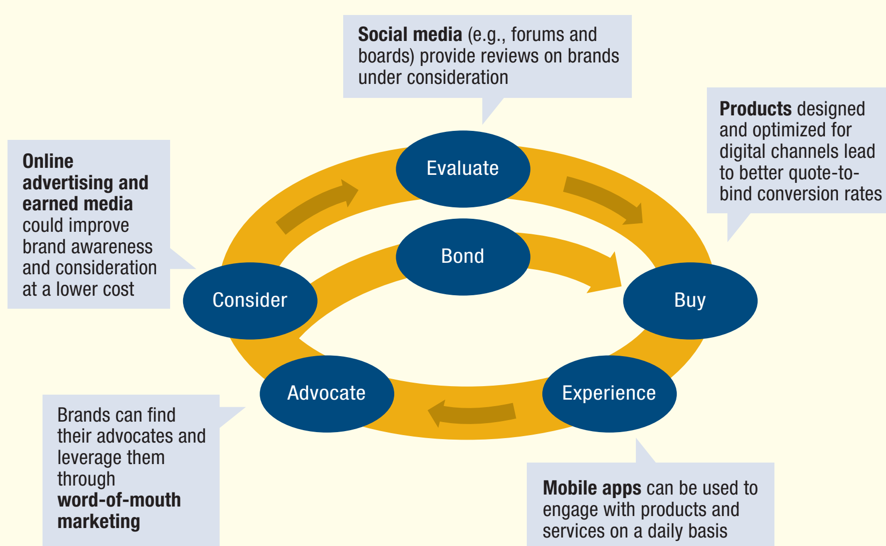
How auto insurance consumers shop today

Many auto insurance consumers begin their shopping journey with four or five brands in their consideration set, and historically most have chosen a policy only from among these brands. Today the process is changing dramatically; it is becoming more dynamic, and brands are not only dropped from the consideration set but *added* throughout the active evaluation stage. So while there is significant competitive advantage in being one of the few brands in the initial consideration set, it is no longer the only way to be in the running.

One of the major drivers of this shift has been the rise of the digital channel, which now plays an ascending and influential role at all crucial touch points on the consumer decision journey (Exhibit 3). Shoppers are exposed to

Exhibit 3

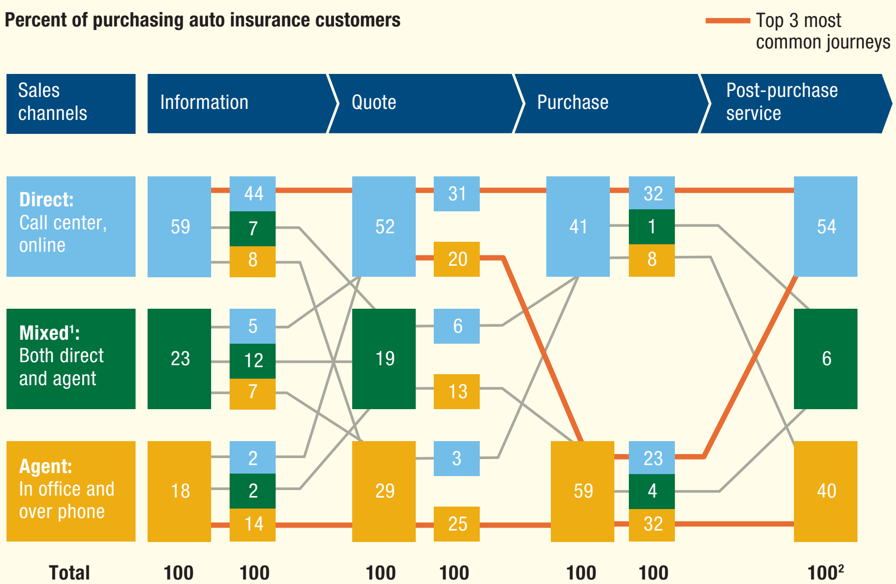
Digital media can make an impact at every point on the customer decision journey



Source: McKinsey P&C Practice

Exhibit 4

The Internet is the predominant research channel for insurance shoppers, even when they purchase through an agent or by phone



Note: Includes only shopper data

[1] Including online aggregators

[2] Normalized; some respondents may not have had servicing with current carrier at time of survey

Source: McKinsey Auto Insurance Buyer Survey, 2012

brands online through digital advocacy initiatives or online advertising, and feedback and open-online communities are also playing a role in consumer evaluation.

Another important driver of change in auto insurance shopping behavior is the growing presence and use of multiple channels. However they eventually finalize a purchase, consumers are increasingly using multiple channels on the way to their decision. They may conduct research online, contact a carrier's call center to ask questions, or reach out to their local agent. In fact, consumers are using multiple channels on the *same step* of their shopping journey. McKinsey research reveals that more than 80 percent of insurance customers began their shopping process using direct channels (Internet and call center), compared to 10 percent in 1998. Perhaps more tellingly, online is increasingly the initial channel of choice even among customers who value the agent relationship: about 60 percent of policyholders who purchased through an exclusive agent gathered quotes through direct channels (Exhibit 4).[2]

The blurring of distinct lines between channels complicates the marketing strategies for auto insurance carriers, because they can no longer segment customers based primarily on channel preference. This challenge is also, of course, an opportunity for insurers that can develop a more sophisticated and granular view of what drives customers decisions in each segment.

[2] The importance of multiple channels is more deeply explored in the paper "The Multichannel Imperative for Property and Casualty Carriers in Personal Lines," McKinsey & Company, March 2011

Core Marketing Capabilities for The Road Ahead

For U.S. auto insurers, the ability to grow profitably will increasingly depend on whether they can reinvent their approach to marketing. Only a few carriers will be able to sustain the high-octane advertising barrage that characterizes today's market. The top five insurers, each of which spends upwards of $500 million per year on marketing, have pulled away from the industry in terms of awareness (Exhibit 5, page 12). And even these leaders are realizing that the narrow focus on price-sensitive shoppers will not deliver sustainable profitable growth. For the rest of the industry, this competitive dynamic raises a strategic question: should they pay the price to command presence in the consumer's initial consideration set, or aim at converting consumers downstream in the decision journey?

Both answers demand a new approach, one that goes beyond tweaking an existing strategy or implementing a few innovative tactics. To thrive, insurers will need to develop a far more sophisticated view of the segments of insurance shoppers and customize their approach based on the specific needs and behaviors of consumers in those segments. They will also need to shift some of their attention to the sometimes overlooked challenge of retaining their valued policyholders. Finally, they must dramatically improve the organizational strength of the marketing function in order to consistently ensure sufficient return on their marketing investments and deliver on the promises they make to consumers.

Segmentation rules

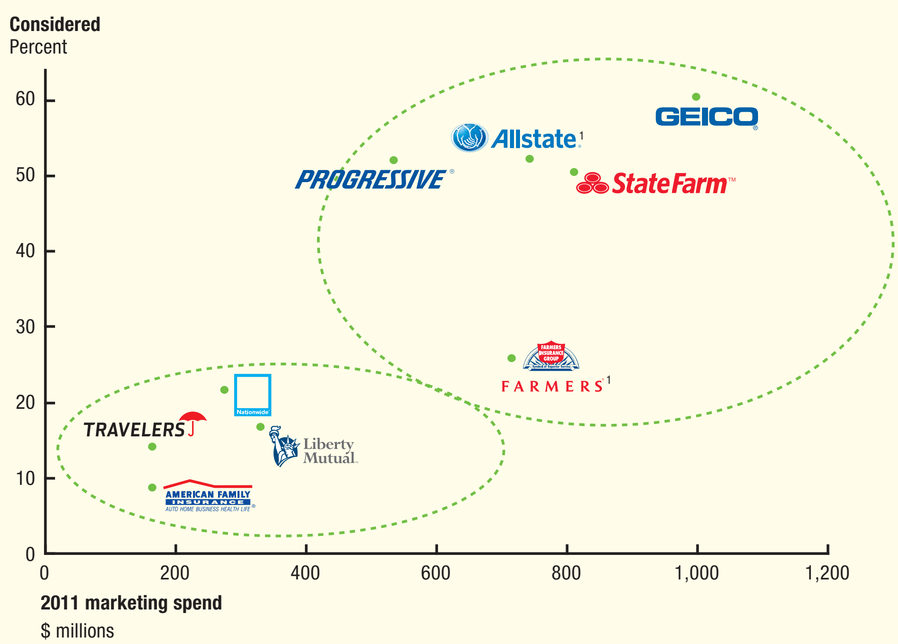
From the moment roughly a decade ago when GEICO and Progressive upended the traditional view of insurance shopping segments by focusing on price and convenience alone, most marketing messaging has focused relentlessly on price. Price-centricity has succeeded on one level: it has conditioned a segment of customers to shop – and frequently switch – at every renewal. But this segment is not as large or as valuable as the marketing firepower aimed at them would indicate. In fact, McKinsey's auto buyer research shows that over 50 percent of quotes come from price-sensitive customers

Exhibit 5

The top five spenders have pulled away from the pack in terms of brand awareness

Consideration versus marketing spend for U.S. personal lines carriers

U.S. auto insurance shoppers



[1] Esurance also enjoys 10% consideration; 21st Century enjoys 9% consideration

Source: McKinsey 2012 Auto Insurance Buyer Survey; JD Power 2012 shopping study; SNL Financial who account for less than 30 percent of policyholders (Exhibit 6). In other words, a very busy segment of serial shoppers make the price-centric marketing message appear more successful than it actually is.

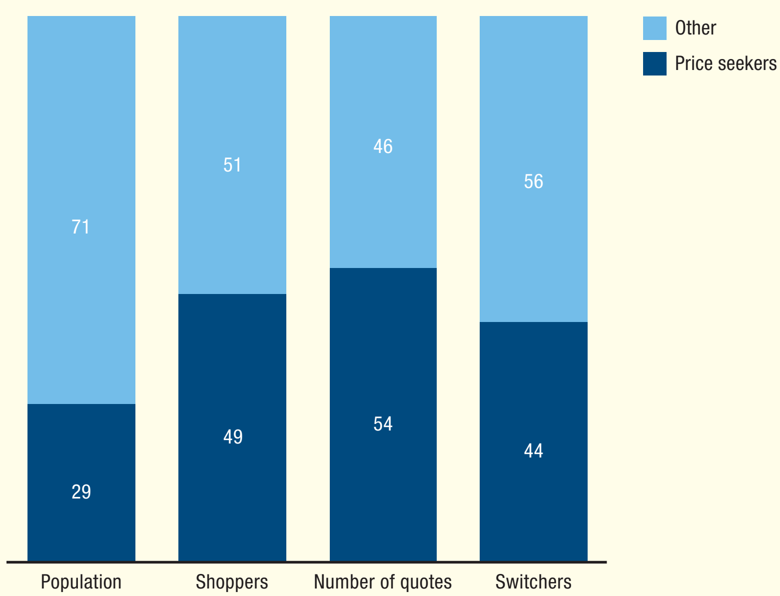
If the other 70 percent – the "silent majority" of policyholders – appears to be difficult to reach, this is likely because they are unresponsive to marketing messages based solely around *price*. McKinsey's Auto Buyer Survey results reveal that this 70 percent is composed of many distinct segments, each with differentiated needs, behaviors and preferences. Some carriers have been successful with one or two segments (e.g., GEICO with customers who value "ease of shopping" or State Farm with those who prioritize "protection"); others paint their customers with a broad brush, and miss the opportunity to sharpen their value proposition for specific segments.

Exhibit 6

30 percent of the consumer population accounts for over 50 percent of all quotes

Share of population, shoppers and switchers, by segment

Percent, 2012



Percent of total population	**100%**	**27%**	**27%**	**9%**

Source: McKinsey Auto Insurance Buyer Survey, 2012

An example segment, *loyal policyholders,* have varying motivations for staying with their carrier. The majority is *actively loyal*; that is, they are satisfied and renew without shopping because they value the relationship for one reason or another. A significant minority (18 percent) of loyal customers, however, is *passively* loyal. They stay put more out of inertia than from any active satisfaction. Insurers that can reach and dislodge these customers will open up new opportunities for growth.

The requirements of taking a segmented view of the insurance customer go beyond understanding preferences and needs. McKinsey's research shows that the relative importance of each stage in the customer decision journey, the brand equities that resonate and even the specific marketing vehicles that are most effective – all vary by customer segment. The most effective marketing efforts will therefore be those that are tailored both in terms of message and medium.

One way to focus marketing efforts on specific segments is to develop stand-alone microbrands, a trend that emerged recently in the U.K. in the context of heightened price competition. Admiral, a British auto insurer, launched its Diamond brand, targeted at women; Elephant, focused on online-only consumers; and Bell, focused on rewarding drivers with low claim activity. In the U.S., a few sub-brands have emerged to broaden market appeal at carriers such as Allstate (Esurance) and Farmers (21st Century, Foremost and Bristol).

To succeed in a segment-based approach to marketing, auto insurers should keep the following imperatives in mind:

- Target segments based on an explicit appreciation for *lifetime value* of the customers.
- Develop a deep understanding of segments' needs and behaviors, *at every step in the consumer journey.*
- Follow through with targeted strategies, and f*ocus on offers that provide a call to action* for customers to make the switch.
- To support their more sophisticated views of segments and tailored marketing messages, insurers must be able to *track the effectiveness of each tactic by channel and segment.*
- *Dislodge competitors' passively loyal* customers with value propositions and calls to action tailored to their unmet needs.

Digital weapons

TV commercials and other traditional media may still be the most visible form of auto insurance marketing, but carriers are gradually adopting new digital tactics such as targeted paid search campaigns, search engine optimization, banner ads and social media. Digital marketing is fast becoming a major battleground in the auto insurance marketing wars. Brand reputation and word-of-mouth recommendations in particular are now strong drivers of consumer choice in insurance (Exhibit 7), and a handful of carriers have launched social media campaigns via carrier-sponsored Facebook fan pages, Twitter accounts and even games. But the scale of social and digital marketing in insurance still pales in comparison with that of the leaders in other categories such as Starbucks, Procter & Gamble and Coca Cola. Insurers that can rapidly build capabilities and sophistication in the digital arena will be well-placed to grow.

Exhibit 7

Brand strength is the strongest differentiator across customer segments

Most significant

Need	Examples
Brand strength	I'm willing to work with a brand that is not well known
Preference to shop	I like to shop around
Personal relationship	It is important for me to work with someone who knows me personally
Access to local agent	I prefer to work with a local agent
Personal claims help	I want a specific person accountable when I have a claim
Price	I want the lowest price
Ease of purchase	I want to make purchases online
Advice	I tend to follow the advice of my agent
Coverage	I am willing to pay to get better coverage

Least significant

Source: McKinsey Auto Insurance Buyer Survey, 2012

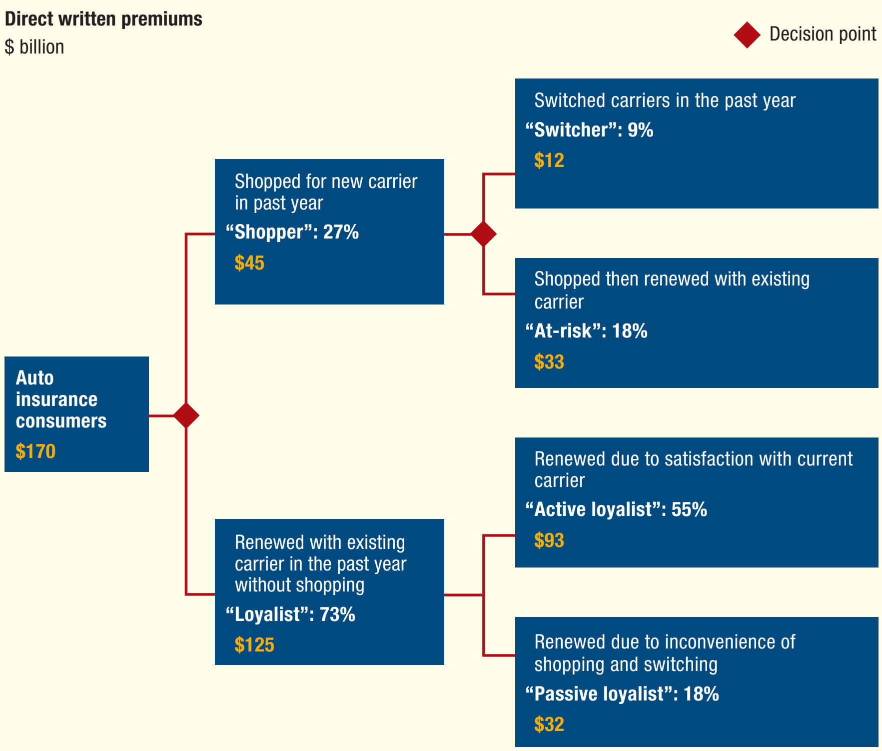
Retention is the new holy grail

Marketing in the insurance industry has historically focused disproportionately on *acquisition*. Hence, vast amounts have been spent on above-the-line, mass market advertising to drive brand awareness. However, marketing messages inducing shopping based on price are driving more customers to view the policy as a commodity, leading them to shop and switch more frequently.

The combination of higher acquisition cost and lower retention for frequent shoppers drives up the relative value of retaining existing policyholders. For large carriers, each percentage point of increased retention is equivalent to a boost of several points in brand awareness. In light of this, carriers must recalibrate their marketing efforts to achieve a better balance between acquisition and retention.

Exhibit 8

27% of consumers shopped for a new carrier in 2011; 9% switched



Source: McKinsey Auto Insurance Buyer Survey, 2012

While retention in 2011 was 91 percent (up from 2008-2010 levels), this is not a cause for complacency. Among the "loyal" majority of policyholders, 18 percent remained with their carriers only after shopping and comparing quotes (Exhibit 8). Protecting the valuable customers within this group as well as the actively loyal customers against attackers with aggressive growth objectives is critical to the survival of many carriers.

Understanding the relative value of existing policyholders

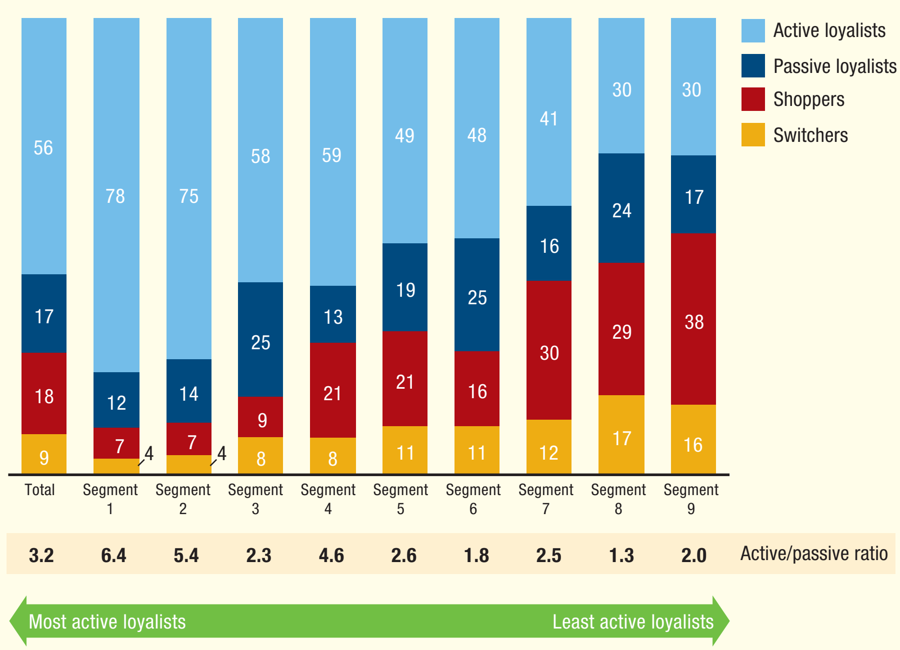
If joining the ranks of the initial consideration set for insurance shoppers is an exercise in blunt-force advertising firepower, retention efforts should be the opposite: a targeted, layered strategy to identify and reach high-value policyholders. McKinsey research shows that degrees of loyalty vary significantly from one segment to another (Exhibit 9);

Exhibit 9

Segments differ significantly in level of loyalty

Propensity to shop and switch by segments[1]

Percent



[1] Segmentation based on consumer needs

Source: McKinsey Auto Insurance Buyer Survey, 2012

most insurers, however, do not have a view of their customers' behavior and preferences that is nuanced enough to carry out a highly effective retention effort.

This is in part due to a tendency to segment policyholders based on pricing attributes and binding channel preference rather than on their needs. Once they have an accurate view of the needs-based segments that comprise their existing policyholders, insurers can determine which segments are worth actively defending. For instance, a percentage of a carrier's book is comprised of customers for whom price is all important. These serial switchers will more than likely leave for a competitor at their next renewal. Insurers must decide whether these customers are worth the retention efforts, or whether they should focus on retaining their more valuable loyal policyholders.

This is a complex challenge. Many touch points can influence a policyholder's decision to renew and a good number fall outside the direct control or influence of the marketing function (e.g., claims, problem-resolution). This means that retention efforts demand both strong marketing capabilities *and* the organizational alignment to deliver on the brand's promise consistently across all touch points.

Delivering on the brand promise

The emerging importance of segmentation and retention as elements of a successful marketing approach in auto insurance leads inevitably to the need for a third core capability: strength in delivering on the value proposition and brand promise that carriers make to their valued customers. The most sophisticated view of the needs and preferences of a valued customer segment will be for naught if promises made to those customers are not consistently kept.

This can be a tall challenge, because the touch points at which a customer can gauge an insurer's fulfillment of the promise run the gamut of the value chain, starting with the initial interaction with an agent or on the company Web site or Facebook page, through the billing and renewal process, all the way to claims and customer service.

The most sophisticated view of the needs and preferences of a valued customer segment will be for naught if promises made to those customers are not consistently kept.

To meet this challenge, the senior management team will need to assume collective responsibility for delivering target segment needs and developing effective customer engagement.

The Marketing Agenda for Auto Insurance Executives

Over the last 10 years the marketing arms race has reshaped the competitive landscape in auto insurance. This expensive battle for customer consideration is not going away. However, changes in consumer behavior and in the understanding of the diversity of auto insurance customer segments are presenting opportunities for new approaches to attracting and retaining those customers. Insurers with the tools and talent to develop sharp insight on the segments they want to reach – and the most effective channels and messages for swaying them – will make inroads. In the new age of marketing in auto insurance, sophistication, savvy and organizational strength will count for as much as spending power in the battle for profitable share.

To set an agenda for success, senior management teams will need to engage in a sustained debate around five strategic imperatives and important related questions:

1. **Target customer segments with compelling marketing messages.** Which segments fit best with our strategy and value proposition relative to the competition? What brand equities and marketing touch points are most effective for our target segments? How do we strengthen our understand-

ing of consumer needs, and make decisions on where and how to invest in meeting those needs?

2. **Get more mileage from marketing spend.** What is the optimal level of marketing spend and the right media mix across multiple distribution channels, geographies and customer segments?
3. **Balance acquisition and retention marketing.** What is the right balance between acquisition and retention? What strategy, investments and tactics will help us successfully retain consumers?
4. **Upgrade marketing organization and capabilities.** What capabilities should we build versus buy? What organization structure will deliver greatest impact? What talent do we need, in which roles, and where can we find it?
5. **Ensure senior executives are engaged in the marketing challenge.** How do we make sure that our business executives understand and drive our marketing agenda, and that they support a strong marketing function?

* * *

Auto insurance shoppers are not as single-minded as the advertising aimed at attracting them would indicate. There are multiple segments, and the consumers in each of these segments are driven by different needs and preferences, and respond to distinct messages at distinct touch points in their shopping journey. All of which is to say that marketing in auto insurance is not a simple challenge.

Fortunately, this challenge is also an opportunity. Auto insurance marketers that begin to grapple with this complexity and translate new marketing insights into new marketing strategies will be well set to grow in the coming years.

About the McKinsey Auto Insurance Buyer Survey

For the McKinsey Auto Buyer Survey 16,000 car insurance shoppers were surveyed in June 2012. The survey explores the reasons behind shopping and switching behaviors by customer segments as well as the performance of carriers, brand equities, touch points and marketing techniques along the consumer decision journey.

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