PRODUCT AND PORTFOLIO MANAGEMENT

Developing the Right Product, the Right Way, at the Right Time to Balance Pricing and Exposure

> *"Innovation is not the product of logical thought, although the result is tied to logical structure."*
> Albert Einstein

Insurance Product and Portfolio Management is about targeting the right risks at the right price and controlling the individual and aggregate risk relative to corporate standards, financial capacity, and reinsurance considerations. A key element is developing innovations that keep the offering competitive and ideally differentiate positively against competitors' pricing and support processes.

The coordination of product and portfolio analysis represents the life's blood of future success, but it requires a hard assessment from different functional perspectives of capital requirements, underwriting risks, regulations, actuarial assumptions, and exposure analysis involved in any product or service change. For example, moving into a new insurance market with a new product or service offering is a high-risk activity that involves well-thought-through internal technology and external distribution plans. Success is rare.

Equally rare is successful development of a product offering that fundamentally changes the value proposition within an industry, e.g., Internet banking. Such new innovations require deep financial commitment. When success does occur, it needs to be understood. Pricing or underwriting inadequacies may prove the success in a different light. Conversely, the adage "too much of a good thing" can skew portfolio exposure or even service levels.

Product and Portfolio Management must find the right balance among insurance coverage pricing, reinsurance, and related loss control services for claims and subrogation that complete the insurance results evaluation cycle. While working closely with Marketing, a key consideration is to understand customer requirements across the total relationship. Being clear on the customer needs while defining the product coverage and service solution that delivers key benefits is a critical success driver within Product and Portfolio Management. The primary challenge is to define a risk retention relationship that drives renewals based on satisfaction with price, value, and service.

Economic, demographic, and industry cycles set the context for the importance of innovation, and its role within Underwriting and Product and Portfolio Management. In fast-growing market segments, product change, coverage adaptation, and distribution fulfillment are part of the competitive race, and significant investments are likely. In mature markets, where growth has slowed, the commoditized context will push Product and Portfolio Management less towards innovation and more towards designing cost savings into the offering. Nevertheless, new developments can help slow the rate of market commoditization and protect margin erosion. These are likely to be incremental, and small advantages can differentiate a leader from less successful followers.

Product management and portfolio alignment are a combination of opportunity identification, evaluation, and new product and service implementation. A pipeline of incremental and more innovative changes will help determine the insurance company's future financial performance and ability to identify organic growth opportunities. Three significant barriers prevent it from delivering the required product changes in the most effective way.

Barrier 1: ***Lack of information to determine strategy requirements***

Evaluating the impact of product and service changes is difficult without access to several sources of information, both internal and external. The insights from these multiple sources need to be integrated into a commercial framework that offers granular clarity and strategic assurance. Insurance Product and Portfolio Management takes the "size of prize" discussion in Marketing further into product and service specifics.

For example, what insurance package could the company design for policyholders in a given age profile, say, below 30, that accounts for their current and future life-stage needs? For those who feel the pinch of financial pressures when life expenses exceed earnings, insurance companies could offer creative solutions to alleviate initial payments. However, product innovation embraces risk. The odds are stacked against continual success, and executive expectations need to be managed carefully.

Measuring financial performance is vital, but interpreting success too rigidly may lead the insurance company to miss innovation opportunities. It is better to define and measure drivers and development milestones that affect the pipeline of new initiatives. Similar to a portfolio investment strategy, these metrics allow for more opportunities (and therefore more failures), but let you know when to "fail fast" to satisfy the overarching premium growth goal.

Only a few product initiatives make it through to financial success. What resources need to be invested in a given initiative? What human capital skills are required? Does the initiative impact internal processes and require infrastructure changes? These costs will need to be evaluated and often incurred before there is any assurance that premium revenue targets will be achieved. The tolerance for calculated financial failure regarding new initiatives will vary by institution. Certain initiatives will be seen as more strategic and critical, while others will not be as important. A portfolio approach to new initiatives helps prioritize resource requirements, expectations, and risk tolerances.

Product and Portfolio Management needs input from Marketing, Claims, and Sales into product and service trends as well as insight into customer segment behavior. Equally the development process needs to work with Actuarial, Underwriting, Reinsurance, and Compliance with regards to shaping the offering. Financial engineering and solutions that leverage cash flow or external specialist providers are increasingly critical to innovation success. Strategic considerations will have an impact, for example, on leveraging the company's distribution network to focus more on new sales opportunities through specialists in parallel channels. Only by integrating all these business inputs and information sweet spots can you achieve a well developed new initiative.

Barrier 2: ***New product and service initiatives lack the integrated business process information needed to develop targeted, comprehensive product offerings***

Product and Portfolio Management alignment decisions affect and rely on Marketing, Sales, Claims, Underwriting, Finance, Actuarial, and other business departments. Without appropriate visibility, departmental barriers may get in the way and stymie the Product and Portfolio Management alignment process. By monitoring the appropriate performance drivers, combined with appropriate incentives, you can improve the Product and Portfolio Management process from idea generation to alignment on priorities to engaging Finance, so the value of new initiatives is understood and forecast.

Barrier 3: ***Inability to define, measure and analyze the drivers of success***

New initiatives depend on timely action, but are hampered and even blocked by the lack of clarity and calculated assurance that any resource investment will lead to a sufficient reward. What are the drivers of success? Have they been measured, evaluated, and communicated effectively? Enterprise risk management analysis is part of the development process. Past failures are not necessarily negative; they may actually assist the development process. Failures can become stepping stones toward success. The key is to understand what drives insurance portfolio success and failure. When new initiatives reach a certain milestone, the department may consider working with Marketing to test the product proposition in the market. The feedback you require will determine the means you select: selective customer input, larger external research, or a limited territorial launch.

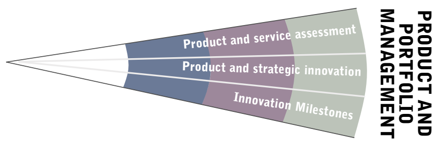
No amount of testing guarantees success. Making the "go or no go" decision requires information sweet spots to allow the business to decide whether it needs more resources to improve the new offering, or if the cost of delay—either in lost revenue or lost competitive advantage—means the product initiative must launch now.

From a Gamble to Controlled Product/Portfolio Management

Product and Portfolio Management combines many cross-functional requirements, balances risk, learns from failures, then both adjusts and develops new product and service initiatives in a timely and effective manner. Accurate information is a key enabler of this process.

The product development process combines three key decision areas with associated information sweet spots:

- **Product and service assessment** ➔ What is our value proposition, and does our product coverage and service portfolio meet customer, market, and regulatory compliance requirements?
- **Product and strategic innovation** ➔ Which strategic initiatives and product/service gaps are addressable with the available resources, and what are the associated risks?
- **Innovation Milestones** ➔ How do we manage priorities, goals, and timing, and monitor risks as they change?



Product and Service Assessment

There is an ebb and flow to any insurance products and services in terms of their relevance, competitiveness, and financial performance. Product and Portfolio Management must manage this life cycle by adapting and innovating the product and service proposition where possible. The first key step in this process is to understand what market and regulatory factors are driving the underwriting cycle.

The spectrum and variables are broad and cross-functional. For example, Claims may report a rise in average incurred commercial property losses and incurred but not reported (IBNR) loss estimates. Actuarial may ascertain that interest rates are likely to rise, leading to a re-assessment of property pricing. Loss Control may propose an Internet-based loss control reporting service to re-design and tailor property underwriting coverage pricing in parallel with risk management service offerings for specific territorial locations. When reinsurance parameters are applied to the product, the insurance company is in a position to assume the customers' risks without unacceptable surplus strain. What are the various scenario implications? Identifying new ways of making life less risky for the customer with more flexible offerings is balanced against process costs, risk implications, and resource infrastructure considerations.

GOALS	METRICS	DIMENSIONS
New Product & Service Opportunity ($) Product & Service Risk Score (#)	Product & Service Achievability New Products/Services at Market ($/%) New Product/Service Suggestions (#) Competitive Score (#) Est. Development Cost $ Income Gain Estimate ($) Incurred Claims Estimate ($) Mkt. Transaction Volume (#) Mkt. Transaction Volume share (%) Project Duration – Plan (Business Days) Project Resource Days – Plan Project Cost – Plan $ Tested Products (#)	Insurance Charter Location Country State / Province Insurance Risk Locations Territories Geo Codes Product - Coverage Product Line Coverage Regulatory Standards Regulation Type Regulation Standard Insurance Hazards Hazards Insurance Market Segment Market Segment Micro-Segment

FUNCTION	DECISION ROLES	PRIMARY WORK	CONTRIBUTORY	STATUS
Underwriting				
	Executives	•		
	Managers	•		
	Analysts	•		
	Professionals	•		
Finance				
	Executives			•
	Analysts		•	
Sales				
	Executives			•
	Analysts		•	
Marketing				
	Executives			•
	Analysts		•	
Customer Service				
	Executives			•
	Analysts		•	
Claims				
	Executives			•
	Analysts		•	
Operations/Production				
	Executives			•
	Analysts		•	
Actuarial				
	Executives			•
	Analysts		•	
Compliance				
	Analysts		•	
Regulatory/Legal				
	Executives			•

The product and service assessment serves as a gap analysis to prioritize the various improvement options and the associated financial scenarios. Initiatives to adapt the current offering or more fundamental innovations represent a pipeline of future revenue opportunities to sustain the insurance company's competitiveness and net premium growth. New initiatives also have an impact on Marketing, as these bring "new news" to your customers. New news fuels the marketing machinery, a significant way to excite and capture attention and customer mindshare. This decision area will not only identify gaps, but determine what effect these changing factors have on premiums, deductibles, cash flow balances, etc. The more up-to-date and dynamic the monitoring of these changing factors, the quicker the ability to identify new opportunities and capitalize on these for the benefit of the insurance company.

Product and Strategic Innovation

This decision area takes potential opportunities identified by the product and service assessment and examines the practicalities in more depth. It answers questions about the costs, resources, and benefits of implementing new initiatives and innovations. It also offers more clarity in terms of benefits, strategic fit, how achievable these initiatives are given available resources, and the risk of failure. Innovation runs the gamut from incremental improvements to a significant strategic shift. For example, a strategic decision to extend the distribution network with the associated up-front investment implications, against a backdrop of competitors' cutting their distribution networks, will require a detailed understanding of the rationale in terms of customer gains. New loss control products will also be considered in cooperation with Loss Control, Claims, and Underwriting to determine the risk/reward profile and relative fit with loss development forecasts.

Whatever the innovation, you must measure the time to market, implementation difficulty, external factors, technical improvements, and financial scenarios, e.g., the value-added return on net capital. These metrics also help you prioritize threats and opportunities. For example, by classifying the initiatives into short-term and long-term priorities, or by measuring the difficulty of implementation, you limit the attention on impractical blue-sky projects that distract attention from what's needed in the short term. Future scenario valuations with estimates of the upper and lower limits on premium and net income growth will help define the relative priorities.

As a decision area, Product and Strategic Innovation recommends which opportunities are right for the business by aligning with other departments, particularly Marketing, Underwriting, and Compliance.

GOALS	METRICS	DIMENSIONS
New Product & Service Developments (#) New Product & Service Income ($/%) New Product & Service Cost ($/%)	Product - Service Achievability Score Implementation Cost ($) New Product - Service Income Potential ($) Potential / Actual Revenue ($/%) Implementation Time (#) Product & Service Risk Score (#)	Fiscal Year Quarter Month Insurance Market Segment Market Segment Micro-Segment Products - Services Product Type Product Line Coverage - Service Sales Channel Partners Sales Channel Type Sales Partner Sales Organization Sales Region Sales Territory Organization Code

FUNCTION	DECISION ROLES	PRIMARY WORK	CONTRIBUTORY	STATUS
Marketing	Executives	•		
	Managers	•		
	Analysts	•		
	Professionals	•		
Underwriting	Executives	•		
	Managers	•		
	Analysts	•		
	Professionals	•		
Finance	Executives			•
	Analysts		•	
Sales	Executives			•
	Analysts		•	
Customer Service	Executives			•
	Analysts		•	
Operations/Production	Executives			•
	Analysts		•	
Actuarial	Executives			•
	Managers		•	
	Analysts		•	
	Professionals		•	
Claims	Executives			•
	Analysts		•	
Loss Control	Executives			•
	Analysts		•	

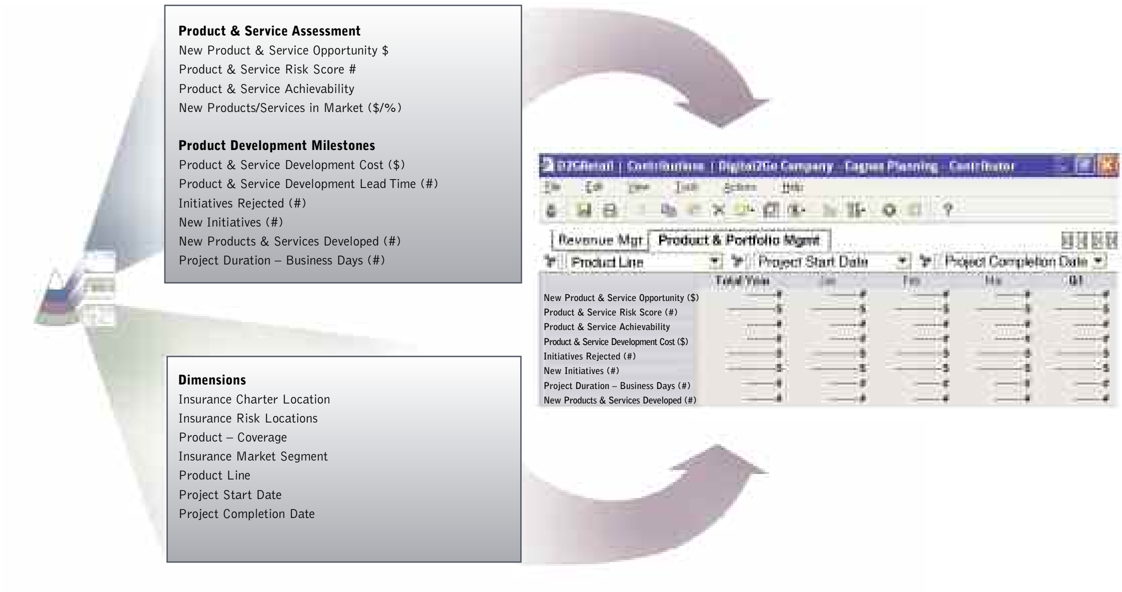
Innovation Milestones

This decision area is used to manage the innovation process. It establishes milestones, manages and adjusts priorities and timing, and monitors risks as they change. Insurance companies may take a cue from the manufacturing sector, where many companies use Stage-Gate® or phase-gate processes involving five stages for product development: preliminary assessment, definition (market), development (product/cost), validation, and commercialization. Typically, a very low percentage of preliminary ideas pass through the final gate. Less formal processes still require that you answer questions such as: *What new product development ideas do we have? What is the scale of the identified opportunity? Do we have the skills in-house? What are the risks? Is the opportunity aligned with our strategic priorities? What are the likely financial rewards?*

In insurance, measuring performance milestones is critical. Given a number of preliminary initiatives, how many milestones are passed before rejection or commercialization? Logging and evaluating the reasons for success or failure through these milestones will help you improve your innovation process. Regular planning and gap analysis reviews anchor the innovation process with business priorities. Without this focus and monitoring, the process may be sidelined by day-to-day concerns. It is critically important to ensure the success of all phases, from design to implementation and full commercialization. Information that focuses and fine tunes each stage and provides incentives is imperative to ensuring successful innovations.

GOALS	METRICS	DIMENSIONS	
Product & Service Development Cost ($) Product & Service Development Lead Time (#) Project Completion by Milestone (#/%)	Initiatives Rejected (#) New Initiatives (#) New Product & Service Launch Failures (#) New Products & Services Developed (#) Modified Products & Services (#) Project Duration – Business Days (#) Project Duration – Variance (%) Rejection Causes (#) Market Tests (#)	Reporting Period Year Quarter Month Forecast Scenario (Plan/Actual/Forecast) Scenario Product Development Milestone Product Line Product Line Project Project/Program Type Project	Project Start Date Year Quarter Month Project Finish Date Project Management Project Team Project Manager Project Member Project Completion Date Year Quarter Month Project Finish Date

FUNCTION	DECISION ROLES	PRIMARY WORK	CONTRIBUTORY	STATUS
Actuarial				
	Executives	•		
	Managers	•		
	Analysts	•		
	Professionals	•		
Underwriting				
	Executives			•
	Analysts		•	
Claims				
	Executives			•
	Analysts		•	
Loss Control				
	Executives			•
	Analysts		•	
Customer Service				
	Executives			•
	Analysts		•	
Finance				
	Analysts		•	
Sales				
	Executives			•
	Analysts		•	
Marketing				
	Executives			•
	Analysts		•	
IT/Systems				
	Executives			•
	Analysts		•	
Operations/Production				
	Executives			•
	Analysts		•	
General Management				
	Executives			•



The Product and Strategic Innovation and Product Management Milestones decision areas illustrate how the Product Development function can monitor its performance, allocate resources, and set plans for future financial targets.