

The Internet of Things: Transforming the Insurance Industry

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The next generation of internet and wireless connected technology is commonly called the “Internet of Things” or M2M (machine to machine). Globally there are about 5.4 billion mobile phones in service. In the next decade an estimated 50 billion devices will be connected to the wireless world. While some of these will be phones and tablets, overwhelmingly they will be devices that monitor, control, inform and enable machines and people to perform tasks in new ways and with greater productivity.

What is causing this connected device explosion? Wireless devices, wireless transmission, computing power and the underlying chipsets are all becoming significantly cheaper (Moore’s Law) enabling “things” to interconnect in previously unavailable ways. Machines now communicate with and message each other; applications send updates to people; people query or receive text messages for information. These new interconnections will change the world more fundamentally than the way mobile phones changed the world. The possibilities are truly endless, and as costs continue to decline companies that deploy solutions early will have a leg up on their competitors. Innovative companies will gather more data, gain increased market knowledge and be able to further accelerate

their product and service innovation. And these early entrants will likely attract more customers thereby accelerating their growth.

The personal Insurance industry is beginning to adopt M2M technology in the form of Usage Based Insurance (UBI). A monitoring device is installed professionally or by the customer and connected to the vehicle’s OnBoard Diagnostic (OBD-II) port. Then information is collected that can include: braking, acceleration, time of day of vehicle operation,

location (if GPS is also installed), miles driven and other driving data. Over time, a driver’s signature can be revealed insofar as each person drives somewhat uniquely and more or less consistently.

Many of the leading personal property and casualty carriers have rolled out programs (see table below) and many other carriers are considering and evaluating them. UBI is intended as a replacement and/or enhancement to credit score, accident history, driving record and self-reported miles driven.

| Usage Based Insurance Programs Major US based property and casualty insurers | | | | |
|---|-------------------------------|-----------------|---------------------|--|
| Company | UBI Program Name | Savings Offered | Cost | Other Features |
| Progressive | SnapShot | Up to 30% | None | Guaranteed not to raise rates Driving info available on website for customers |
| AllState | Drive Wise | Up to 30% | None | Guaranteed not to raise rates Driving info available on website |
| State Farm | In-Drive | Up to 50% | \$10 activation fee | 10% up front discount |
| Liberty Mutual | On-board Advisor (Commercial) | Up to 40% | None | Fuel efficiency, Safety Score Driving info available on website |

Carriers are banking on three outcomes from their initiatives with UBI. First, that their risk selection process will improve and that the lower rates offered will be more than offset by lower claims. Today most UBI programs are optional, which is to say that carriers promise to either maintain current rates or offer a discount. Second, the data that companies gather on the pool of drivers who test or adopt UBI will enable them to better understand operator risk, thereby allowing them to broadly improve underwriting. Marconi Pacific refers to this as improving 'addressable risk'. And third, that UBI provides the larger carriers with a competitive marketing and rating advantage over smaller carriers which may not have the resources to roll-out UBI programs. If UBI is successful, it will create a sea-change in the industry – underwriters with UBI tools will underwrite less risk, shifting “bad-risk” to their less sophisticated competitors.

But there are some opportunities that we believe insurance carriers may be missing.

- Carriers have an opportunity to add value for drivers/insureds through UBI, just as they bring value to themselves. The auto insurance market in the US has become heavily dependent on price competition. Most carriers tout their lower rates and UBI appears to have fallen into the same price trap. Also many customers who are not re-rated lower as a result of UBI will find no apparent benefit in the program. As other insureds become aware that few of their peers are receiving discounts they will be less inclined to sign up for UBI programs – denying the carriers the valuable information they are seeking.

Marconi Pacific has assisted many clients in developing co-creation projects. Co-creation is the concept that companies can build platforms to engage their customers in meaningful value-added exchanges of information and products/services whereby customers and the company together create a virtuous cycle of mutually beneficial added value. In the UBI space the platform can provide drivers with a dashboard to help them better understand their driving behavior and to better understand how they might waste fuel through aggressive acceleration, hard braking or speeding. This approach can provide value and mitigate the magnitude of rate reduction. The challenge is to determine what insureds want and then cost effectively deliver the value.

- M2M has just begun to scratch the surface of monitoring. Witness UBI which is in its infancy. The next step in insurance is to expand the monitoring of businesses, homes and lots of other assets especially in the commercial market but increasingly in the residential world as well. M2M could enable underwriters to remind customers to lock their doors or windows. Both insured and insurer could be alerted if a boiler is performing improperly or if the basement is flooding. If a gas fireplace or stove top remains ignited for too long a period an alert could be sent. The list goes on and on. The critical first question for underwriters is to figure out what their customers' value. Then the insurance company can determine how to deliver that value while capturing new information for itself and building customer loyalty.

Connecting the home and collecting data may also provide a horizontal market opportunity for insurance companies, enabling them to provide information to energy companies, home security companies, and others. Many of the potential use-cases for home connectivity and monitoring require customers to pay for the services (thereby slowing adoption) for no cost. Significant innovation needs to occur before a UBI home product offers value to both insureds and carriers.

Marconi Pacific is contributing to a telecommunications industry group that is studying M2M and its many application areas and many industry standards issues. The opportunities for M2M extend well beyond insurance to health care, energy management, time management and many other areas. Insurance carriers which explore M2M monitoring of homes, businesses and other assets can get an early start in adding more value to their companies and to their customers, thereby accelerating growth and profitability.

UBI for autos is here to stay. Insurance carriers can expand their success with UBI by adding value to insureds beyond price/rate cutting. And insurance carriers can expand UBI concepts into the home, businesses and other assets where M2M technology can be cost-effectively deployed to reduce risk and provide more information to insureds about their assets and usage. This will reduce costs for insureds and claims for carriers. The Internet of Things provides a lot of new opportunities for insurance carriers to gain competitive advantage.

About Marconi Pacific, LLC

Marconi Pacific, LLC is a strategy and venture consulting firm providing business advisory services in the telecommunications, Internet and financial services industries. We build value for our clients by providing strategic analysis and practical solutions to complex business issues. In addition, we pursue selected investments in emerging companies, and we identify and pursue our own new venture opportunities.

Strategy Consulting: Marconi Pacific provides strategic advisory services to senior management to help build long-term shareholder value. Our clients select us over other consulting firms for our incisive analysis, industry knowledge and creative, yet pragmatic, recommendations. We work with clients to define a differentiated value proposition that can they can offer their customers. We then work to refine the core operational elements of the business to deliver this value. This requires understanding the market in detail; segmenting the customer base; determining demand; making decisions on positioning, pricing and channels of distribution; and then defining the operational processes and structures needed to deliver the value. We take a pragmatic view of our advisory work, recognizing that creating value requires strategies and plans with a singular focus on financial results rather than elegant studies and academic observations.

Venturing: The very applied nature of our management consulting work makes us very much "in the market" in which our clients operate. As a result, Marconi Pacific, unlike many professional consulting firms, is very involved in creating new ventures, both with our own capital and in partnership with our clients. We also maintain relationships with venture capital firms, private equity firms and investment banks with which we can work to create value.

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