



# **SPECIMEN COURSEWORK ASSIGNMENT AND ANSWER**

## **990 - (Insurance Corporate Management)**

The following is a specimen coursework assignment question and answer. It provides a guide as to the style and format of coursework questions that will be asked and indicates the depth and breadth of answers sought by markers. The answer given is not intended to be the definitive answer; well reasoned alternative views will also gain good marks.

Before commencing work on an actual coursework assignment, you need to fully familiarise yourself with the following documents:

- *Coursework assessment guidelines and instructions;*
- *How to approach coursework assignments;*
- *Explaining your results notification.*

Coursework assignments involve the application of knowledge to work-related questions. They require you to explore issues in the workplace relevant to the unit for which you have enrolled.

## **Coursework submission rules and important notes**

Before commencing on, or submitting, your coursework assignment it is essential that you fully familiarise yourself with the content of *Coursework assessment guidelines and instructions*. This includes the following information:

- The maximum word limit for coursework assignments is 3,200 words.
- Arial font and size 11 to be used in your answers.
- Important rules relating to referencing all sources including the study text, regulations and citing statute and case law.
- Penalties for contravention of the rules relating to plagiarism and collaboration.
- Deadline for submission of coursework answers.
- There are 80 marks available per assignment. You must obtain a minimum of 40 marks (50%) per assignment to achieve a pass.
- The coursework marking criteria applied by markers to submitted answers.
- Do not include your name or CII PIN anywhere in your answers.

## **Top tips for answering coursework assignments**

- Read the assignments carefully and ensure you answer all parts of the assignments.
- Ensure that each answer includes a relevant context, regardless of the country or countries to which it refers.
- You must include a context in each answer. You may use the same context for each of the three answers.
- For assignments relating to regulation and law, knowledge of the UK regulatory framework is appropriate. However, marks can be awarded for non-UK examples if they are more relevant to your context.
- There is no minimum word requirement, but an answer with fewer than 2,800 words may be insufficiently comprehensive.

## Assignment

Provide a brief context for an insurance organisation or a division of an insurance organisation with which you are familiar. For **this** organisation or division of an organisation:

- Define the terms 'new entrants' and 'substitutes' in its competitive environment.
- Explain the potential threat of new entrants to the market and the threat of substitutions.
- Analyse the threats of new entrants and substitutes entering the market.
- Make recommendations, based on your analysis, to respond to the threats identified to maintain its competitive position.

**Note:** You are recommended to discuss your own organisation, or one that is familiar to you. Your answer is confidential to the CII and will not be shared. For this exemplar answer, which is widely publicised, a fictitious company has been chosen so as not to highlight any particular company.

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**Start typing your answer here:**

## Context

For the last five years I have worked for a regional, independently owned insurance broker called CBA Ltd (CBA). With a head office in London, CBA has six other offices, each specialising in different classes of business and employing 230 people in total.

For the purposes of this assignment, I will base my answer on CBA's Private Client and Personal Lines (PC&PL) Division which is based in Birmingham. CBA is a recognised market leader in this class of business and has a reputation for delivering high quality service for its clients whilst seen by the insurers it places business with, as reliable and trustworthy.

CBA places its private client and personal lines (PC&PL) business in the open market, at Lloyd's and through a number of delegated authority schemes. New business is generated through a combination of affinity relationships, cross selling, targeted marketing and sponsorship, an energetic new business team generating organic growth, as well as a small telesales team and targeted acquisitions of smaller insurance broking businesses. CBA's PC&PL Division also have a small wholesale team who place business with CBA's insurers on behalf of a limited number of producing brokers.

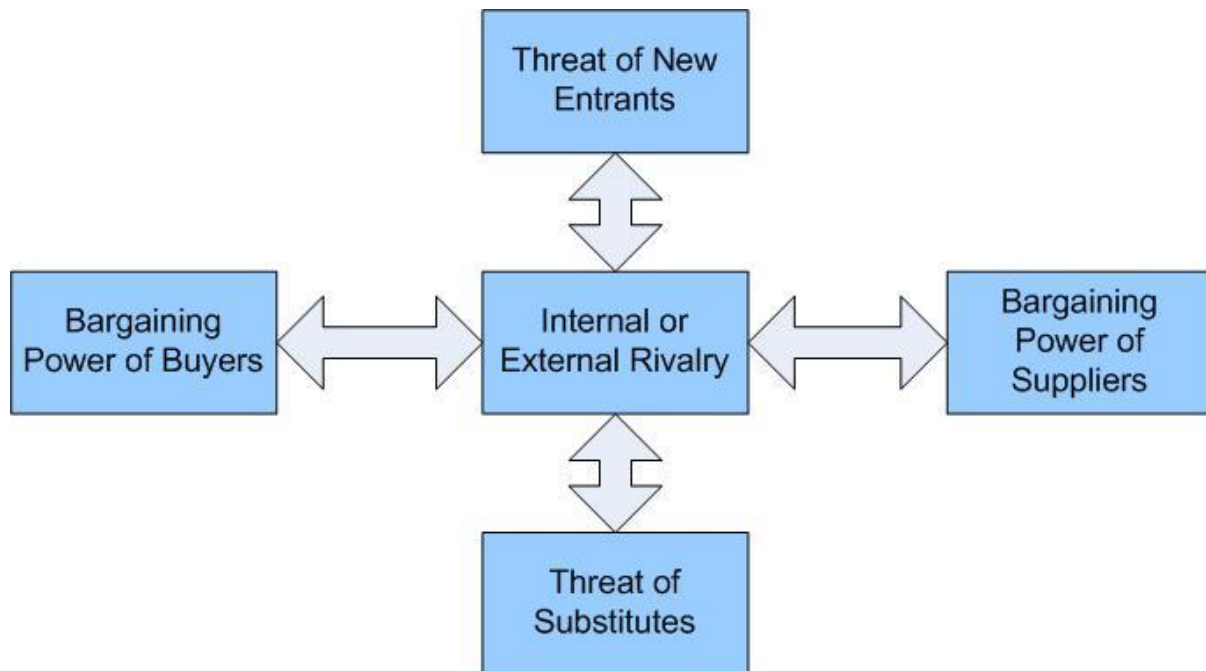
## The competitive environment

CBA's PC&PL Division have a range of clients with differing personal lines needs and offer them products ranging from high net worth (HNW) to standard household and motor products. The service model for these clients is segmented and ranges from face-to-face contact (for HNW clients) and an outsourced call centre (for clients with premiums below £500). The personal lines market is highly competitive, especially for lower premium household and motor products. CBA's competition comes from a number of areas ranging from bespoke HNW brokers to direct insurers and a whole range of other competitors in between. CBA's success comes from its ability to offer clients the right products at competitive prices and by ensuring the most appropriate and cost effective service offering is applied.

As with any market, but particularly a competitive one, the challenge for management at CBA, is to understand the market, identifying potential new threats and opportunities in order to ensure the company can defend itself against negative forces and take advantage of the opportunities. By doing so it will be able to achieve or maintain competitive advantage and 'get or stay ahead of the competition'. For CBA, this is a complex issue as the market is competitive, complex and fragmented with differing forces acting on the various customer groups and the products offered. CBA is, therefore, aware that it needs to spend time analysing the current and future competition and understand all its markets better. It does this through strategic planning and competitor analysis.

## Definition of new entrants

Michael Porter of Harvard Business School (1979) developed a strategic planning tool to display the state of competition in any specific market and in particular the five forces which influence any particular company within a given market. A diagram of Porter's Five Forces is shown below:



When using the tool to conduct strategic planning, management identify specific issues under each heading and analyse them in terms of their threat to the organisation. The forces include the 'Threat of New Entrants' as well as 'Substitutes'. Within CBA's competitive environment new entrants can be defined as any new direct organisation who seeks to compete for the insurance business of CBA's existing or potential new clients, or those of CBA's existing competitors within the PC&PL market. This may include an existing competitor who decides to offer a new product in a different segment, a completely new start up business or an existing company (not previously in direct competition with CBA), offering a more diversified product range that now presents direct competition.

An example of this is an insurance broker who specialised in commercial business only. When the wealthy owners of the businesses asked this organisation to arrange for the placement of the insurances of their private assets, this broker arranged for CBA to place the business for them on a wholesale basis. However, recently, this company decided to widen their product portfolio and offer personal lines products themselves and in doing so, it became a new entrant to the PC&PL market.

### Definition of substitutes

According to Nalebuff, B.J. and Brandenburger, A.M. in an article entitled *Co-opetition, Doubleday Business* (1996), 'The critical aspect of a substitute is that it is paid for with the same money that would be used for the item being replaced. Substitutes hence compete for 'share of wallet'.'

Substitutes may be partial substitutes, for example consolidators who offer the same product, but in a completely new way, or full substitutes, where existing products are rendered redundant. A simple analogy is the substitution of butter for margarine. By definition, all beverages can be seen as substitutes as they are all drinks. Another example is the evolution of technology. Providers of mobile phones and computers operate in a highly competitive and fast paced environment where there is a high threat of substitution for newly developed products which render existing products technologically obsolete, as well as competition between similar products.

In CBA's PC&PL business, competitors as well as new entrants may bring a substitute to market at any stage and the challenge is to be able to identify it before it is too late.

### **An explanation of the threat of new entrants and substitutes to CBA's PC&PL markets**

New entrants and substitutes both pose a similar threat to CBA's market. Their primary threat is the fact that competition for market share increases. And CBA are likely to lose clients. In a perfect market, this means that in order to maintain market its share, CBA must react in some way. The main options are to enhance customer service or reduce price.

The personal lines market is primarily driven by price for its standard household products. HNW clients tend to focus more on service, but these clients are also demanding and look for value.

New entrants can have an impact on the insurance market cycle. As competition for market share increases with new entrants, so rates are cut and that has a knock on effect on commissions. Business becomes less sticky at the low end, as clients search for the cheapest deals. At the other end of the market, the costs of delivering a high-quality service mean our profit margins are squeezed. For CBA, this means we need to be aware of new entrants and understand our business strategy well, ensuring it is regularly reviewed in line with market dynamics.

The threat posed by substitutes, is potentially greater although as we will see below, substitutes are considered less common in CBA's market. This is because there is less CBA can do to compete directly with substitutes and may lose market share unless CBA can be innovative and widen its product base to include the substitute offering. This is not always possible as we will see below.

## Analysis of the threat of new entrants and substitutes to CBA's PC&PL market

### New entrants

CBA's PC&PL market is highly competitive. Because of this, the expectation might be that the threat from new entrants is low, because any new entrant is unlikely to gain a significant market share quickly. However, the personal lines market is driven by price, especially when it comes to motor insurance, (possibly because motor insurance is compulsory in the UK), and standard household products. The insurers are as much to blame as anyone else due to industry advertising where unrealistic expectations are generated between cost cutting and service. (Howard Posner, HBOS).

Because of this focus on price, a new entrant with a highly-developed IT system may be able to create cost benefits and attract customers away from CBA. Unlike the banking system, where complexities of moving from one account to another create customer loyalty (also known as 'sticky business'), it is easy for consumers to move from one insurer and one broker to another based entirely on the price of their renewal. The high level of regulation focusing on giving the customer the freedom to choose means that this situation is likely to continue.

CBA also face completion from insurers entering the direct market for the first time to achieve increased profitability. Examples include Direct Line. Insurers pay away commission to brokers in return for cost savings generated by not having to service the clients, allowing them to concentrate on underwriting and claims management (although even this has been delegated to CBA through our delegated underwriting and claims authorities, allowing insurers to act as capacity providers with a potentially higher margin of profitability achieved through reduction in staff cost). The development of more sophisticated web based business means that insurers can offer products directly to the insured without the need for a broker. A new entrant, whether acting as an intermediary or an insurer can start from scratch with IT systems tailor-made for e-business. New entrants can do this quickly, whereas CBA and its competitors take longer to design and purchase new systems, which are expensive and which have to be integrated into the existing legacy systems.

The key issues in relation to new entrants into CBA's market are as follows:

- Barriers to entry: the regulator requires insurers and brokers to be approved before they can conduct business in the UK. This can act as a barrier. In addition, there are stringent capitalisation requirements for insurers. However, the regulator aims to protect the rights of individual customers and this means that the regulator is unlikely to accept the dominance of a few large providers (an oligopolistic market) and prefers a highly competitive market made up of many companies (monopolistic competition).

- The market attractiveness, including potential profit or other benefits. The UK personal lines market is huge. According to Swiss Re, Sigma No 3/2014, the UK insurance industry is the biggest in Europe and third largest in the world. This is an attractive market.
- New entrants can have better economies of scale, newer technology, lower cost structures, existing brand reputation or other differentiating advantages.
- There are no switching costs for customers to move to new entrants.
- This is an established and mature market and existing competitors, as well as CBA, could be complacent from time to time, leading to a lack of investment by current companies in the market.

By way of summary, the personal lines market is diverse and highly competitive. The key driver for clients is price, but this is less important for HNW clients who demand a high level of service and are often willing to pay for it, although they still demand value.

According to David Martin, Chief Executive Officer (CEO) of Willis Towers Watson:

“The insurance industry is obsessed with price. Brokers have to learn that if they give the lowest price the customer will get the lowest service.”

When John Sims was CEO of Chubb, a HNW insurer that CBA uses, he made the comment that:

“As an insurance group with a specialist product portfolio which sells on service, not price, we find that the competition tends to come from new entrants that arrive and claim they are experts in the sector and will seek to underwrite business at a 30% discount.”

There are a number of recommendations that naturally follow on from this analysis and these will be discussed in the next section.

## Substitutes

In CBA's PC&PL market, there is a lower threat of substitutes, although in the wider insurance market alternative risk transfer (ART), captives and self-Insurance are examples of full substitutes and are seen as a risk. These have less impact on the personal lines market due to the relatively low premium rates involved.

Substitutes to CBA's market include consolidators. This is a classic partial substitute where the product is still similar, but it is offered in a new way. Consolidators are organisations who act merely as host web based marketing companies for other insurers to offer their products. It could even be argued that such organisations are substitutes, because their offering is completely different. With highly sophisticated IT systems allowing customers to



search for products dependant on their individual preference and risk profile, consolidators generally sell on price and examples include [www.gocompair.com](http://www.gocompair.com) and [www.searchthemarket.com](http://www.searchthemarket.com).

Substitutes are highly unlikely for CBA's motor insurance products as motor is a compulsory insurance required by law. However, in an effort to gain market share, some HNW insurers have radically changed their insurance product to include a range of benefits that would appeal to clients with higher value cars (such as so called 'all-risks' products that include added extensions, such as same value replacement vehicles and agreed value cover).

These products, whilst not strictly substitutes are aimed at differentiating their products among discerning customers for whom service is often more important than price. As brokers, CBA is well placed to ensure its product range matches the requirements of its customer base and any complacency in terms of its market share should be avoided to ensure it maintains market share. As intermediaries we are able to recommend products from a wide range of sources. Another example is the emergence a few years ago, of the composite HNW policy where homes, contents, liabilities, motor, travel, overseas homes and even marine risks, as well as a wide range of other add-on products were introduced under one policy. Whilst not necessarily the cheapest way to insure household risks, these products offered clients simplicity and wider cover.

The key issues in relation to substitutes in CBA's markets are as follows:

- When buyers are open to alternative solutions, they may be attracted to alternatives. This is why CBA should be aware of all market developments, especially in terms of technology.
- Where a substitute offers significant price benefits, customers will be willing to change.
- Where substitutes are seen to offer better features, such as cover 'add-ons', they may be willing to move.
- Just as for new entrants, where switching costs are low for customers, customers may move.
- If customers are dissatisfied with current offerings, they are more likely to consider substitutes, especially if there are already substitutes within the market.

Insurance is such an intangible commodity and because this market is so competitive, clients are likely to move if they perceive any substitute as being lower in price.

The threat to CBA's market of new entrants is classed as high for standard business. For HNW business the threat is slightly lower, depending where the new entry or substitute product is being targeted.

Again there are several recommendations and actions that CBA could take to respond to the threat of these substitutes, which come out of this analysis. These will now be considered below.

## **Recommendations to respond to the threat of new entrants and substitutes in CBA's PC&PL market**

There are a range of actions CBA could take to respond to the threat of new entrants and substitutes in the PC&PL market. Due to the differences between the private client and standard household account these recommendations will be discussed separately.

### Private client business

CBA's private client (PC) business consists of higher value risks characterised by wide cover, from composite, all risks policies at relatively high premiums. These clients are serviced by nominated account managers offering face-to-face visits. There are a range of recommendations CBA could follow up to ensure it maintains its market share whilst the market becomes more competitive due to new entrants and/or substitutions. CBA PC Division should:

- a) Regularly review and adjust its strategic and business plan. The strategic plan of CBA is to create competitive advantage. Considerations include, the profitability of segmentation of customers, the products and services offered, technology and competitive analysis.
- b) Not become complacent. Just because we currently have a good market share does not mean this will continue. Continual analysis of new products and services available should be carried out.
- c) Review of insurer panel. The price, cover and service of the products offered by our existing insurer panel should be regularly reviewed and new insurers should be considered on their merits to ensure our panel remains comprehensive. It is important to note that we must be able to provide enough premium volume for all our markets to ensure we maintain our good reputation and do not dilute our offering just to 'cover every base'. A wide insurer panel is not necessarily an indication of our competitive position, but we must be able to offer our clients innovative, competitive and appropriate insurance products.
- d) Consider investing in new technology to ensure new entrants which may have more advanced IT systems do not achieve a competitive edge.
- e) Regularly seek customer feedback to ensure our service and products remain relevant to our customer base.
- f) Consider a marketing campaign which could be employed in the event that a new entrant or substitute offers a lower value alternative. This client segment demands a high level of service and value. It may be that a new entrant may try to steal market share by offering products at a lower price and it may need a sustained and consistent marketing

message to be set out that cheap is not necessarily best. This may also be achieved by high quality marketing material and documentation, so that anything tangible sends the right marketing messages and supports the quality of the brand.

## Standard Household Business

CBA's standard household business is offered through a combination of delegated authority and open market placement and it is either serviced in house, or, where premiums are below £500, through a third-party service provider. This allows for a highly flexible and appropriate service model, a wide range of products and cost efficiencies. However, the business is not sticky and clients have a high turn-over rate. Because of this, this segment may be at greater risk from new entrants and substitutes. In order to respond to the threat of new entrants and substitutes, CBA's standard household division should:

- a) Regularly review and adjust its strategic and business plan. The strategic plan of CBA is to create competitive advantage. Considerations include the profitability of segmentation of customers, the products and services offered, technology and competitive analysis.
- b) Continual analysis of new products and services available should be carried out. In particular, for this segment, the use of innovative IT is essential as customers are particularly price sensitive and may more their business if a cheaper alternative is available.
- c) Review of insurer panel. The price, cover and service of the products offered by our existing insurer panel should be regularly reviewed and new insurers should be considered on their merits to ensure our panel remains comprehensive.
- d) Consider investing in new technology to ensure new entrants which may have more advanced IT systems do not achieve a competitive edge. Again, this is essential for lower premium policies where clients may look to buy on-line, either directly or with consolidators. It may not be cost effective to continually seek to compete with new entrants who have the most modern IT as any updates to our system will need to be integrated to our legacy systems. However, we do have a third-party service provider who will be able to offer the latest technology due to their economies of scale. Constantly reviewing the business which is serviced by this outsource arrangement should feed back into the strategy review and business planning process identified in a) above.
- e) Regularly seek customer feedback. Agility and flexibility are essential in this price sensitive segment.

One final consideration for CBA and this may be appropriate for both the PC and standard household, is to consider buying new entrants before they achieve a hold in the market. This is a strategy CBA has adopted before, but careful due diligence is essential before considering merger and acquisition activity in a competitive market as this is an expensive measure to take.

## Conclusions

CBA's PC&PL Division operates in a competitive market. Because personal lines business is price sensitive, it does mean CBA must be alert to new entrants. Substitutions are less of a threat in this market, but complacency is our enemy if we wish to retain and enhance our market share.

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