# Nordic Insurance Company performance
## *The customer view on quality and value*

by Jan Eklöf

*This article aims at presenting some results from the annual Pan-Nordic benchmark study on customer satisfaction and loyalty in the insurance sector. Focus is on results from the study in the fall 2007 and comparisons with the longer term trends. The study is based on the EPSI (European Performance Satisfaction Index) initiative and overall approach developed within this framework.*

*The indicators given by the actual customers offer insight into the functioning of the insurance industry in the Nordic countries, as well as how individual companies perform in relation to their respective customers. From the empirical results it is found that customers are relatively satisfied in the industry (compared to the economy as a whole). It is further seen that the image of most insurance companies is low, as well as the value for money determinants. Customer loyalty with the current insurance company varies quite a lot between the Nordic countries, as well as between individual companies within the same country. Overall, the satisfaction index is a good forward looking indicator of actual retention (loyalty to the current insurance company).*

*From the analysis it is possible to point out the main drivers for increasing satisfaction and loyalty. These vary significantly from one company to another, illustrating that the customer base characteristics also vary between companies, as well as do the perception of the deliverables for individual insurance companies.*

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## Introduction

Any organization has to listen to its external customers and other stakeholders. A number of studies have shown that the long-term success of a corporation is closely related to its ability to adapt to customer needs and changing preferences. Customer Satisfaction is a crucial goal for most organizations, and it has proven effective to forecast the long-term financial performance of any company (Ittner, Larker, 1998).

In the present study we illustrate and analyze how systematic measurement of customer satisfaction, loyalty and its driving forces can be used to highlight similarities and differences in the Nordic insurance markets. This in turn gives indication about the functioning of the various markets and specific

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relationship between suppliers and customers. It is further shown how such information may support improvement work and company specific priority setting and evaluation of strategies.

The next section gives a basic foundation for the used methodology, while some Pan Nordic benchmarks are given thereafter. A few results on causal relationships and usage of the model approach for analysis are given in the latter part of the article. It is ended with some proposals and ideas for corporate analysis and references to further reading and related studies.

## Analysis of Customer Satisfaction in a Causal Model

What is classified as a good, acceptable or appropriate level of satisfaction, retention or customer loyalty? This depends on how it is measured and presented, but even more so, on the expectations and targets set for the activity. The concept of benchmarking is increasing in use for relating one actor's performance to another's in a systematic way and for learning how to strive for improvement. Benchmarking the framework for comparison has to be duly calibrated and studied sets of data have to be "harmonized".

The following characteristics of a system for EPSI at national level are adhered to:

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**Constitutive Characteristics of** EPSI at national level[1]

(1) a measurement of satisfaction as well as key success factors
(2) of companies and institutions
(3) comprising several industries/sectors of
(4) a nation or a distinct economic area
(5) via periodical analyses
(6) by a neutral institution.

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For measuring Customer Satisfaction in a wider context a structural equation model has been developed based on components considered crucial for causal analysis (cf. EPSI Rating 2007). Thus, the model contains the components:

• Image
• Customer Expectations
• Customer Perceived Product Quality
• Customer Perceived Service Quality
• Customer Perceived Value
• Customer Satisfaction
• Customer Loyalty

The components are viewed as latent variables determined by a set of manifest constructs for each component. Each component is measured, the level of each component estimated, the relevant connections between the components established and the magnitude of the connections estimated. The objective is to provide results that are relevant, reliable, valid and have predictive financial capability. The structure of the model is illustrated in Figure 1.

In order to estimate the model, to calculate the index values and the magnitude of the impacts, data must exist that is representative for the customers of the company/institution in the country. The survey design considered consists of:

• The design of a questionnaire for measuring the latent variables via the manifests. The questionnaire contains the manifest variables and some background variables.
• The selection of a representative sample of customers.
• The field operations for collecting the data from the sample using the questionnaire. This also includes the consistency checking and the creation of data files for analysis.
• The analysis of the data and the preparation of reports.

A set of master questionnaires has been developed and their performance tested. The questions related in blocks to the latent variables. Each latent variable was covered by at least 3 questions concerning different aspects of the

*Figure 1: The EPSI Rating Structural model*
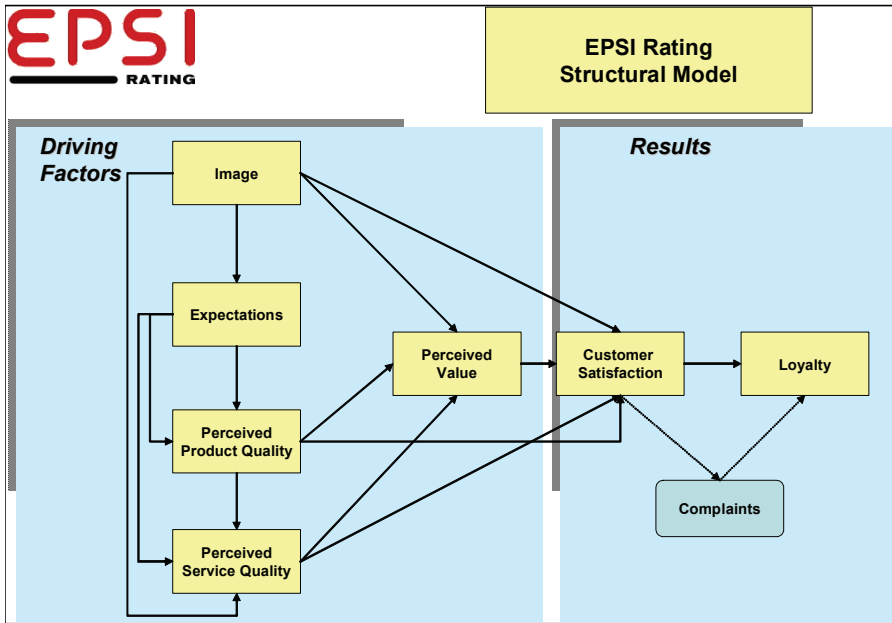
latent variable. The respondents were requested to respond on a scale from 1 to 10 where 1 means the customer was not at all satisfied with the specific aspect under study while a 10 means the customer is completely satisfied. In all around 30 to 35 questions must be answered to fulfil the requirements of the model. Three specific questions are related to the Customer Satisfaction variable. They cover:

• The overall satisfaction with the product
• Satisfaction compared to expectations
• Comparison to an ideal product

For the Loyalty latent the questions cover:

• Intention to buy again
• Intention to recommend the product
• Price sensitivity assessment (in a few countries)

On the driver side some 15 –25 questions are used depending on the characteristics of the industries under study, but the wording of these questions is to a great extent standardized.

The model is estimated using Partial Least Squares (PLS) techniques. The 1–10 scale is, for ease of interpretation, transformed into a 0 –100 scale. The values of the impacts were estimated together with error margins. A separate model is estimated for each company where reliable results can be obtained. For the sector the average indexes were calculated using weights derived from the market shares of the companies. The data could be further disaggregated according to the background variables to study some sociological properties.

Each estimated model is empirically evaluated and clear-cut quality assurance indicators are given. Such Quality assessment measures are monitored for all steps of the process. These are related to the following aspects:

• Validity (relevance aspects);
• Availability;
• Simplicity;
• Comparability.

From a statistical perspective the models must possess enough predictive power and an ability to explain variation in data to make it meaningful for drawing inference. From a more general stakeholder perspective the models developed must be easy to understand and be relevant for the various users. The presented estimated models are *empirically evaluated* regarding:

- Reliability (precision, coverage and other accuracy components);
- Robustness;
- Predictive Power.

All these aspects are important in their own right. At the same time it should be observed that they are highly inter-related and require simultaneous attention in the design stage. Thus, fulfilment of acceptable levels for these criteria calls for strict handling of data collection throughout the process.

The following minimum quality requirements are agreed upon for each individual model to be part of the EPSI Rating approach. Any substantial failure to fulfil any of these must be commented and the reasons analysed.

### Precision

The 95 percent confidence interval for the customer satisfaction index must have a width of not more than 4 units (referring to an index scale of 0–100)[2] .

### Explanatory power

The econometric model must be able to explain approximately 65% of what drives customer satisfaction.

On average an error margin of 2 units has been realized for the indices (measured by a 95 percent confidence interval). This may be interpreted as confidence interval with 95 percent probability covering the true value (lies between the estimated value plus/minus 2 units).

## Satisfaction with the Insurance company – National benchmarks

The Insurance sector has been measured in the majority of Nordic countries since year 1999 in annual studies. The coverage has successively been increased and in 2007 both General Insurance (final Consumers and Corporate Customers) and Life/pension insurance (final Consumers) are covered in the majority of the Nordic markets. Below a few key trends and benchmark results are given.

### *General Insurance Private Consumer segment*

In the diagram below, the private consumers in the respective country give the scores of their General Insurance Company. The average for the entire region (calculated as the GDP-weighted average of the respective country result) has increased significantly since last year.

The Icelandic consumers give the lowest average scores, while Sweden falls on second place from the bottom. Denmark and Finland are on top. The highest relative increases are reported for Finland and Denmark during the entire period studied, while Norway has been stable sine 2005.

*Table 1. EPSI, General Insurance Private Consumer segment, Nordic countries, 2004 - 2007*

| **Final Consumers** | | **Satisfaction** | | |
|---|---|---|---|---|
| *Country* | *2004* | *2005* | *2006* | *2007* |
| Denmark | 73.0 | 74.2 | 74.6 | 77.7 |
| Finland | | 70.7 | 70.6 | 75.4 |
| Iceland | | 69.7 | 68.1 | 66.7 |
| Norway | 64.6 | 69.6 | 68.6 | 68.9 |
| Sweden | 65.9 | 66.7 | 67.2 | 67.6 |
| The Nordic Countries | 67.6 | 69.9 | 69.9 | 71.3 |

The satisfaction has improved significantly in both the Danish and Finnish sectors during the last year, while a small increase is registered for Sweden, a decrease in Iceland and fluctu-

## General Insurance EPSI Nordic Satisfaction 2004 - 2007
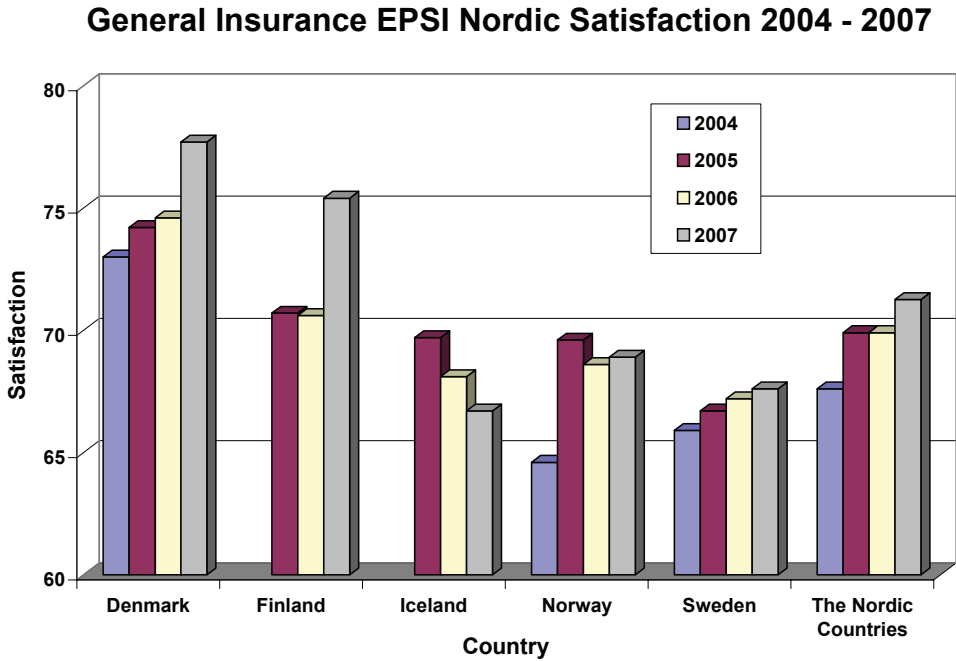


ations in Norway. The difference between the highest country average year 2007 (Denmark) and lowest (Iceland) is 11.2 units. The number of companies and spread in satisfaction within each country differ also quite a bit. This gap is taken as an indicator of the actual competitive situation in the respective nation The highest score for the Nordic region is obtained for the group "other insurance companies" in Denmark (with 83.4) and the lowest score in satisfaction for one of the main companies in Sweden (63.3).

The scores for insurance can be compared to the average for the economy in the respective country in order to tell whether this sector is strong or weak in terms of market transparency. This is illustrated in table 2. It is seen that the insurance sector is higher than the national average in Denmark, Finland and Norway, while on par with the national average in Iceland and lagging slightly behind in Sweden. For the Nordic region as such the Insurance sector obtains higher scores than the entire economy measured.

*Table 2: EPSI Economy scores compared to General Insurance 2007by country*

| Country | Economy | Insurance |
|---|---|---|
| Denmark | 70.3 | 77.7 |
| Finland | 72.6 | 75.4 |
| Iceland | 66.5 | 66.7 |
| Norway | 66.4 | 68.9 |
| Sweden | 68.4 | 67.6 |
| The Nordic Countries | 68.8 | 71.3 |

The profile of general insurance sector according to EPSI is illustrated in graph 2. The scores here relate to the model aspects above from company image through the other drivers to satisfaction (CSI) and perceived Loyalty.
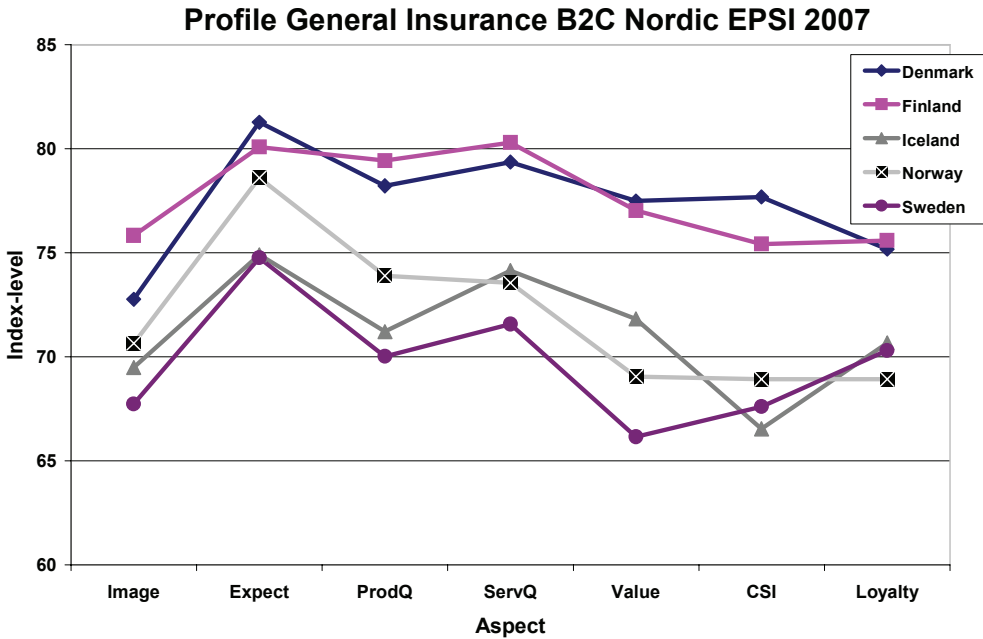
It is seen that the basic profile coincide between countries. At the same time a few special features are observed, like:

- Image is highest in Finland, and lowest in Sweden;
- The gap between expectations and perceived quality is largest in Norway and Sweden;
- The perception of value (for insurance fees) varies largely with Denmark and Finland on top and Sweden lowest according to the final consumers; and
- Perceived loyalty is lower than satisfaction in Denmark, while the opposite holds for Sweden and Iceland, illustrating a strong switching barrier in these countries.

### General Insurance corporate customer market

The coverage of also corporate Markets for General Insurance has successively been increased. The results for the last few years are illustrated in Table 3 and Graph 3.

*Table 3:* *EPSI - General Insurance, Corporate Customer segment, Nordic countries, 2004- 2007*

| *Corporate customers* | | *Satisfaction* | |
|---|---|---|---|
| *Country* | *2005* | *2006* | *2007* |
| Denmark | | 70.6 | 73.4 |
| Finland | 72.6 | 74.2 | 73.3 |
| Norway | 67.1 | 65.5 | 68.5 |
| Sweden | 65.3 | 66.9 | 68.8 |
| The Nordic Countries | 67.6 | 68.9 | 71.0 |

This means that the satisfaction among professional (corporate) customers (B2B segment) is almost as high as for final (individual) consumers (B2C segment). It has also improved more for corporate customers on average than for final consumers.

*Graph 3.* *Corporate Customer satisfaction EPSI 2005 - 2007*

## General Insurance Corporate customers EPSI Satisfaction 2005 - 2007
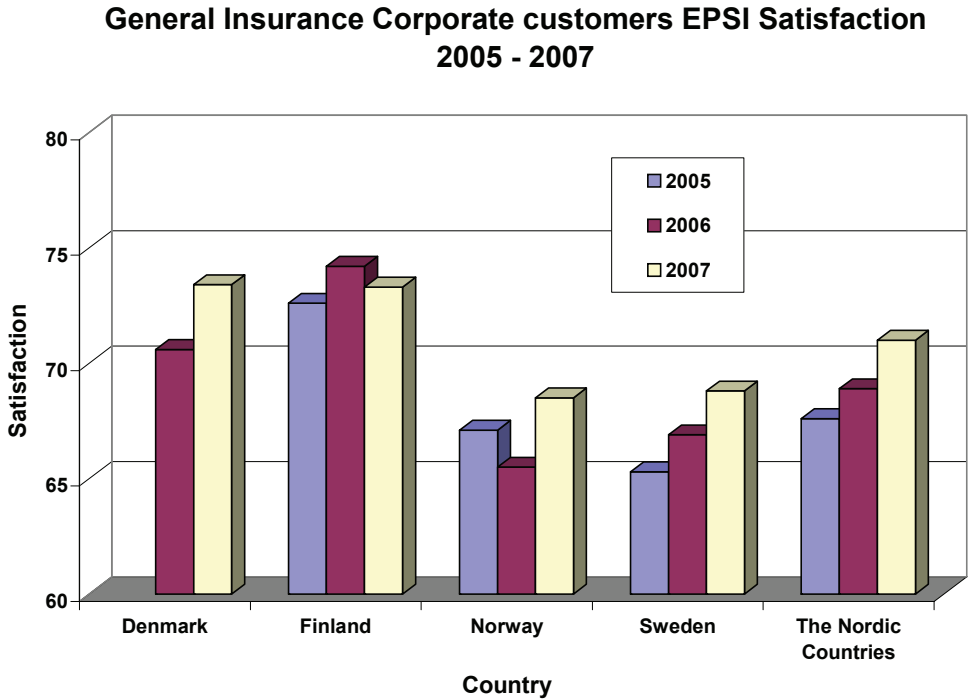


### Life/Pension Insurance, brokers and vehicle insurance in Sweden

Above, some core results for the general insurance industry were given. Within the insurance sector also other areas are successively being included in the regular EPSI studies. At present we have life insurance covered to some extent, as well as emerging studies for the insurance broker industry and special for the motor vehicle segment.

Time trends for the life/pension insurance segment are only available for Sweden so far, as this segment only recently was introduced into the studies in the other Nordic countries.

The Swedish life insurance market and the individual companies are illustrated below.

As can be seen Skandia constitutes a special case, and still exhibit a satisfaction level more than 10 units below any of the other measured companies. From the more detailed analysis it is clear that main explanatory factors for the low satisfaction with Skandia still has to do with image and service quality, while the score for product quality is (almost) on par with the industry average.

The main driver for explaining the satisfaction with the life insurance company, apart from the performance of the savings, is trust in the corporation. The explanation of the insurance product(s) that a life insurance customer has needs also further improvement according to the respondents to the survey.

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*Graph 4.* Customer Satisfaction Swedish Life insurance companies
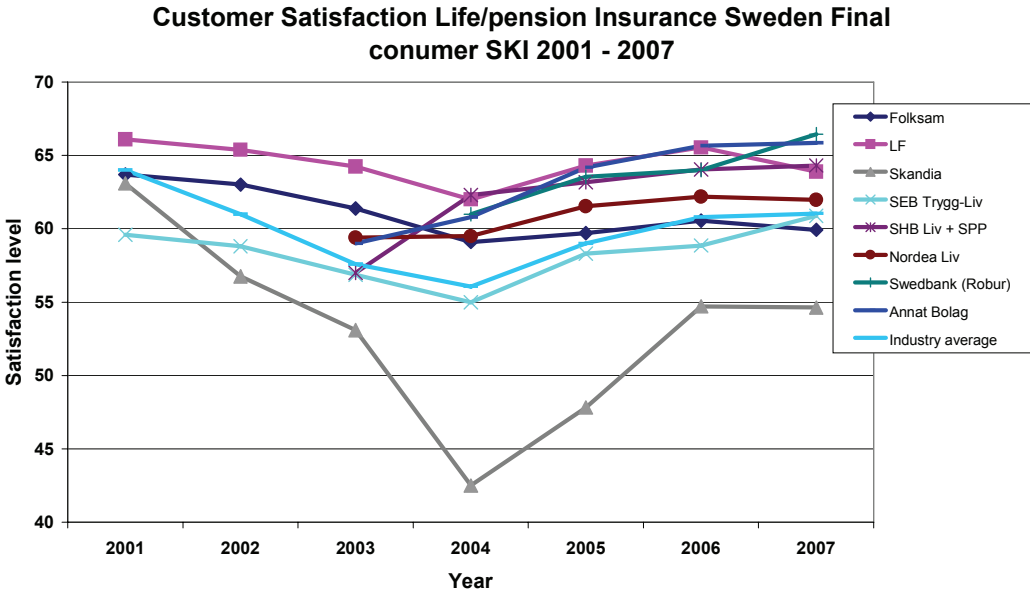
### Customer Satisfaction Life/pension Insurance Sweden Final conumer SKI 2001 - 2007



The main driver for explaining the satisfaction with the life insurance company, apart from the performance of the savings, is trust in the corporation. The explanation of the insurance product(s) that a life insurance customer has needs also further improvement according to the respondents to the survey.

In parallel to the above sketch, the rating by the corporate customers for life-insurance/ pension are as follows.

*Graph 5.* Profile for B2B insurance life/pension Sweden 2007

### Profile Life/pension B2B segment EPSI 2007 Sweden
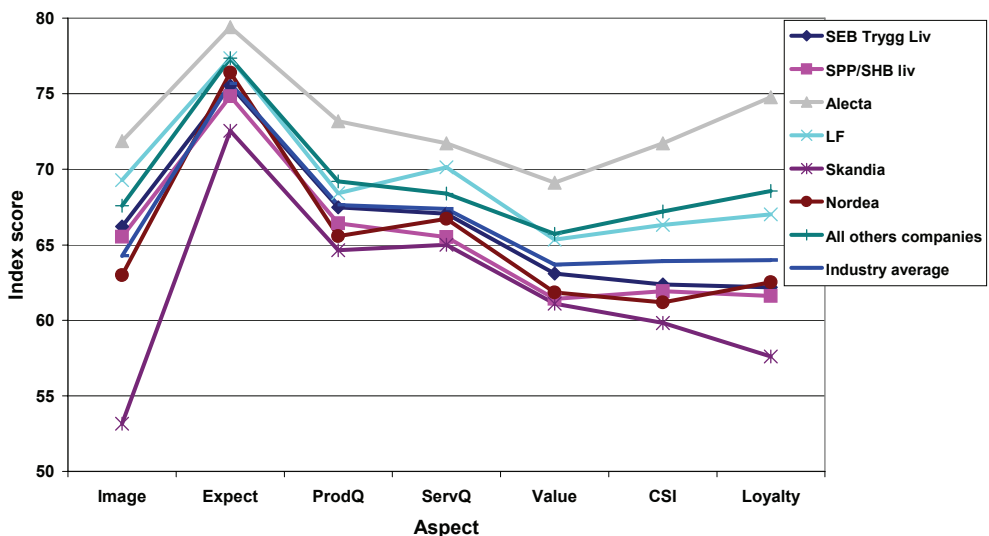
It is seen that the image as well as the loyalty (trust) in the company vary widely between insurance companies, while the expectations are more even. None of the insurance providers deliver product and service quality in accordance with what is expected. This gap is especially large for a few of the big banks, generating low satisfaction. Alecta has obtained the highest improvement in their overall scores from the previous year (2006).

### *Insurance brokers add value to the insurance products offered*

In corporate insurance (both general and life/pension) insurance brokers play an important role in all Nordic countries. Thus, the assessment of the performance by also the brokers,

are important in order to understand the functioning of the insurance sector. With a start from year 2007 EPSI has also initiated studies of insurance brokers. The first study was conducted in Sweden. The satisfaction levels are high (74.5 on average). Among the largest insurance brokers Söderberg and Partners and Säkra are on top. Länsförsäkringar are on top also among the customers to insurances through brokerage with If on second place.

The profile for corporate insurances via broker and those directly assigned by the customer are illustrated below.

The added value of brokerage in insurance is here estimated to be between 5 – 10 units on the EPSI scale (highest in the life/pension area).

*Graph 6.* Profile for B2B insurance through broker and direct relationship, Sweden 2007



**Profile by relationship Broker - direct EPSI 2007 Sweden**
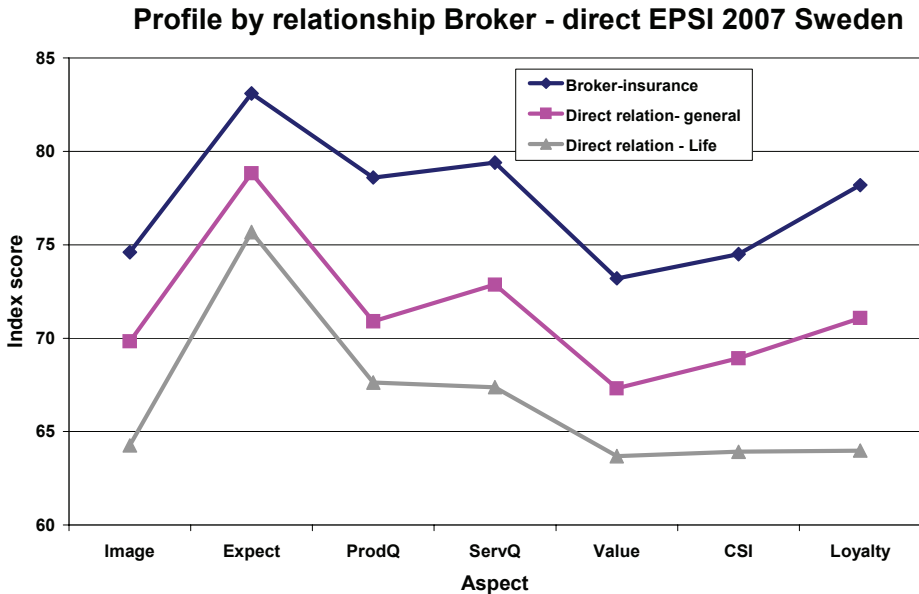
## Product specific rating indices – Vehicle insurance

Within the general insurance final consumer segment we have now extended the annual benchmark study to cover also a special survey of vehicle insurance in Sweden

The Satisfaction indices with the auto vehicle insurance company are given below for the Swedish market. Here also companies focussing on automotive insurance – including the various vehicle brands are included. It is to be noted that these vary quite a bit from the overall scores given for general insurance by the customers. The reason for this is that in the global study of general insurance the re-spondent is asked to think about the company with which he has the most active relation-ship. Vehicle insurance does not always come on top in that situation. More often home/villa-insurance is the first one to refer to by a responding consumer.

From the diagram below we see inter alia that the perceived loyalty differs within wide margins between companies. Volia and Läns-försäkringar have the strongest loyalty for a given satisfaction level (seen by the direction of the curve to the right) while both Folksam and Trygg Hansa show a low perceived loyal-ty. They have to work hard to maintain the current customer base for any given satisfac-tion level, as the curve points downwards.

<u>Graph 7.</u>  *Profile for B2C Vehicle insurance Sweden 2007*
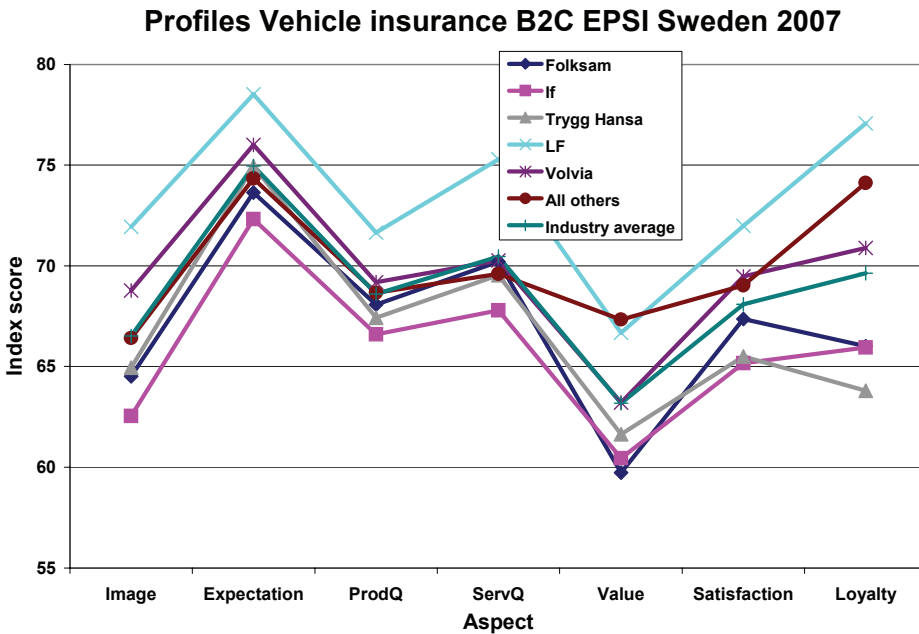
## Customers are different – Insurance company profiles

Customers are different, exhibiting varying satisfaction levels. Differences in customer profiles may depend on individual (socio-demographic and life-style) characteristics as well as on mis-matches between expectations and deliveries. The aim should certainly be to minimize the number of dis-satisfied customers at the same time as improving the satisfaction for those that are generating the lionshare of profits is rational. Analysis shows that sometimes golden clients have other priorities than average customers. However, all dis-satisfied customers constitute a threat to the recognition of the insurance company. Here also the handling of claims play an important role for satisfaction. All this is

possible to assess in the EPSI-approach.

As a standard rule-of-thumb it may be taken that customers with satisfaction below 60 are very dis-satisfied and vulnerable for leaving, and not least due to communicate bad word of mouth about the insurance company. In the same fashion, customers with satisfaction on 75 or above are most loyal and due to spread positive comments about the company. The profile below illustrates the situation. It is taken from the Norwegian general Insurance B2C-study 2007. As is clear from this the aim should be to reduce the percentage of customers with low loyalty for company 1. Their challenge is to try finding some "common features" among these customers in order to devise possible targeted improvement programs.

*Graph 8. Satisfaction profile by level*



**Spread Customer Satisfaction General Insurance B2C EPSI Norway 2007**
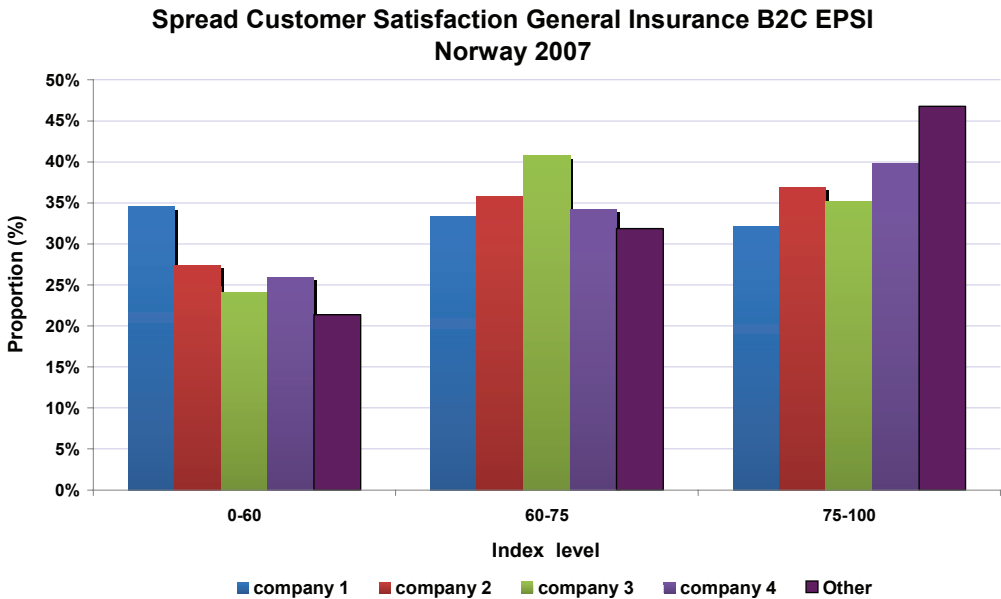
There is a strong relationship between satisfaction and loyalty as is illustrated by the following Graph 9, based on an analysis of the results for each individual insurance company (B2C-market) in the Nordic region measured separately 2006.

<u>Graph 9.</u> *Relationship between Satisfaction and Loyalty in Insurance sector*



**Customer satisfaction vs Loyalty**
**Propety insurance B2C 2006 EPSI Rating**
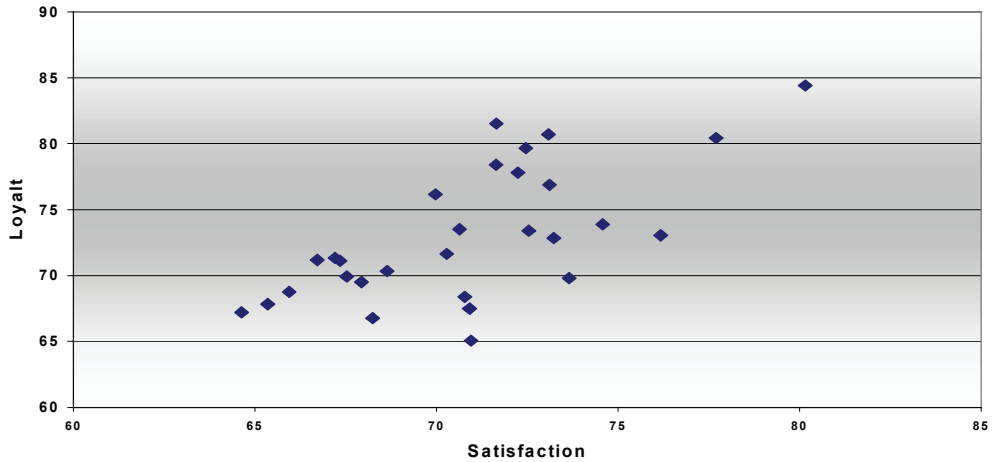
Most customers in the insurance sector do not actively consider any alternative to their current company, though the perceived loyalty for any given satisfaction level differs widely from company to company as was indicated above. In the following table the percentage of final consumers considering alternatives to their current general insurance company are given.

<u>Table 4.</u> *Percentage of final consumers by alternatives seen*

| Alternative to the current company | Denmark | Finland | Iceland | Norway | Sweden |
|---|---|---|---|---|---|
| No other company at all | 22.7 | 31.1 | 38.5 | 32.2 | 31.2 |
| ONE alternative insurance company | 8.1 | 27.7 | 22.3 | 14.3 | 26.1 |
| 2 - 3 alternative companies | 19.9 | 28.4 | 19.6 | 27.0 | 26.5 |
| 4 or more alternative insurance companies | 25.2 | 8.1 | 7.1 | 12.5 | 8.1 |
| Do not know | 24.1 | 4.8 | 12.5 | 14.0 | 8.2 |
| **Total percentage** | **100.0** | **100.0** | **100.0** | **100.0** | **100.0** |

As is seen from this table, the highest percentage of customers that see one or more competitors to the current insurance company is found in Denmark, while the lowest is in Iceland. At the same time, the percentage of customers answering "I do not know" is highest in Denmark.

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## Use of the results for Priority Setting

From the causal analysis it is possible to trace the relative importance/effects on satisfaction and loyalty of changing individual drivers. From the graph below it is illustrated that the effects differ significantly. The illustration is taken from the Danish general insurance B2C-segment. The value "total effect" tells how much satisfaction will be changed (improved) if the score on the respective driving latent variable is increased by one unit.

*Graph 10.* Total effects on satisfaction by driving aspect in model

**Total Effect from Drivers to Customer Satisfaction - EPSI Denmark 2007**
**Driver is increased by one unit**
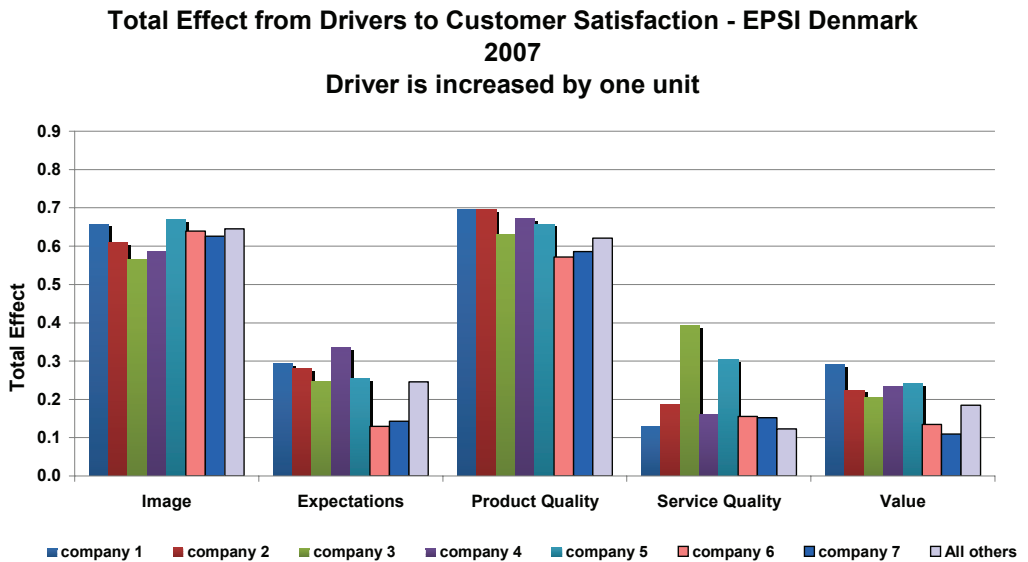


As is seen here, improvements in Product Quality will have the highest effect on Satisfaction – and from that on loyalty, with image as the second most effective. However for some individual companies (like company 6) the most effective strategy would be to focus on image (improve or at least maintain). At the same time it is seen that for company 3, "Service Quality" is a much more effective area for resources focusing than for any of the other considered insurance companies.

The driving aspects indicated above are general in character. For true improvement work it is crucial to being able to be more specific. This is possible by analysing individual manifest questions in the survey. Below, this is illustrated for one of the Finnish companies in the corporate segment. We focus on the latent drivers "Image" and "Value for Money".

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*Graph 11.* *Score and relative importance for improvement*

## Score and Weight Image EPSI Finland 2007
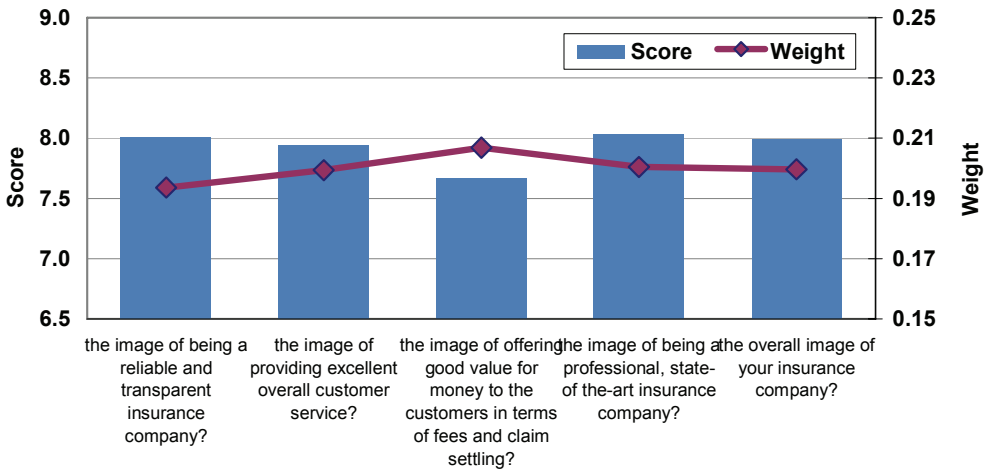


It is seen from the diagram that the score on the five different sub-aspects vary rather little (between 7.5 – 8 on the 10 unit scale used in interviews) for this company. The bars refer to the 5 questions in the survey related directly to the Image concept. Neither the relative weight of either of these vary much. That means that focus should be on the aspect(s)/variable(s) that is least expensive to improve. If improvement is targeted to the two aspects "excellent customer service" and "value for money perception", the following analysis and framework for evaluation may be specified.

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### Effect Calculation – Image

**A:** Improve the image of providing "excellent customer service" with one unit on 1-10 scale 2007 yields (result 2006 in parenthesis)…

….An increase in overall Image by 2.60 units (2.92 units last year)
….An increase in customer satisfaction by 1.63 units (1.93 units)

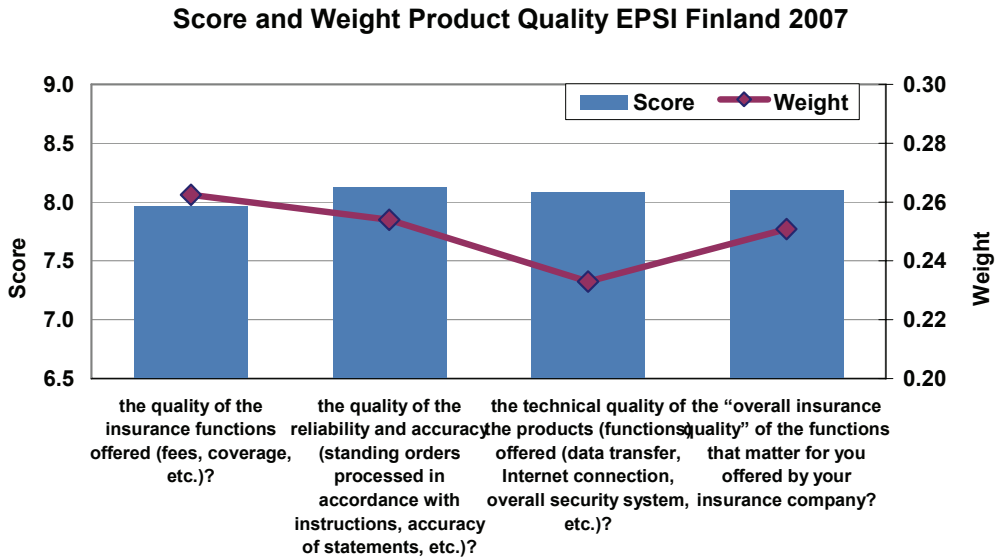**B**: Improve the image of providing "value for money" with one unit on 1-10 scale 2007 yields …..

….An increase in overall Image by 2.10 units
….An increase in customer satisfaction by 1.30 units

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The other important aspect for improving customer satisfaction in this situation (for the company and segment under consideration) is "Product Quality". Here four different questions are asked in the survey and the following analysis foundation may be specified.

<u>*Graph12.*</u> *Score and relative importance "Product Quality"*

## Score and Weight Product Quality EPSI Finland 2007



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### Effect Calculation - ProductQ

**A:** Improving the quality of the "reliability and accuracy" with one unit on 1-10 scale 2007 yields (result 2006 in parenthesis)…

….An increase in overall Product Quality by 2.94 units (3.14 units last year)
….An increase in customer satisfaction by 1.81 units (1.78 units)

**B:** Improving the quality of "product functions" with one unit on 1-10 scale 2007 yields …

….An increase in overall Product Quality by 2.70 units
….An increase in customer satisfaction by 1.66 units

Thus – provided these above aspects can be improved in the eyes of the customers it is possible to obtain a significant increase in satisfaction  (and consequently loyalty).

• With 1 unit each (from 7.9; 7.6; 7.9 and 8.1 respectively) – it is possible others have succeeded with improvements of 1 unit or more during 1 – 2 years time

• The customer satisfaction may (theoretically) improve with (up to) 6.4 units. Highly significant indeed!

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The above illustration gives some ideas about how the EPSI analysis model may be used for prioritizing alternative improvement schemes, and for successive follow-up and evaluating effects of undertaken activities. At this step, it must be kept in mind that preferences of the customers may change over time.  The ones expressed here are those obtained in the annual analyses in 2006 and 2007.

## Conclusions and possibilities for Improving Customer Trust

The Pan-Nordic EPSI studies will be run annually also in the future. The coverage and level of detail will be increased step-by-step. Combinations from the insurance sector with other industries will give insight into the general and specific characteristics of the insurance industry. At the same time the global scores may be used for assessing changes in the market operation and penetration within the sector, country by country. For individual companies and business areas the approach further gives insight for priority setting and evaluation work.

### Notes

[1] ECSI (1998), Foundation and Structure. In the end of 1990-s the European initiative to stimulate the development of National Customer Satisfaction studies was initiated. It started in the mid 1990s by discussions emerging from experience in Sweden, where a national platform was established in 1989, and from USA, where a national study similar to the Swedish model, commenced in 1994.

[2] Based on an explicit account of both sample and model uncertainty.

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