NEW MODEL ARMY

Aon UK chief executive Peter Harmer talks to IQ

When Peter Harmer accepted the commission of heading Aon UK at the start of 2007, he could have been forgiven for doing so with some trepidation.

On the back of two tough years, with significant job cuts and other efficiency measures in the UK as part of the broking giant's post-Spitzer rationalisation programme "Project Inflection", he might have expected to confront battle weary, beleaguered and unmotivated ranks.

The former head of the broker's Australian operations would also have to step into the shoes of Dennis Mahoney – an influential general who had effectively marshalled Aon's London market operations since 1984.

And not only would the Sydney native have to win support among a staff loyal to Mahoney, he would be expected to pick up the mantle of process reform that had been championed by his predecessor before his move to Bermuda as chairman of Aon Global.

Add the twin threat to margins of softening market conditions and an aggressive scramble for distribution among rival brokers and insurers alike, and the newcomer might have felt he had walked into a fire fight he couldn't win.

But less than 18 months into his tenure, *IQ* finds Harmer in relaxed and confident mood, as he lays out what he says is a model allowing Aon's UK operations to flex through the cycle, and shares his views on distribution and broker consolidators.

And in his new role as chairman of the Market Reform Group, he talks about London's competitiveness, and Aon's role in driving change...

How did you find Aon UK when you arrived, and what were your first priorities?

I arrived here expecting to find morale pretty low, with a disenfranchised workforce. We had just come off the back of two difficult years. A lot had gone on under Project Inflection to rebuild our operating model to match the new economic model in the post-Spitzer era after giving up a considerable sum in contingent commissions that was straight off the top and bottom line.

It's surprising the extent that "free income" allows you to not focus on a lot of the hard things you should do as a business. We had to play a game of catch-up in that period.

But I found a workforce that was surprisingly committed, with bundles of energy that was not necessarily finding the right outlet.

We had to find ways of simplifying our business to allow our employees to do what they do best.

How is that shaping the model and structure of the business in the UK?

As a broking industry we have become very fixated with the product. Although brokers will tell you they are risk advisors, the advice they typically provide is shaped to a great extent by the product. We had an opportunity to turn that model on its head.

We're partway through a three-year plan and have spent the last 18 months looking at simplifying the business, reducing bureaucracy to put decision making in the hands of those closest to clients, supporting the right governance framework, and preparing our employees better in areas such as financial literacy so time spent with clients is more productive.

We hope that work will put several points of margin into the business by the end of that process – that's a lot of money.

And how are you applying that in different areas of the business?

In our wholesale business – which accounts for about half of our UK revenue – we've accelerated investment in straight through processing, where we are accessing the London market on behalf of our network offices. That removes a layer of duplication and cost.

Once that infrastructure is in place, we become less of a funnel – i.e. processor and administrator – and can concentrate on the value-add around programme design and placement.

We're also looking to improve the global mobility of our workforce. In that model you're able to flex your resources to where it's needed at the time, depending on where you are in the cycle.

Initiatives like the work we're doing with RI3K then take on a whole new level of significance. The speed and urgency with which we're pushing that ahead is a function of our need to get that model in place before the market turns.

We've also looked closely at simplification across our SME client base. In one area we had 62 binding authorities with 18 distinct processes to support them. The processes of binding a risk ought to be the same across that customer segment. When you standardise and simplify you remove duplication and can invest more time with clients.

If you look at some of the broker models out there in the SME market you could say they are adding cost to the supply chain. If we can take a very different model to market that compresses that supply chain, reducing cost in a segment that is very price driven, we should have a competitive offering.

Is the consolidator model sustainable and is it a long-term threat?

In the short term it's very aggressive and a threat to our growth aspirations – particularly inorganic growth.

But in the longer term, I don't think a supply chain that spends 40-50 percent of the revenue in distribution is sustainable. And that unsustainability will be accelerated if we end up in a position of full transparency and disclosure on earnings – something we would certainly favour.

In a price driven sector, the secret to success is not in complicating the supply chain; it's in taking cost out. At the low end of the risk sophistication curve, we believe we have the insight and can design solutions for segments of clients.

We might be entering the market with facilities, or limited panels, but it doesn't change the fact our model is advisory – it's just that the advice is applied to the segment as opposed to individual clients.

As you move up the sophistication curve, that advisory model becomes more risk specific to the individual client, shaped within the needs of the segment.

Would Aon look to replicate the Towergate model – namely aggregating your business to negotiate larger commission terms?

It's not for me to be critical of the way our competitors build their business and you can't deny the success – measured in some terms – of those models.

But we can afford to take a long-term view. We're very satisfied with the way our work is developing in this area. I'm loathe to react to competitive pressures in the market place with a model I don't believe is sustainable. We have responsibilities to our clients, our people and to our markets.

We'll weather the storm quietly and we'll be around to pick up the pieces.

Does that assessment also apply to insurers, such as AXA, building distribution?

We moan about insurers interfering in our space, but then you have to ask why they are doing that.

They're doing it to get certainty over business flow. Does that mean our relationship with them wasn't strong enough for them to get that flow, and what does that say about our need to invest in supply side management?

If you think about what has typified the relationship between brokers and underwriters in the last five years it's been the constant grab for money. And what have brokers done? They've probably threatened carriers by moving portfolios of business to try and extract better terms. We're just not in that game.

But over time, you also have to look at the statements that brokers bought by carriers have made about maintaining their independence. All I would say is, good luck!

I think as customers become more savvy about risk and costs of providing product and service, these carrier owned distributors are going to come under a lot of pressure, and it will be very difficult for them to maintain the assertion that theirs is an advice based model.

The CEO of one insurer recently said that he expects the five percent his company sees of the broker's book it bought to increase to 25 percent. How can you make that claim but at the same time say you're going to be independent?

I think the FSA's flagged interest in this space is a very good thing – they're very well placed to take a view.

And, finally, how do you view the London market's progress in terms of process reform and competitiveness?

18 months ago the dialogue was around if, now it's around when – the market has crossed the Rubicon, it knows there's no alternative, and now it's about execution.

Often resistance to change is not founded in common sense. As far as Aon is concerned, we've copped some stick for taking big steps, but as I've said to our key trading partners, we didn't feel we had a choice.

We didn't want to embed additional cost in anyone else's business model, but if we didn't make a stand there would be no traction. We're hopeful the work we've done paves the way for others to come on board. We definitely need a market solution.

Is it down to the big brokers to drive that?

I think you'll find the three bigger players are all at different points in their evolutionary journey right now, so getting common ground it going to be difficult – and getting all three at the same place at the right time would be impossible. But two out of three? That's quite probable.