consumer intelligence

Pricing agility in general insurance:

Empower your organisation to survive and grow in a competitive and fast-moving market.

Foreword from our CEO

Ian Hughes, CEO

In the last decade, Consumer Intelligence has observed a radical change in the way that insurance is priced.

In this paper, we explore the current best practice in insurance pricing and give you some guidance about where the industry is about to go next.

Ten years ago, the cycle at which prices changed was measured in weeks and months and the feedback loops of success and failure were slow. Insurers would upload their rates to the pricing platforms about 2 weeks before the beginning of the month and then watch the results come in.

Today many more companies are in direct control of their prices and may change prices more than once per day. Some are now deploying artificial intelligence to help manage pricing for them.

The heart of this revolution is a muscle of raw processing power at lightening speeds and a flow of data which acts as the life blood of the industry. Pricing is now as much about data science and data sources as it is about actuarial science.

This paper will help you discover the state of the art as it exists today and give you a framework to assess your own position in relation to the competitive environment.

Our hope is that this will empower your organisation to survive in a world that is increasingly competitive and fast moving.

The importance of data in today's approach to pricing

Industry observers always say that claims are the shop window for insurance, but when it comes to getting people through the front door, having the right price is vital.

And underpinning everything in the world of pricing these days is one thing: data.

Having the right data allows actuaries and underwriters to analyse risk, the likelihood of a policyholder making a claim and the estimated size of that claim. But it can also do much more than that.

AXA technical director David Williams says "the vast array of data sources available today has transformed the pricing arena."

"If you compare the granularity of our pricing models now, compared with a few years ago, they've transformed, and the thing that's transformed them is the availability of additional data sources," David Williams says. "We will look at no end of potential data sources, see which ones have some benefit to us in terms of pricing and use them as appropriate."

"Every quotation these days is unique for an individual and a lot of that is based on external data and things that we haven't previously had available."

And these extra data sources allow insurers to price policies more appropriately, helping them to escape the race to the bottom that has been driven by the rise of the price comparison website and intensive commoditisation in the personal lines insurance market.

"The main reason we as insurers are after more appropriate data is that we want to better assess the risk we are writing; we want to understand the likelihood of someone having a claim and potentially the size of the claim as well," LV= head of direct motor pricing Draganco Trpcevski says. "That then translates to better pricing, which means we can give customers a fairer price – if you understand the risk better, those that are less likely to claim will get it cheaper and those more likely to claim will get a higher price."

When it comes to pricing performance, resources matter

This proliferation of data has, however, brought with it its own difficulties and complications, with more data needing more time and more resources to analyse it, all at a greater cost to the insurer or broker.

Consumer Intelligence key account director, Matthew Green, says a lack of resource in newer and smaller insurance companies can make it difficult for pricing departments to be effective in crafting tailored pricing strategies.

"For smaller insurers there is an issue with a lack of resource when it comes to pricing," he says. "Sometimes the pricing department can be just one person, so it can be quite a challenge to get the right price for the right business. Doing the day-to-day work means they can't do any analysis and it therefore becomes very difficult to add value to the business through better pricing."

The availability of the data itself can also be a problem for smaller players, and AXA's Williams says smaller insurers will always suffer from having less internal data to base their pricing decisions on.

"One of the disadvantages a small insurer will always have is, no matter how many actuaries or data scientists they employ and no matter how good they are, the data that they will have will be limited in size and it is easier to test things out with bigger datasets," he says.

Trpcevski agrees, and says that smaller and less established insurers can garner greater benefits from taking advantage of additional data sources outside of their organisation, helping them to close the gap on their rivals, and even carve out a competitive advantage.

> "External data sets are even more important for smaller insurers," he says. "The thing with data is that if the data is useful and no one else is using it, then that gives you a head start on the market, but if everyone else is using it and you're not, then you have to make up that gap. How you make up that gap by doing something other than using that same data is very difficult."

"You need to invest in top quality analytics, both the tools and the people to do the analysis, and then you need to be able to understand the analysis to see if it is valuable to you or not."

And Consumer Intelligence's Phil Paterson-Fox says bigger insurers have already made that move to take advantage of these new and emerging datasets, investing heavily in finding data that can help set them apart from their competitors.

"Where big insurers are winning is by using this external data to gain a competitive advantage, and that is difficult to compete with because smaller insurers don't necessarily have the resources to either buy the data in the first place and/or to analyse it," he says. "Insurance has always been about finding a pricing advantage, and data is what creates competitive advantage in the sector."

> "So if competitors haven't got access to the data you have, or haven't interrogated the linkages between risks and that data set, then that is going to give you a competitive advantage."

Price is still important, but it isn't everything

The advent of the aggregator market made price king when it came to consumer buying habits, but that doesn't mean you have to always be the cheapest in the market.

Insurers that have built a brand that is respected by consumers and represents trust can leverage this especially in the aggregator market, and Green says "competitor benchmarking can be used to optimise an insurer's position on an aggregator listing."

"Price is absolutely key, but it is not the only factor you need to consider," he says. "Some insurers will want to aim for position six or seven on the aggregator listings, but another brand, which may not have as much prestige, will aim for position one."

"Benchmarking is very important; there is not a one-size-fits-all solution, so you could have two insurers with very different approaches to the types of business they want to write, with very different ways of using data."

Our insight in action

- A home insurance brand was struggling to achieve conversions through the aggregators, despite having a product that they saw as being incredibly strong and competitively priced.
- Consumer Intelligence's data on real-life home insurance customers was able to determine that the company's aggregator product was not meeting the needs of the average home insurance purchaser, and as such the company was missing out on a sizeable share of the market as it was triggering the premium product and pushing it down the rankings.
- Consumer Intelligence was then able to use its in-depth knowledge of the customers they were targeting to help them build a product tailored for that specific segment of the market, and ensure they are listed in the rankings in their optimum position for converting quotes to sales.

This means that some insurers may decide to use pricing data to see where they are competitive and what percentage of consumers can make a saving when buying their product and then they use this insight to craft marketing messages for their advertising.

Another insurer may want to focus on their value proposition and price their product accordingly.

LV='s Trpcevski says his company uses such pricing data to analyse its competitiveness in different sectors of the market, and tailor pricing models accordingly.

"We look at how often we are top of the screen [on aggregators] and that gives us a good idea as to the competitiveness of our rate," he says. "We try and look at different segments and see where we are competitive and where we are not, and then that leads us to look into whether or not we are competitive in a particular segment, and whether or not we are happy with that."

"If we have a view to go into a segment where we are not particularly competitive, we will try and pick down into why we are not competitive: is it something we are doing? Do we have a different view to how that risk is written compared to the rest of the market? That then feeds back into our pricing and how we fit into the market."

For smaller brands, this benchmarking is often even more critical, as they do not have the brand strength to help draw in customers from lower positions on the aggregator listings.

> "If you are a smaller company, there is only one place you are going to be able to sell from, and that is the number one position," Consumer Intelligence insurance market specialist John Blevins says. "Although this is broadly true it doesn't mean you will automatically sell, however, if you are not there you don't really stand a chance. But, if you take one of the stronger brands, then they would not want to be in that first place, because they will feel that their brand can carry them from further down the list."

"We can show those smaller companies if they are the cheapest, how often they are the cheapest and if not, how far from the cheapest price they are."

The key to capitalising on this data, however, is knowing when (and how) to change your pricing strategy in reaction to market or competitor changes, and then reassessing the situation once the changes have taken effect.

As such, Consumer Intelligence's Paterson-Fox says price-testing is vital.

"The right data gives you the opportunity to test your rates prior to putting them out on an aggregator," he says. "As an insurer, unless you have incredibly flexible systems that allow you to change prices quickly, the volume of traffic on aggregators means any discrepancies in your pricing will be exposed very quickly."

> "If your goal is to maintain margin and focus on value, you can follow your pricing methodology because you probably don't need to look at it quite so often. But if you are about volume and competing at the top of the aggregators based on brand and conversion prices, then you need to change prices regularly."
>
> "The data allows you to adapt and respond to market conditions," he adds.

Don't leave it all on the table

As we have seen, brand positioning in an aggregator's listing is an essential part of any pricing strategy, but focusing too much on ranking can leave insurers open to missing out on valuable revenue.

As well as the ranking of a policy, insurers and brokers need to be aware of how close their premium is to their main rivals in the listing.

If the next cheapest policy is significantly higher than the premium you are quoting, then your prices could be raised without denting conversion rates. The amount that the gap can be closed by, ultimately depends on the relevant brand strength of you and your competitors.

> "A smaller player without a brand will have to be quite a bit cheaper than the next insurer on the list to even be considered," Blevins says. "On the flip-side, you can look at how far away you are from the insurer above you, and ask yourself given your margin can you compete?"

"Some insurers will be looking to get more margin on fewer policies, because they can then hold less risk, whereas others will be looking to get the volume of cases required to cover their fixed costs, and both will change prices accordingly."

But key to an effective use of this approach to pricing is understanding the strength of your brand, and here, once again, having the right data is key.

Paterson-Fox says: "Alongside the pricing data, we have consumer benchmarking data we can use to come up with a brand strength score, and we can then combine that with the pricing data. You can look at a brand's position on the aggregators and who is around them and then assess their threat based on brand strength.

"You can then start to optimise pricing by saying: I don't need to be rank one, but depending who is in rank one, two and three, I can rank in position four and still convert well because my brand is strong."

"That means you get a good margin and good volume," he adds. "It's the best of both worlds really."

AXA's Williams says his team spends a lot of time looking at market and competitor pricing to adjust the core technical price they have already calculated, allowing them to ensure maximum margin from a particular position within the market.

"We get a lot of information on where we are successful or otherwise on quotations and we build up layers. One of our layers is market pricing, so we will adapt our core technical price to reflect what we see is going on in the market, but that could be in either direction," he says. "We are confident in our pricing so we don't seek to match what someone else is doing, but if, for instance, our technical price was £500 and the next cheapest in the market was £600, well why would we quote £500? We'd be leaving money on the table."

> "If there is a segment of business we are particularly keen on, or a distribution channel, then we will sometimes reduce our rates if we are not seeing sufficient conversions, and tiny rate changes can make a massive difference to conversions. So it is about being very alert, proactive and knowing precisely what your conversion stats are at any moment in time, adjusting your pricing accordingly."

But this frequent tweaking of pricing does bring its own risks, and Trpcevski says constant vigilance is key to ensuring you are not leaving yourself exposed in the market. "You need to be flexible with your pricing, but if the market is moving in one direction and you've misstepped then you potentially need to be able to bring yourself back into line quickly (unless you are happy to be out of line), otherwise you could get left behind," he says.

Paterson-Fox adds: "You take your eye off the ball at your peril. It is not just about the price that you are offering, but also the price your competitors are offering and the techniques and tools you can use to get a competitive advantage in the channels in which you are operating."

> "But it is still really important to stay focused on your own pricing strategy, because if you get drawn into battle with a big player with deep pockets, prepared to operate at a loss because they are driving a volume target where they can take a shorter-term hit, that could be life-threatening for a smaller insurer."

Finding the right people, at the right price

The lifetime value of a policy is still an important underwriting metric despite the increase of churn in the market, and being able to find loyal customers hidden within a sea of potential new policyholders can really help insurers extract the most value from their new business.

5 key metrics for pricing policies outside of traditional risk factors

- Lifetime value
- Competitor and market rates
- Money left on the table
- Distribution channel behaviour
- Profit margins

"If you identify a tranche of customers that are likely to be more loyal and stick with you as a brand with an element of trust, then we can help you identify what that market looks like and then tailor the analysis specifically around that target group," Green says. "It is one thing to have an attractive price, but it is another to ensure you are getting it in front of the right people."

Trpcevski says that such knowledge then allows pricing teams to adjust prices in order to draw in potentially lucrative long-term customers.

"There is more churn nowadays, especially because of price comparison websites, so we do look at things like lifetime value to offer the best price we can," he says. "If we think someone is going to stay with us for a longer period of time then we will try and offer a more competitive price, because we know it makes commercial sense."

Blevins says that intermediaries can also benefit from this approach, adjusting the rate given to them by the insurer after giving full consideration to the lifetime value of a policy.

"Intermediaries are selling policies based on a net rate from the insurer, and they can either go above or below that net rate," he says. "They can't choose exactly who buys from them, so if they are selling to a customer they don't really want to buy from them; they want to get all of the benefit up front in that first purchase, so may increase the price."

"If it's a customer they believe they can cultivate and retain they may go below the net rate to secure that new business sale."

This method can, however, mean that insurers and intermediaries may make a loss on the first year of the policy, showing the importance of having the right data to make accurate calculations on the loyalty of particular customers.

> "Lifetime value is something we build into every price and, despite the churn, we rarely make a profit in the first year," Williams says. "In the old days we would look at demographic data that was pretty broad brush and take a view as to how long we were likely to retain a customer. But now, we can use external data to give us a better view on what the lifetime value is going to be on a particular customer and build that into the pricing."

As well as finding the right people for a particular policy, insurers also need to focus on finding the right customer for other products within their suite of policies. And Williams says this cross-selling of additional products is one area where insurers are letting themselves down.

"Insurers still have quite a long way to go when it comes to cross-selling," he says. "If you look at the likes of Amazon and Tesco with their clubcard, they are much better than insurers."

"Theoretically, we are beginning to use data to understand which products better suit our customers, so if we have a motor customer, which of our home products should we be marketing to them? Do they want a policy with all the bells and whistles, or do they want a more basic cover? Data can help us inform that process and tailor that product, but at the moment we are way behind the major retailers in that regard."

Consumer Intelligence's Green says this is once again where proper data analysis can help carve out a competitive edge.

"If an insurer knows it is competitive in certain areas of the market, then we can use our data to target other product lines where they will also be competitive for that particular customer and highlight opportunities where a cross-sell will be valuable," he says. "We can also identify which types of customers will be attracted and will be the most useful as a multi-product customer."

Intermediaries

As well as direct insurers and panel underwriters using data to drive effective pricing, intermediaries have an additional layer to consider. In addition to writing profitable business for the underwriter, intermediaries must also balance generating their own margins while still aiming to be competitive. Blevins says: "Intermediaries must factor in net rates from the underwriter, aggregator or new business acquisitions costs and commission charges, and then price accordingly."

Understanding their target customer base is key in deciding which risks to aim for and who is most likely to provide the most margin and lifetime value, but this is not always in line with the underwriter, hence the balancing act between healthy margins (lower loss ratios) for the underwriter and profitable margins for the intermediary.

"Intermediaries generally like customers paying on monthly instalments, which can generate substantial income, but a customer who pays in full is more favourable to the underwriter as they are less likely to be a fraudster, for example, or cancel their policy so the two can sometimes be at odds," Blevins says.

> "The underwriting rate for instalment business could therefore be higher than that of paid-in-full business. Intermediaries will then look to use their margins from monthly finance income, and the selling of add-on products such as breakdown or legal cover, to reduce the underwriting premium to secure this more profitable business for themselves."

"The underwriter gets their higher rate, the intermediary gets their instalment business and subsequent income, so as long as the underwriting footprint and loss ratios do not cause any problems, everyone wins. But, this is not always the case. If underwriters start to see increased claims then net rates increase to compensate, the intermediary in turn needs to invest more of their margin to remain competitive and a downward spiral ensues, leading to unsustainability."

Understanding where you are playing in the market and pricing to capture these demographics, is all about data collection and widening the sources to get as broad a view as possible, and understanding the implications on your pricing activity.

Alan Brown, director of operations at Ageas Retail says: "The big advantage of the direct players who dominate the market these days is that they have the ability to change pricing strategy instantly to respond to market conditions and maintain their volumes. For an intermediary to compete with that though they would also have to ensure that they are monitoring the market movements in the same way as the direct players do, and are willing to invest in the technology and resource required to allow them to maintain pace with the rest of the market."

> "This is actually one of the key benefits of insurer-hosted rating (IHR). Insurers who trade with brokers and intermediaries who have this technology, find that this closes the gap somewhat to direct players by allowing insurers to make changes overnight as opposed to the traditional method of sending rates to software houses six weeks before implementation."

Insurers can use this IHR technology to change rates without giving any notice to brokers as they will look to make changes that ultimately benefit them and their own results, so this can lead to conflicts between broker and insurer pricing and strategy.

Brown says: "You could have an insurer writing a lot of business that is working for you as a broker, and overnight they increase rates with no notice and you find your broker performance is immediately impacted."

Another consideration of IHR is that insurers have invested in counter fraud processes that are now built into these schemes. This not only improves the quality of business written through these schemes, but can help a broker reduce their costs because as IHR becomes more popular it could mean they no longer need to invest in their own processes.

Looking to the future

With a seemingly endless list of data sources available, direct insurers and brokers face the complex task of filtering through what does and doesn't matter to the risks they are holding and how they price quotes accordingly.

Continued commoditisation and new entrants into the market also means that the pressure to get this right will only increase.

Insurer-hosted rating is set to ease the pain of having to wait long-periods of time to make pricing changes, but it also presents new challenges. As market and competitor rates change more frequently, this creates an ever-changing landscape through which insurers and brokers need to navigate.

Ultimately, all of this means that having the right data, and the right analysis, will be the key to unlocking long-term success in a highly competitive marketplace.

7 steps to pricing agility

Where are you on the journey to pricing agility?

1 Understand current position of my brand within the market

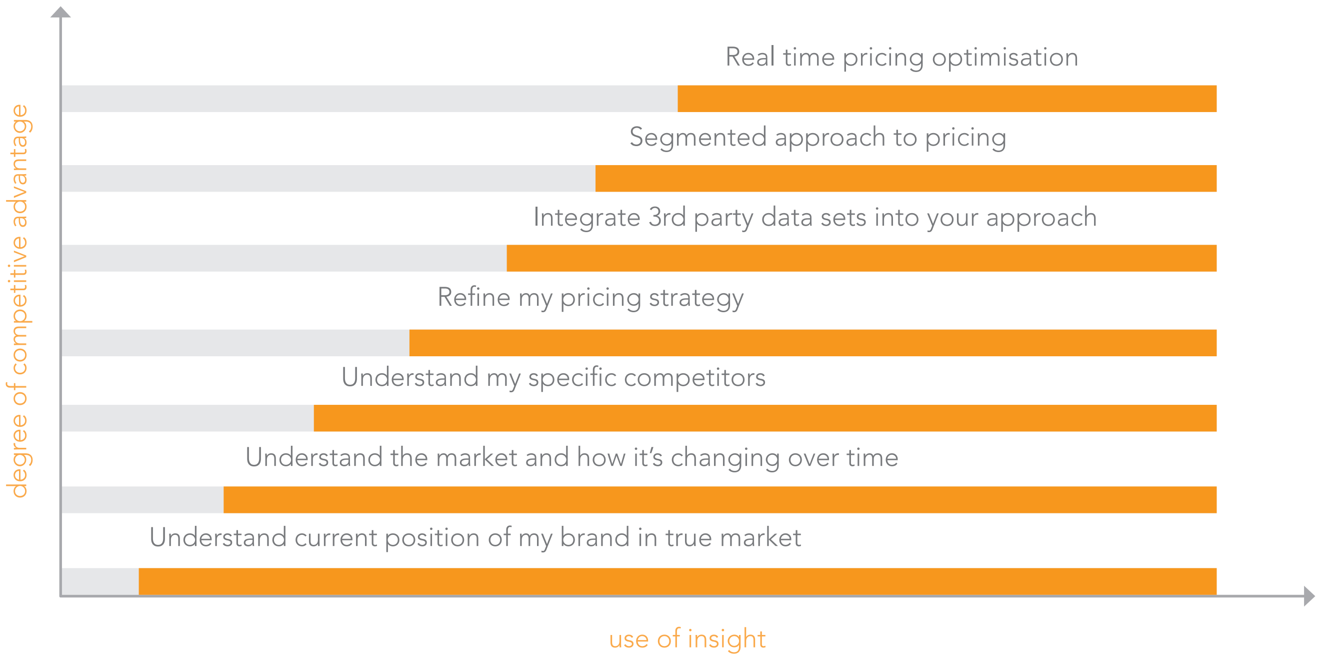
- Do I know how I benchmark against other brands in my market in terms of competitiveness?
- Do I know how I benchmark against other brands in my market in terms of quotability?
- Do I know how consistently my brand is performing across all channels I distribute through?
- Do I know who is competitive or quoting when my brand is not?

2 Understand the market and how it has changed over time

- Do I know how average premiums have changed in the past 12 months and how I compare?
- Do I know who has joined or left my market and if they are competitors to my brand?
- Have new underwriters joined the marketplace and how competitive could they be on my panel?

3 Understand my specific competitors

- Do I know who my true competitors are?
- Am I comparing myself to like for like competitors?
- Do I know how members of my underwriting panel perform on competitors' panels?



4 Refine my pricing strategy

- Do I have access to enough market data to allow me to understand where I can make effective changes?
- Do I have access to market data which helps to benchmark my pricing changes?
- Do I know by how much I am being beaten when I'm not competitive?
- Do I know how much money I am leaving on the table when I am competitive?
- Now I know where I am in the market do I need to reduce/open up my underwriting footprint or add/lose underwriters from my panel?

5 Integrate 3rd party data sets into your approach

- Do I have access to, and resource to study and use 3rd party data sets?
- Do I know which data I need and where to source this from?
- Do I use 3rd party data and overlay this with my own already? Do I need more?

6 Segmented approach to pricing

- Do I understand and can I tell which specific risk element I am most competitive for?
- Conversely do I know which risk element I am uncompetitive for?
- Do I know which channels offer me the best route to market when I have a competitive offering?

7 Real time pricing optimisation

- Do I have enough data to make confident pricing decisions?
- Do I have access to credible and reliable data frequently to help me make quick, effective decisions?
- Do I have access to frequent data which shows how effective my pricing changes have been?

About us

We can help you improve your pricing agility by helping you understand:

- How you perform in the marketplace and measure you against your true competitors.
- How the marketplace has changed over time and whether or not you are keeping up with those changes.
- How far away you are from the top brands when you are not competitive.
- How effective your panel is and which underwriters are competitive for your risk segment.

Consumer Intelligence is a market benchmarking and insight agency specialising in Insurance and Financial Services. We work in partnerships with our clients to help them create and protect distinct relationships with their customers through our unique combination of market and consumer insight.

We do this because we believe that companies who fixate on customer satisfaction will survive and grow.

We have over 13 years' quantitative and qualitative research experience and the insights we gather enables our clients to benchmark themselves, better understand their customers, and help attract new business.

Meet our experts

Matt Scott is an award-winning journalist and editor with an MSC in Actuarial Finance who specialises in data-led journalism and research for the insurance and financial services industries. He has previously worked as an editor for Insurance Times and as a contributor for the Chartered Insurance Institute.

John Blevins is a General Insurance specialist with 19 years experience in the insurance industry. Having worked as an intermediary, aggregator and direct insurer, John has accumulated a wealth of knowledge around how these markets operate. John is based in Scotland and recently joined Consumer Intelligence as product manager for general insurance pricing.

Matthew Green has been with Consumer Intelligence since 2012, helping some of the UK's biggest insurers interpret their customers needs and improve their pricing performance. Recently Matt has featured at various conferences on the subject of connected home and car insurance, plus the I Love Claims Home and Commercial events.

Phil Patterson-Fox has over 20 years' experience within the financial services sector, particularly in respect of general insurance. He has worked for a major bancassurer and one of the Big 4 price comparison websites providing a strong understanding of insurance distribution. He currently oversees a wide range of syndicated and bespoke research for CI clients and has run qualitative and quantitative research projects in previous roles.

Consumer Intelligence

Canard Court,
St Georges Road,
Bristol, BS1 5UU

0117 317 8181
insights@consumerintelligence.com
www.consumerintelligence.com

Consumer Intelligence | Pricing | Service | Proposition | Buying Behaviour | Customer Experience