2013 North America Auto Insurance Pricing Benchmark Survey

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Executive Summary

With the goal of helping insurance executives and pricing professionals learn from the experiences of their peers, Earnix conducted this survey to uncover pricing best practices used by North-American insurance companies in their auto business.

Survey responses were collected online from 73 executives and pricing professionals representing insurance companies that sell auto coverage in Canada and the United States.

Some of the key findings of the survey include:

- **The top three challenges in the pricing process are:**
  1. Effectively incorporating knowledge of customer price elasticity
  2. Getting and utilizing competitor data
  3. Predicting the business impact of new rates

- **The primary strategic goal influencing pricing changes over the past year was the drive for greater profitability,** mentioned by 68% of survey respondents.

- **72% of the respondents consider competitor's prices when setting their own prices.** Other considerations include customer price elasticity (55%), policy lifetime value (40%) and the value of other policies in the customer's portfolio (34%).

- **57% of the survey respondents differentiate new and renewal prices**.

- **The size of the company marks the way the overall effect of a rate change is estimated.** About half (48%) of the companies with over $1B GWP use segment-level demand models to estimate the effective rate change, while most (62%) of the smaller companies rerate their book (assuming 100% retention) to estimate the change.

- While the majority of the respondents take 1-2 months (46%) or less (18%) to implement new rates following filing approval, **35% take as long as 3-6 months to implement new rates.**

- 63% of the respondent either currently optimize their prices or have plans to implement optimization in the near future. **Of the companies with over $1B GWP, 45% currently optimize their prices and additional 29% are planning to optimize in the near future**.

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Pricing Drivers: Strategic Goals

The primary strategic goal influencing pricing changes over the past year was the drive for greater profitability, mentioned by 68% of survey respondents.

New customer acquisition (growth) was mentioned as the primary strategic driver by 19% of the respondents, and adopting of a consistent product design across the country was cited by 8% of survey respondents.
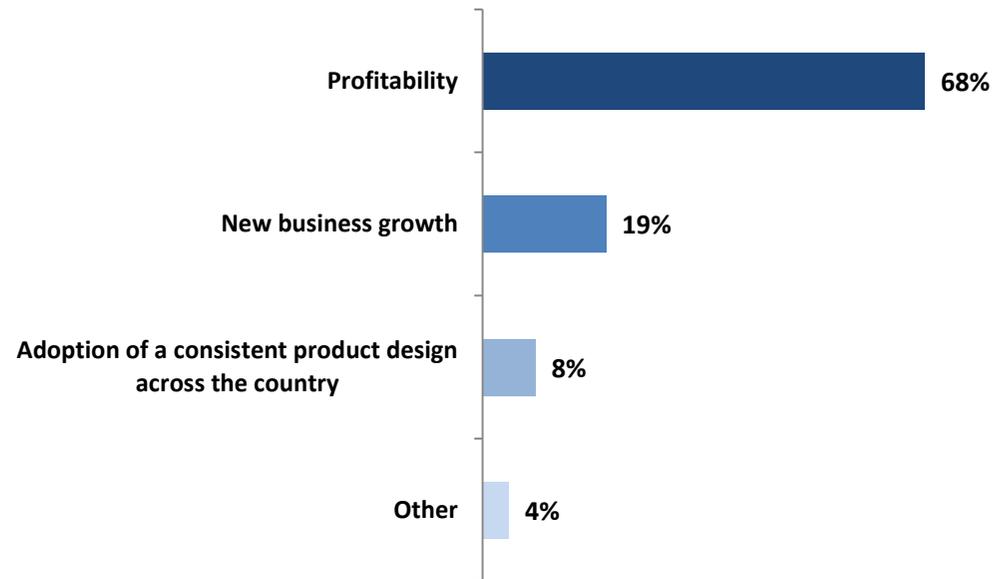
Figure 1: Strategic goals influencing rate changes

Pricing Drivers: Reasons for Rate Changes

The predominant reason for rate changes over the past year was changes in loss cost (62%).

Other reasons include response to the competition (16%) and new product design (14%).
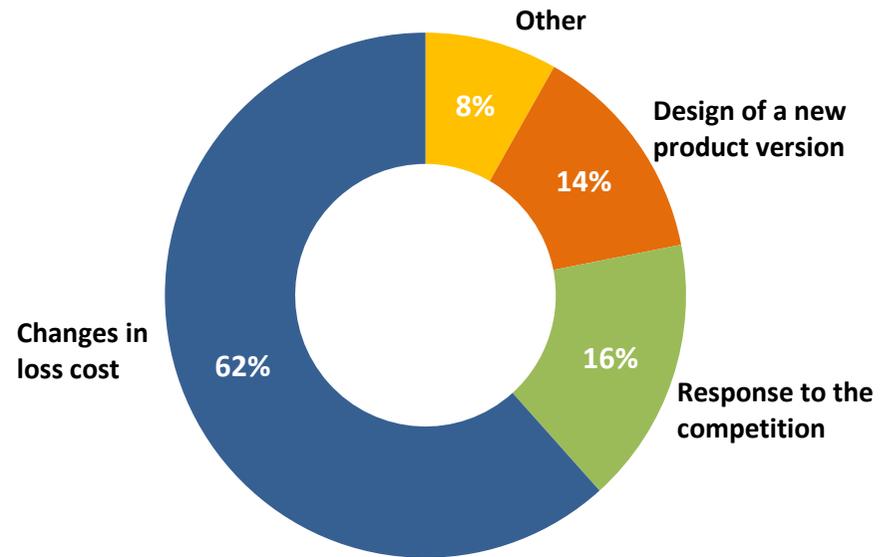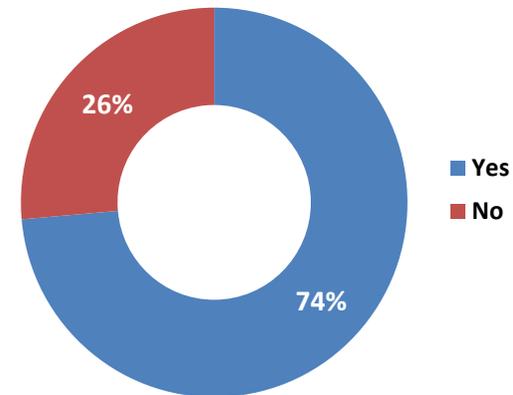

Figure 2: Reasons for pricing changes

Rate Change Schedule
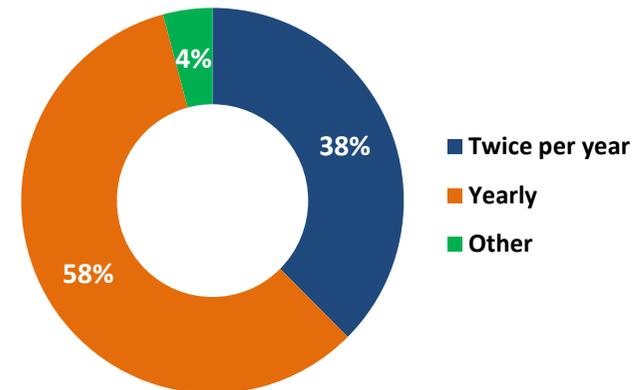
74% of the insurers participating in this survey have a set schedule for rate changes.

Figure 3: Have a set schedule for rate change

Over half (58%) of the respondents change their rates once a year.
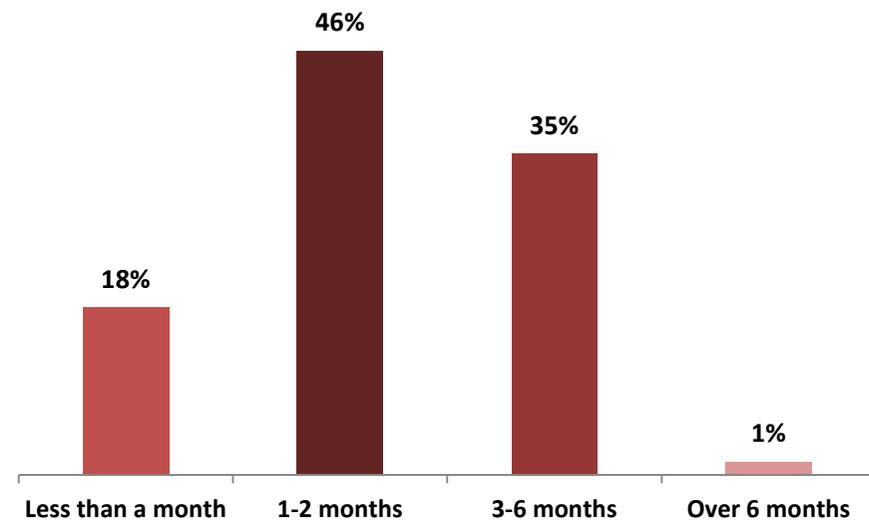
38% make changes twice a year.

Figure 4: Frequency of rate change

Time to Implement New Rates

While the majority of the respondents take 1-2 months (46%) or less (18%) to implement new rates following filing approval, **as many as 35% take as long as 3-6 months to implement new rates and 1% take longer than 6 months.**

Figure 5: Time to implement new rates

Time to Implement New Rates vs. Frequency of Rate Change

There is a strong correlation between the time to implement new rates and the frequency of rate change.

78% of the companies that change rates twice a year are able to implement new rates in two months or less, while only 57% of the companies that make changes just once a year are able to make changes that quickly.
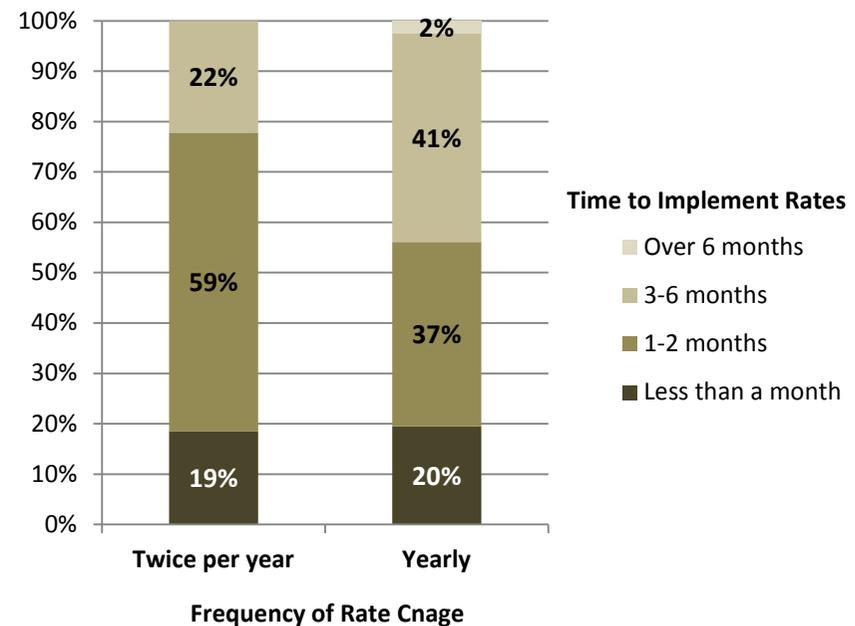

Figure 6: Time to implement new rates vs. frequency of rate change

Methods for Estimating the Overall Effect of a Rate Change

Companies use different methods for estimating the overall effect of a rate change.

The most common method, used by 51% of the respondents, assumes 100% retention and no effect on new business conversion (e.g., a 5% rate increase will result in a 5% premium growth).

29% of the respondents use statistical models of customer demand to predict the effect of any rate change.

21% of the respondents use a rule of thumb, typically based on some history with rate changes across the company (for example, a 10% increase in premiums would result in a 2% relative drop in retention).
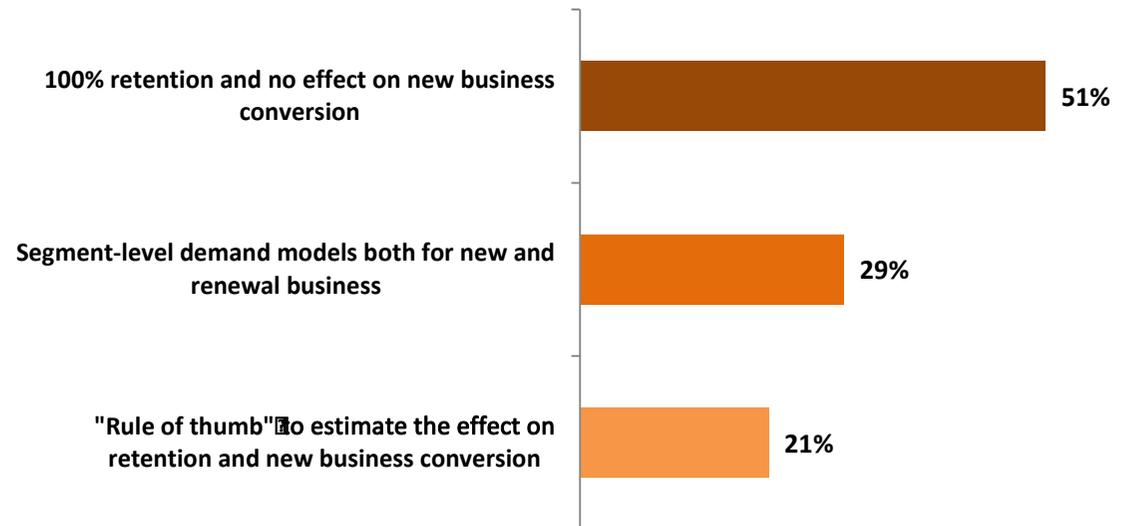

Figure 7: Methods for estimating the overall effect of a rate change

Estimating the Overall Effect of a Rate Change

The size of the company marks the way the overall effect of a rate change is estimated.

About half (48%) of the companies with over $1B GWP use segment-level demand models to estimate the effective rate change, while most (62%) of the smaller companies just rerate their in-force book assuming 100% retention.
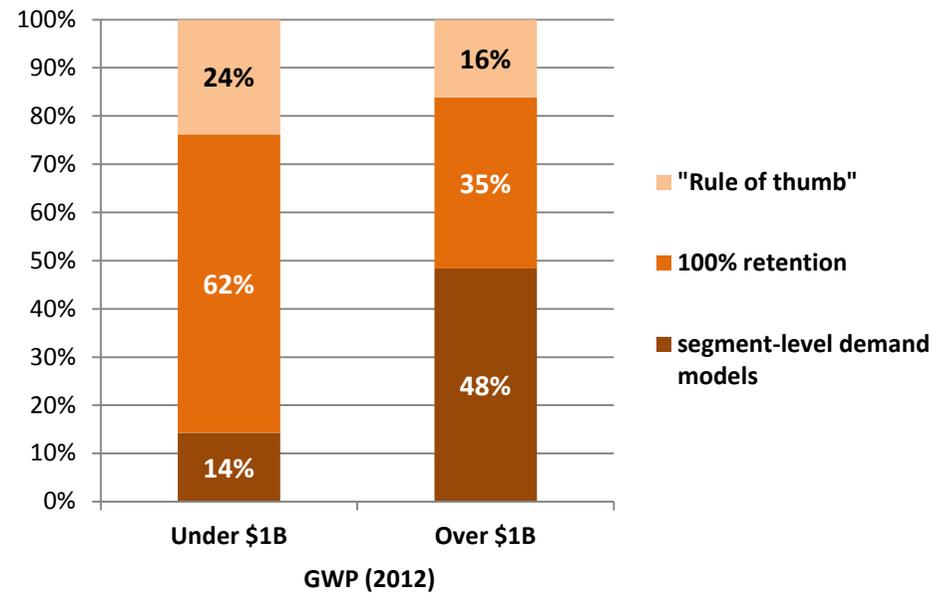

Figure 8: Estimating the overall effect of a rate change by company size

Differentiating New and Renewal Prices

57% of the survey respondents differentiate new and renewal prices.

The most common strategy for differentiating new and renewal prices involves discounts that apply exclusively to new business (64%) or renewals (48%).

Other strategies include renewal rate caps (38%), tiering rules that apply only to new business (31%), and the use of a separate company to introduce a new product version (31%).
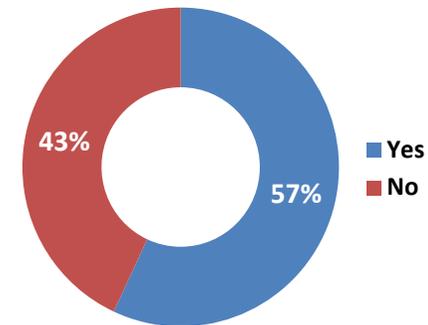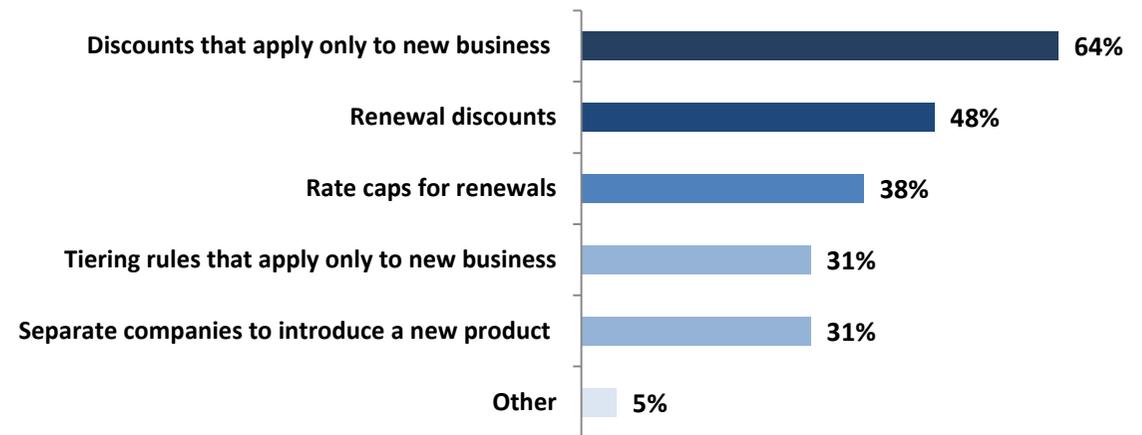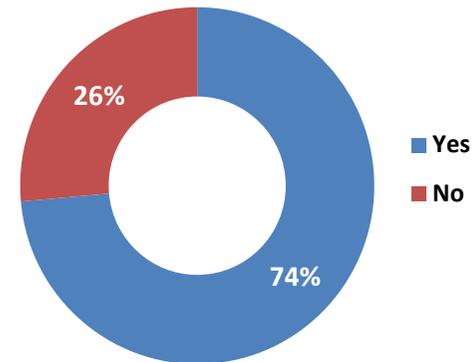

Figure 9: Differentiate new and renewal prices

Figure 10: Ways to differentiate new and renewal prices

Rate Caps

Of the companies that use renewal rate caps, **the vast majority (74%) apply different (nonsymmetrical) caps for rate increases vs. rate decreases.**


Figure 11: Different caps for rate increase vs. rate decrease

Other Considerations When Setting Prices

72% of the insurers that participated in the survey consider competitors' prices in their rate setting process.

Other considerations include customer price elasticity (55%), policy lifetime value mentioned (40%), and the value of other policies in the customer's portfolio (34%).
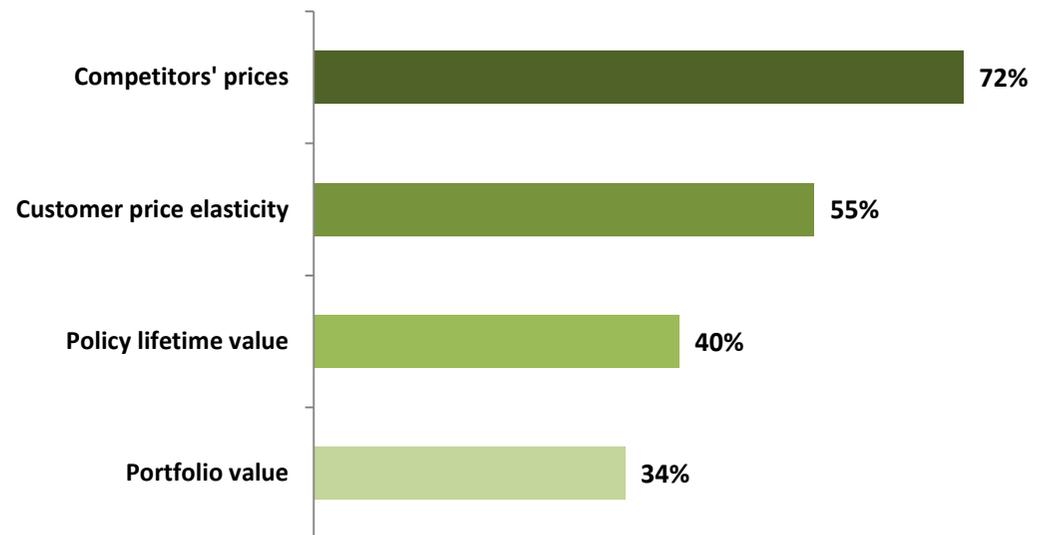
Figure 12: Considerations included in price calculation

Use of Elasticity Models

Most of those that use price elasticity models apply it to both renewals and new business (70%), while 16% use it just for new business and 14% for renewals only.

The most common use of elasticity models is for factor selection, mentioned by 58% of the companies that use such models.

50% of these companies use the models to estimate the effect of a rate change, 39% for product design, and 32% to determine factors via an optimization algorithm (respondents could choose more than one answer).
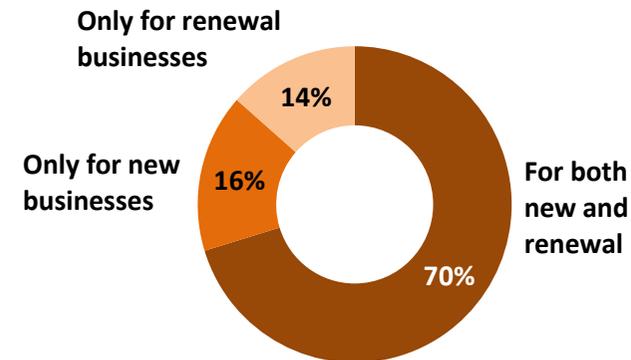
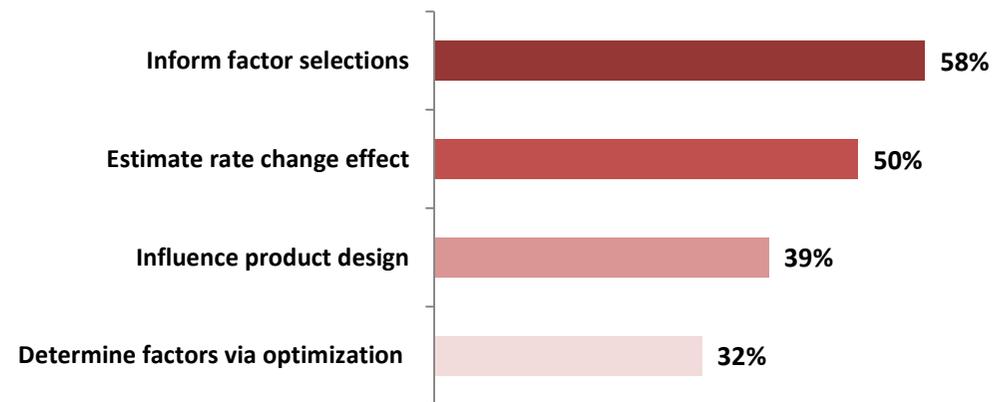*Figure 13: Business segment use of elasticity models*

Figure 14: Functional use of elasticity models

Pricing Process Challenges

When asked to rate the top challenges in their pricing processes, respondents pointed out to the following challenges (in order of rating):

1. **Effectively incorporating knowledge of customer price elasticity**
2. **Getting and utilizing competitor data**
3. **Predicting the business impact of new rates**
4. Getting and utilizing the right customer data
5. Time lag for implementing new rates in IT systems
6. Ensuring regulatory compliance
7. Collaborating and communicating with all stakeholders in the process
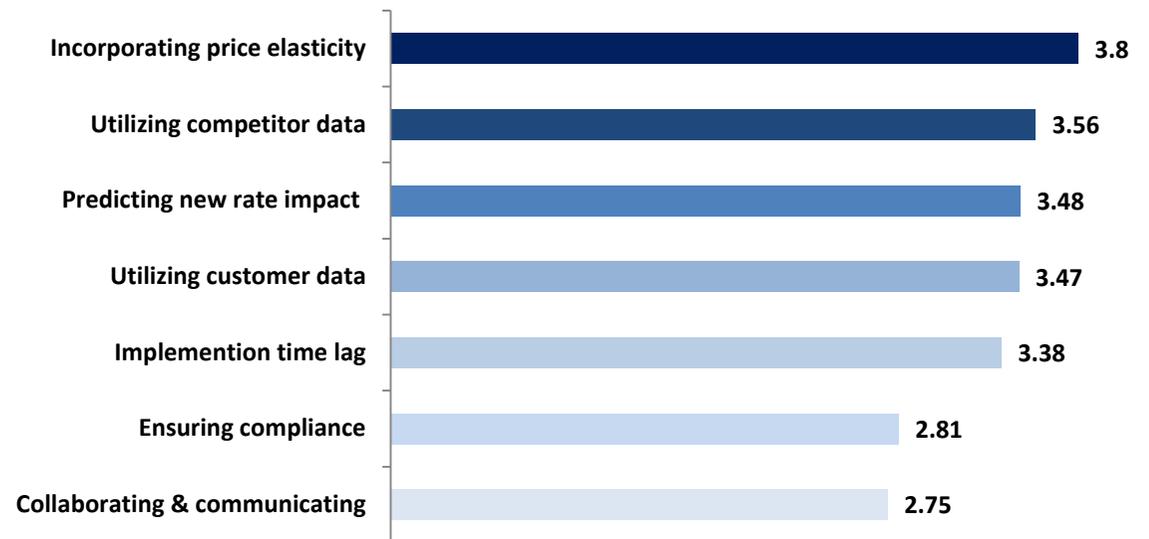
Figure 15: Pricing process challenges (on a 1-5 scale)

Pricing Systems

Over half of the respondents (57%) say they have a common system for managing the pricing process across the organization (R&D, Pricing and Product/State Management) **while 43% don't have such a system in place**.

Figure 16: Common pricing systems across the organizations

Almost all of the respondents (86%) use spreadsheets in the pricing process, and 71% use a statistical program.

36% use commercially-developed pricing software, while 33% use an internally-developed pricing system.
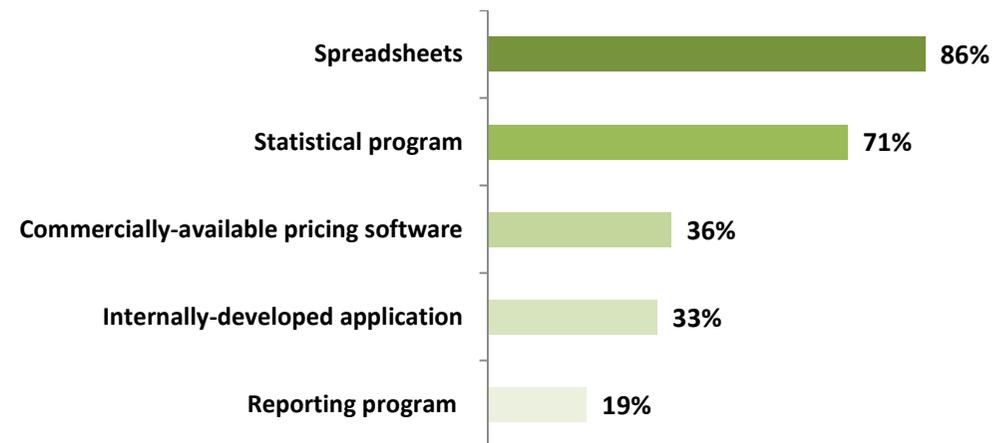
Figure 17: Systems used in the pricing process

Price Optimization

Price optimization is defined as using mathematical algorithms to determine optimal values of rating factors to meet certain business goals and constraints (e.g. maximizing profitability while achieving X% of policy growth).

Overall, 26% of the respondents currently use pricing optimization, and additional 36% have plans to implement optimization in the near future.

No plans
15%

Currently use
26%

Probably in
the future
22%

Planning to
optimize in the
near future
36%
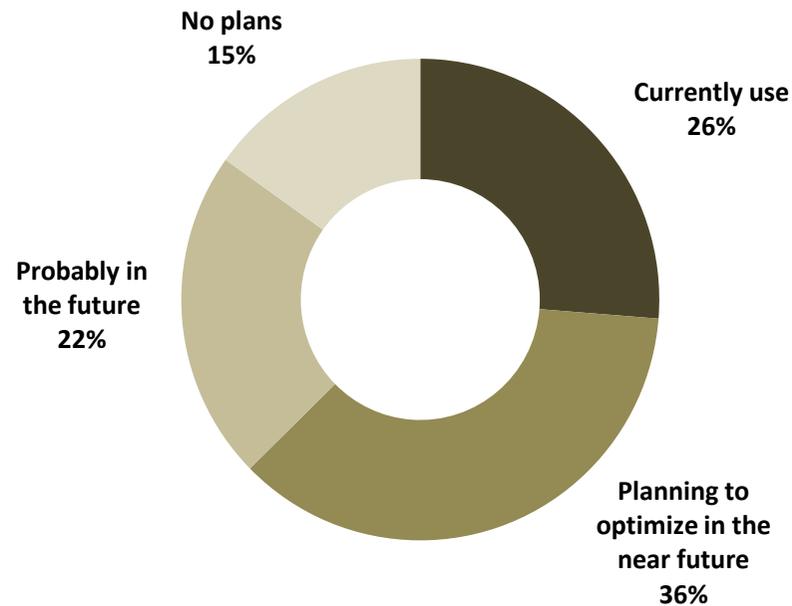
Figure 18: Plans for price optimization

Price Optimization by Company Size

The larger companies are the ones leading the charge. **Of the companies with over $1B GWP, 45% currently optimize their prices and an additional 29% are planning to adopt optimization in the near future**.

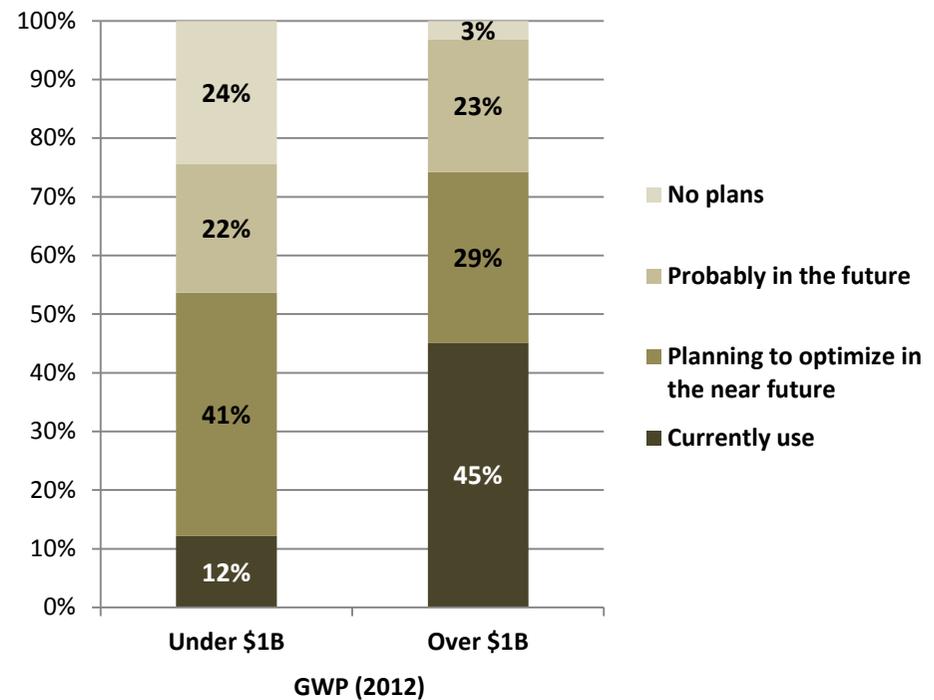Only 3% of the companies with over $1B have no plans for price optimization.

Figure 19: Plans for price optimization by company size

Respondent Demographics: Product Offered

The survey was completed by 73 representatives of auto insurance carriers operating in the United States (86%) and Canada (14%).

In addition to auto insurance, 84% of the respondents also write homeowners insurance and 34% write other insurance types including, umbrella, commercial, boat, and farm owner insurance.
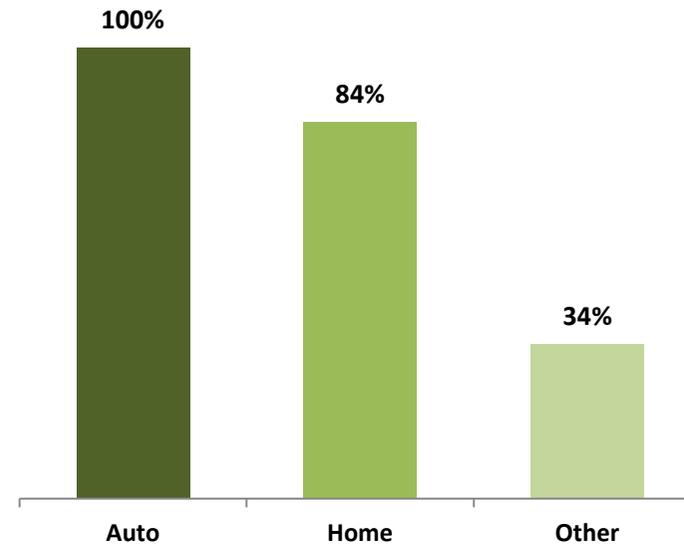
Figure 20: Products offered

Respondent Demographics: Book Size

Survey respondents represent a mix of small and large companies.

57% are coming from companies with up to $1B of auto insurance Gross Written Premium (GWP) and 43% are from companies writing over $1B in premiums (2012 figures).
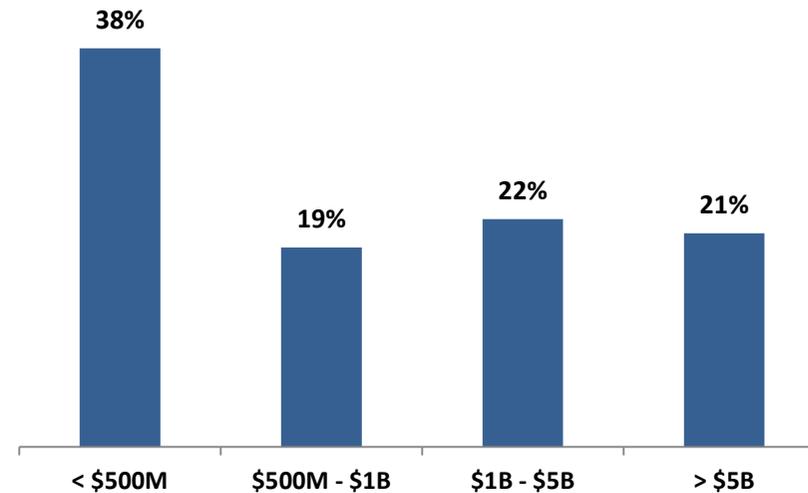
Figure 21: Auto insurance Gross Written Premium (2012)

Respondent Demographics: Respondents Roles

28% of the survey respondents are pricing analysts or managers, while 23% hold executive management positions.

15% are product or state managers, and another 15% are R&D analysts or managers.

Figure 22: Respondent roles

Legend:
- Pricing Analyst or Manager
- Executive Management
- Product/State Manager
- R&D Analyst or Manager
- Marketing Analyst or Manager
- IT

Pie chart values: 28%, 23%, 15%, 15%, 3%, 3%, 13%

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Earnix Integrated Pricing and Customer Analytics™ software empowers financial services companies to predict customer demand and its impact on business performance, enabling the alignment of pricing and products with changing market dynamics. Earnix combines risk and demand modeling with real-time connectivity to core operational systems, bringing the power of analytic-driven decisions to every customer interaction in any regulatory environment. Leading banks and insurance companies rely on Earnix solutions to optimize the prices of deposits, loans, and policies, delivering greater value to customers and higher returns to shareholders.

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