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Removal of Gender Bias in Insurance Creates Need for New Pricing Strategy in Europe

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The insurance industry in Europe received a jolt with the March 2011 ruling by the European Court of Justice that gender cannot be a risk factor in determining an insurance premium. Women have so far been paying lower premiums than men while buying car insurance and life insurance, whilst suffering with lower pension annuity rates. The ruling comes at a time when the industry is recovering from the impact of the financial market crisis. Low interest rates and a weak market have taken a toll on both the life and non-life sectors. The latest development has further dampened spirits.

Traditionally, the insurance sector in Europe has struggled with tight regulatory controls. In two surveys conducted by the Centre for the Study of Financial Innovation, in coordination with PricewaterhouseCoopers, in 2007 and 2009, termed Insurance Banana Skins survey, ‘too much regulation’ has been identified as one of the top five risk factors for the industry. In 2007, survey respondents constituting primarily of insurance industry professionals from Europe, placed it as the topmost risk factor. In 2009, the fall-out of the credit crunch took precedence over other concerns and regulatory control slipped to the number five worrying factor for industry professionals. The latest ruling brings it back into focus. The ruling comes into effect from December 2012 but changes in premiums could start before that.

In the past couple of years, growth for the insurance industry in Europe has been stymied by tough economic realities. According to an Ernst & Young report on the Europe insurance outlook, this year began on a stronger financial note than did 2010, but the sluggish economy throughout Europe and low interest rates will continue to be the main obstacles for high growth. In this environment, the ruling against gender discrimination may turn away women customers and create further capital crunch.

How Does the Ruling Affect the Industry?

Let’s examine the implications of the court ruling. Motor insurance providers now cannot use historical data to support their policy of offering different premiums to men and women. In the case of motor insurance, the gender-based discrimination was founded on the argument that women were safer drivers and far less likely to make an insurance claim. Even if they did, the size of the claim was likely to be far lower than that of a man in the same age group. The BBC reported the British Insurance Brokers' Association (BIBA) as saying that currently the cost of the average car claim by an 18-year old man was GBP 4,400, while that for an 18-year old woman was GBP 2,700.

In effect, now women motorists, who earlier paid close to 50 percent less premium than men in the same age group, will have to pay the price of cross-subsidization for men. The rise in premium will be significant; for instance, for a woman under 25 years of age, there may be a 25 percent hike which could even go up to 60 percent. Insurance companies are now faced with the grave risk of losing women customers because of this sudden rise in premiums.

The same holds true for life insurance and pension annuity. Historical data shows that women live longer than men and hence the premium that they pay for their life insurance has been much lower than that by men. Now that differentiation goes. There will have to be one rate for men and women of the same age and with similar other risk factors. Insurers will now have to blend rates to bring down the premium for men and take the premium for women up. For a woman under 30, the cost of life insurance may go up to 25 – 30 percent and for a man of that age, it may go down by 10 percent.

Income from pension annuities will change. Older men will have to bear a fall in their income from annuities and women will see a rise. So far, for a particular sum, a woman was getting lesser annual pension income than a man of the same age because she was expected to live longer. But with the gender factor out of the way, both men and women will receive the same pension annuity.

The BBC reported Graeme Trudgill of BIBA as saying, "The ruling will have a significant effect on the insurance industry which has used the system of risk-based pricing to award discounts to lower risk drivers like young females who are statistically safer drivers" Now to sustain its women client base in motor and life insurance and grow it in the years ahead, insurance companies will have to look for newer ways to make its product pricing attractive. Efforts have to go in to classify new parameters to calculate risks. For instance, a person's behavior or attitude could be a parameter to ascertain the risk he or she faces. The second way of mitigating the possible crisis is by introducing different products for different sorts of risks. But how does an insurance provider devise new parameters and design new products to effectively reverse the negative sentiments among its women customers?

Research and Analytics Shows the Way

This is where the role of Research and Analytics (R&A) comes in. An offshore company with the right R&A capabilities can help an insurance provider come out with a new pricing model based on a different set of risk parameters and new products designed for different categories of risk.

New parameters can also be deduced from data that comes out of telematics capabilities installed in vehicles. Telematics features in vehicles work like the black box in an aircraft which records all data about the vehicle and the driver. Analysing vehicle telematics data will throw up unique characteristics of drivers from which new risk parameters can be drawn.

WNS, a leading Business Process Outsourcing (BPO) company, employs its rich R&A capabilities to devise comprehensive pricing models for clients. The WNS R&A-powered pricing strategy is three-pronged:

- It looks at the ability of the client to compete effectively by implementing a pricing strategy based on business goals such as profitability and customer retention.
- It helps the client understand the various customer segments and each segment's price sensitivity towards each brand.
- It is a step away from traditional pricing models and includes competitor price, demand and risk / loss cost in determining rating factors.

WNS Designs a Demand Pricing Model for an Insurance Client

Let's look at a customer success story to understand how the WNS pricing model worked for an insurance client. A U.S.-based property and casualty insurer was faced with stagnant growth and wanted to understand the drivers of demand for customer retention, mid-term cancellation and conversion or acquisition of insurance policies in the auto insurance market. Insurance companies have traditionally priced their products based on the estimated costs incurred in the payment of claims. This model does not include demand-side pricing, or the customer's willingness to pay.

WNS designed a price optimization process that helped the insurer identify the drivers for customer retention, or the factors that make the customer continue to pay the premium. The client used the drivers identified by the WNS R&A team to understand policyholders' behavior better and predict retention patterns. The models helped identify factors that drive demand and segment customers according to their willingness to pay. It also offered a clear picture of customers' price elasticity at different price points. The process included extraction of data to create predictive models, make projections of future demand and test various scenarios to develop optimal pricing.

The WNS analytics solution enabled the client to improve policy retention and maintain the same levels of profitability by deploying demand models in their pricing strategy. The demand-pricing model for auto insurance products, once proved successful in its pilot launch in one state, was extended to other states in the U.S. as part of its nationwide strategy.

Backed by deep knowledge and experience in analytics, WNS can provide European insurance providers better insights into customer behavior and risk propensity. These factors can go into designing new pricing parameters and products that blunt the impact that the gender ruling has brought about in the market. With the new parameters, insurance providers can segment customers into different risk categories at different price points and offer them more targeted products.

To learn more, please write to us at **info@wns.com**