PINNACLE
ACTUARIAL RESOURCES, INC.
Commitment Beyond Numbers

Monograph

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Ms. Walker also has considerable experience in the development and monitoring of key metrics, attestation and management reporting, data governance and trend analysis.

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Competitive Intelligence – An Insurance Policy for Pricing

Kathryn A. Walker, FCAS, MAAA, CPCU

Insurance carriers are continually looking for a competitive advantage through initiatives such as new product offerings, unique customer segmentation, innovative rating variables and deeper market knowledge. Each of these is a stepping stone to growth and profitability. However, insurers are challenged to connect these into a cohesive business strategy. The decentralized core processes of rating, product development, underwriting and marketing have created competing goals and disconnected views of the business.

As insurers strive to become more innovative and add increased analytics and metrics to their operations, the need for more comprehensive data is even greater. Companies seek to make more confident decisions as they continue to work through existing system, operational and regulatory time constraints. Insurers are focused on continuously monitoring and synthesizing results given the perpetual flow of information now available.

Consumer shopping data has become a valuable addition to traditional insurance data sources for these very reasons. Insurers are desperate to understand factors driving sales and retention, and they want to make more informed decisions to avoid costly implementation mistakes.

KEY POINT

The most successful insurance companies have maintained a broad view of the industry and focused on creating additional segmentation and increased pricing accuracy.

A prime example is Vertafore Market Basket data. Vertafore's Personal Lines Rater is a national comparative rater that allows agents to concurrently quote personal lines policies in real-time from multiple carriers. Key data elements about the quotes, including quoted premium amounts and policy, driver, and vehicle characteristics are compiled into robust market basket datasets that can be used for analytics purposes. These data sets reflect real consumers shopping for insurance and the real pricing for the risk at that point in time.

Pinnacle and Vertafore are collaborating by engaging individual customers on custom projects, developing industry solutions and

producing cutting-edge research. The analysis of Vertafore's expansive insurance data set offers new insights into consumer behavior, industry trends and insurer competitive positioning. Pinnacle's and Vertafore's combined offerings will empower insurers to better monitor market position and make informed decisions.

Consumer shopping data can be used for a number of different applications such as:

1. Filling existing information gaps
2. Validating business decisions
3. Identifying shopping trends
4. Creating benchmarks and metrics

Filling Existing Information Gaps

Insurance companies face information gaps in various situations, such as entering a new state or product line or adding a new variable, discount or surcharge to their rating plan. By incorporating comparative rater data, insurers can overcome these information gaps.

Entering a new state is a challenge. Insurers have limited market information and only one opportunity to present an initial rate filing. If the rate level is incorrect or variable segmentation is not aligned with competitor offerings, then the insurer incurs significant opportunity costs in time delays, resources and market reputation while the rating plan is modified. Incorporating Vertafore Market Basket data allows the insurer to compare its proposed rating plan against competitors' rating plans. Using basic metrics such as low, high and median premium of quoted competitors, the competitive landscape can be visualized. These insights can help insurance companies develop a more competitive rate. Once the overall state rate level has been set, additional refinements can be made to key rating variables.

Further, with information about the consumers in the new state, the insurer is able to set realistic sales goals, develop benchmarks and create monitoring reports. By better understanding their competitive position, insurers will have increased confidence in their rating plans and be better able to work with agents to target profitable business.

Insurance carriers are also continuously working to refine and improve their own rating plans and keep pace with competitor rating plan innovations. A common business question is whether it is efficient and cost effective, or even necessary, to incorporate certain rating variables being used by competitors.

When an insurer is able to link the Vertafore aggregate quote data with its own data, this provides information to help answer these types of questions. An initial review can evaluate whether adverse selection is occurring, as well as the resulting impacts to the quality of the book, the conversion rate and the average rate level. This can then be expanded to include behavioral information about agent perception and reaction. A decreased number of actual quotes based on that particular variable may indicate that an agent is aware of the premium differentiation for that variable and has made the assumption of a lack of competitiveness.

Validating Business Decisions

Insurers are investing significant resources to develop more sophisticated rating plans with new variables and increased segmentation. Many of the new rating plans feature complex matrices with multiple correlated variables, which increases the challenge of understanding premium levels. Further, disruption is expected in the existing book of business with the implementation of these plans and it is essential for insurers to predict that disruption and adjust business plans.

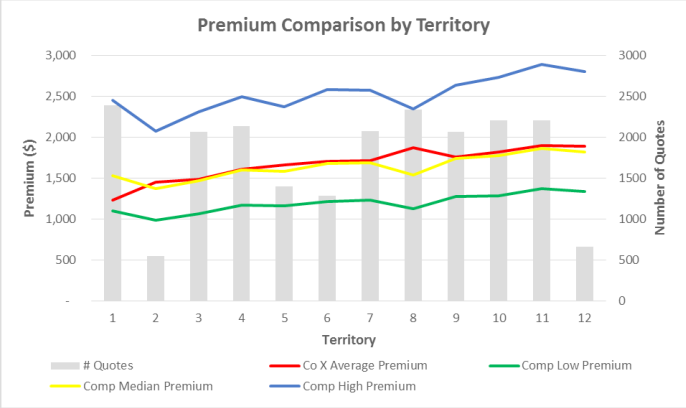
A standard impact analysis will compare the existing premium of each policy to the projected premium from the new rating plan. But an insurer can improve its knowledge base by adding competitive data. Opportunities exist when competitors are not yet using new variables, and weaknesses are mitigated by adding variables that are broadly used in the marketplace.

Insurers concurrently seek rate adequacy, battle competitive challenges and strive to align their programs with regulatory requirements. As rating plans are refined, the view of the competitive landscape provides additional insights on expected performance for retention and conversion. This information is extremely valuable when setting internal business goals related to conversion, retention, average rate levels and agent response.

In a specific example shown in **Exhibit 1**, a company observed noticeable levels of non-competitiveness in key regions, both higher and lower than competitor rates. A competitive analysis indicated that the

overall rate levels of the state were consistent with the median competitor rate levels. A more detailed review of the regions indicated a territory assignment issue at the zip code level rather than an overall rate level disconnect.

Exhibit 1



For most companies, a market view of territory competitiveness is common practice. In many cases, companies have a solution without fully understanding the problem of being "uncompetitive." The perception of competitive rates is biased by competitor choices and the amount of information and analysis used to make those choices. Traditional competitor analysis will compare the relative factor levels and a series of scenarios to evaluate whether quoted premiums are low enough to obtain new business, but these types of analyses usually do not capture the true competitive landscape.

When insurers have accurate pricing and segmentation, uncompetitive rates can be a symptom of business with higher expected loss costs or business that is not aligned with its core strategy. Territory analyses often highlight how insurers have selected different territory definitions based on loss costs, growth potential and marketing considerations.

The use of Vertafore's comparative rater data helps insurers understand the scope of the issue – i.e. overall statewide rate level versus specific territories – as well as its magnitude. The methodology first reviews the overall rate level, then the relative competitive level of each territory, and finally the range within a territory. If the insurance carrier identifies disconnects with the statewide rate level, the solution is different than if the carrier finds that specific territories have rates that are materially different than the competition.

Identifying Shopping Trends

Traditional target marketing methods have focused on identifying an "ideal" customer who is less prone to loss based on certain risk characteristics. Unfortunately, there is not always an abundance of these "ideal" customers in the shopping population. By reviewing characteristics of recent insurance quotes, an insurer will soon realize that these customers make up only a fraction of a percent, and will thus be forced to develop a more realistic view of the shopping population.

As an example, an insurer may describe an "ideal" homeowners risk as follows:

- Home/auto package policy
- $250,000-$350,000 Coverage A limit
- Home built in the last 15 years
- Roof less than 6 years of age
- No prior losses
- Located in Protection Class 1-4
- Insured age 30-50
- No youthful drivers
- Exceptional credit

In a sample of more than 330,000 quotes for Midwestern states, only 1,609 quotes (0.49%) met this definition of an "ideal" risk, and these risks accounted for less than $2 million of written premium (see Exhibits 2 and 3).

Exhibit 2

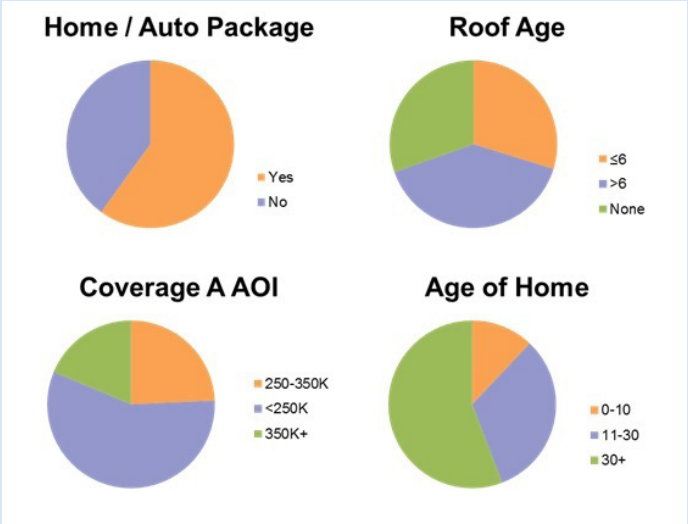
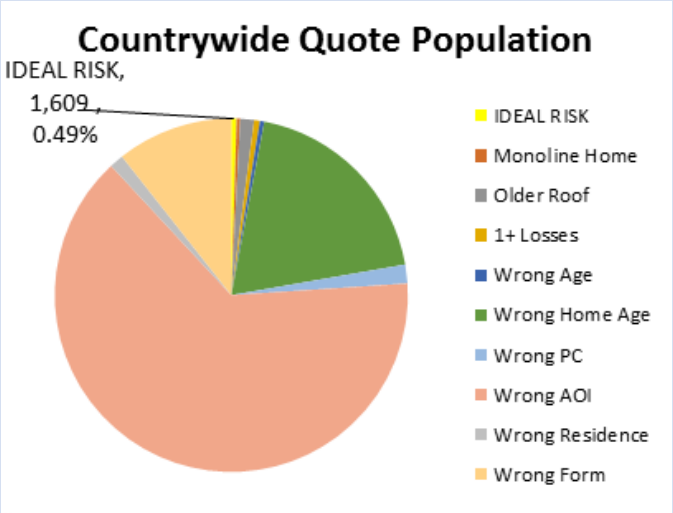


Exhibit 3



Less than 0.5% of all quotes are considered "ideal" risks by insurers.

To grow the business profitably, an insurance company must first understand the business that is available and how it is changing. Consumer shopping data can provide a meaningful overview of opportunities in a marketplace. Answering basic questions such as the average rate level, premium splits between coverages, number of total quotes, number of times being quoted and the range of premiums quoted provides a starting point for developing rating change proposals. This enables a company to prioritize and allocate resources to focus on the most prevalent issues.

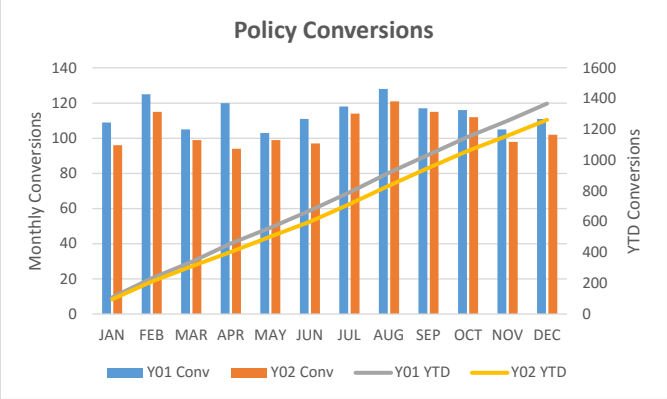
Consumer shopping behavior provides information beyond the policy characteristics and also provides insights about agent and competitor behavior. Insurance companies have traditionally interacted with agents via field personnel and gathered anecdotal information about competitiveness and the available quantity and quality of business. Vertafore's data allows insurers to determine the number of quotes issued, number of competitors quoted and hit ratios by agent. This information creates quantifiable metrics which can be used to evaluate the quality of business being converted.

Creating Benchmarks and Metrics

Insurance companies, like most companies, have growth and profitability goals. The measurement of those goals is often on a calendar year view to align with budgets and contingency plans. To actively manage business performance, insurers need to create dynamic business plans. An annual plan created in July of the prior calendar year may become obsolete or unattainable when rating plan changes are implemented.

Standard metrics such as retention and conversion can be monitored in a more meaningful way. For instance, a decrease in the absolute number of converted quotes may not be cause for alarm. With additional consumer shopping data, this metric can be better interpreted as a reduced number of total available quotes or a reduced number of available quotes in the insurer's core segments. The dissemination of this information across the organization can then influence an insurer's goals and plans.

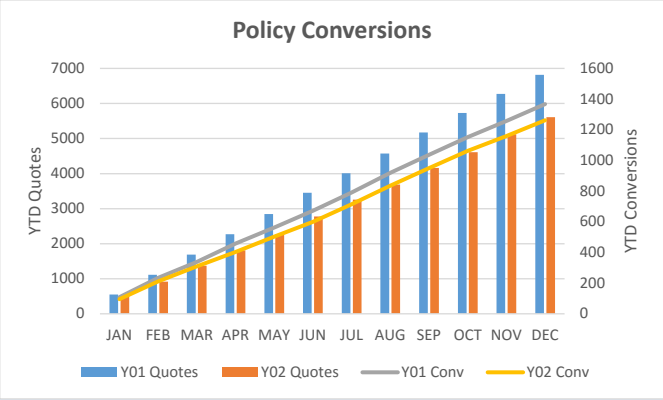
Exhibit 4



View 1 – Comparing Total number of conversions (Y01 vs Y02)

A more traditional view as seen in **Exhibit 4** focuses on the absolute number of converted quotes with the decrease signaling various problems including uncompetitiveness. By expanding and enhancing the metric as seen in **Exhibit 5**, an insurer more appropriately interprets the marketplace as a reduced

Exhibit 5



View 2 – Total policy conversions when considering available quotes. Y02 has 1,262 conversions vs 1,368 for Y01, but converts at 22.9% vs. 20.2%

number of shoppers. Further analysis can identify broad market trends in shopping behavior versus regional trends. The focus then becomes the quality of business available and adapting strategies to identify and convert key segments of the business.

Additionally, shifts in the population can be observed over time when an insurer monitors the market more broadly. When increased shopping is observed for a core segment of an insurer's book, an insurer has the option to create an actionable plan or to adjust the expected outcomes.

Conclusion

As insurers continue to seek competitive advantages to profitably grow their business, they will rely on innovative applications of data, analytics and metrics. Including competitive data and behavioral information will supplement traditional pricing, underwriting and marketing practices, and will allow the insurers to make more intuitive business decisions.

Traditionally, most companies have created plans and goals using historical information and then developed action plans to achieve those goals. With more information available today, the sequence is beginning to reverse such that insurers will be able to gather information related to the individual policy risks and create more accurate and insightful forecasts. This information can then be used to drive strategic plans related to growth, retention and profitability, and to create tactical plans and metrics.

The most successful insurance companies have maintained a broad view of the industry and focused on creating additional segmentation and increased pricing accuracy. Utilizing a perpetual flow of information related to the competitive landscape allows these companies to continuously monitor results and make strategic changes as needed. These adjustments are often related to the underwriting and marketing of the program rather than modifying the rates.

ABOUT PINNACLE

Pinnacle Actuarial Resources, Inc. is an independent, full-service actuarial firm that focuses on the property/casualty insurance industry. Our home office is located in Bloomington, Ill., with additional offices in Atlanta, Chicago, Des Moines, Indianapolis and San Francisco.

Our *Commitment Beyond Numbers* philosophy encompasses all of who we are and what we do. It drives us to do whatever it takes to help our clients address their risks, understand the challenges they face and find the right solutions to meet their goals.

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