Profit and Customer Outcomes – CORs & Effect
Thoughts on the FCA General Insurance Pricing Practices Review

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23 September 2019
Agenda

1. Introduction: FCA Market Study
2. The need for a review
3. Potential interventions
4. Stakeholder perspectives
5. CORs and Effects
6. Conclusion
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Introduction

FCA Market Study launched 31 October 2018

• “TR18/4: Pricing practices in the retail general insurance sector: Household insurance”
• Market study: How general insurance firms charge for home and motor insurance
• Citizens Advice super-complaint: long term customers overpaying
Introduction

Potential interventions and CORs and Effects on Stakeholders

• New vs. Renewal pricing is a key issue we need to address
• Mitigations create winners and losers
• There will be unintended consequences
Agenda

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Citizens Advice super-complaint

Price differentials exist – but customer behaviour plays a key role

1. People don’t have time to shop
2. Finding a good deal is a struggle
3. Vulnerable consumers unable to get the best deals
4. High cost of switching
5. Fear of things going wrong
What the FCA found in Home Insurance

**Figure 1: Policy count and average margins by number of renewals**

Source: FCA’s TR18/4 page 13
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Some Potential Interventions

**Supply Side**
- Tariffs
- Rate filing
- New business incentive has to be cashback
- Limit on renewal v new business price

**Demand Side**
- Improve renewal messaging
- No auto renewal
- Show difference between new business and renewal price
- Commission disclosure
- Price Comparison Websites quote all renewals, 1 click purchase
- Fixed policy length
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4. **Stakeholder perspectives**
5. CORs and Effects
6. Conclusion
Stakeholders – Split the room

Customer

Regulator

Insurer
Stakeholders

Customer
Give me great value
Treat me fairly
Don't make me complain

Regulator
Protect customers
"Easy" to supervise

Insurer
Make money
Happy customers
No regulatory censure
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Demand side: More transparency

**Appeal**

- Nobody can argue with better informing customers

  Except…

**Problems**

- Customers overwhelmed with information
- Renewal transparency impact minimal
- Different customers want different information
Demand side: Force customers to...

Shop every X years

Make active decisions at renewal

But does this really work?

Europe's small cars an endangered species
Supply side: Let’s try a little price control

Let’s create a model company

• ShoppersReward Ltd has exactly the same shape portfolio as the FCA observed in the Home study!
• They have played with some price control scenarios

Grotesquely simplifying assumptions

• Price interventions do not impact on new business volumes or retention rates
• Costs (other than acquisition costs) do not change with tenure
• Everyone at tenure 10 and beyond has same premium and margin
• ShoppersReward Ltd makes 6.9% margin on the portfolio and carries on trying to do so
## Pricing scenario: Base case

<table>
<thead>
<tr>
<th>Tenure</th>
<th>Count</th>
<th>Margin %</th>
<th>Ave Prem</th>
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<td>0.45</td>
<td>30%</td>
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<tr>
<td>10+</td>
<td>1.5</td>
<td>37%</td>
<td>£315</td>
</tr>
<tr>
<td>Total</td>
<td>12.0</td>
<td><strong>6.9%</strong></td>
<td></td>
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</table>

Premiums scaled to give a reasonable average

Loyal customers: 40% margin consistent with FCA findings

**23 September 2019**
## Pricing scenario: Renewal equals New Business

<table>
<thead>
<tr>
<th>Tenure</th>
<th>Base Case Ave Prem</th>
<th>Ren = NB Ave Prem</th>
<th>Difference</th>
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<td>6%</td>
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<td>3</td>
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<td>0%</td>
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<td>4</td>
<td>£ 276</td>
<td>£ 253</td>
<td>-8%</td>
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</tr>
<tr>
<td>10+</td>
<td>£ 315</td>
<td>£ 253</td>
<td>-20%</td>
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</tbody>
</table>

### Ren = NB vs Base Case

- **Book margin**: 6.9% vs 6.9%
- **Average premium**: £253 vs £253
- **NB price increase**: 22%
Pricing scenario: Max New Business discount: 33%

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<thead>
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<th>Base Case Ave Prem</th>
<th>Ren ≤ NB+50% Ave Prem</th>
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</tr>
<tr>
<td>5</td>
<td>£ 288</td>
<td>£ 272</td>
<td>-6%</td>
</tr>
<tr>
<td>6</td>
<td>£ 297</td>
<td>£ 286</td>
<td>-4%</td>
</tr>
<tr>
<td>7</td>
<td>£ 299</td>
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<td>£ 320</td>
<td>7%</td>
</tr>
<tr>
<td>10+</td>
<td>£ 315</td>
<td>£ 320</td>
<td>2%</td>
</tr>
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</table>

Assumes 5% pa increase until NB + 50%
Pricing Scenario: Enforced shopping every 3 years

<table>
<thead>
<tr>
<th>Tenure</th>
<th>Base Case Ave Prem</th>
<th>Shop every 3 yrs Ave Prem</th>
<th>Difference</th>
</tr>
</thead>
<tbody>
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<td>0</td>
<td>£ 207</td>
<td>£255</td>
<td>23%</td>
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<tr>
<td>1</td>
<td>£ 221</td>
<td>£281</td>
<td>27%</td>
</tr>
<tr>
<td>2</td>
<td>£ 239</td>
<td>£309</td>
<td>29%</td>
</tr>
</tbody>
</table>

Using 10% increases each year to reduce NB price!

<table>
<thead>
<tr>
<th>Forced Shopping</th>
<th>Base</th>
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</thead>
<tbody>
<tr>
<td>Book margin</td>
<td>6.9%</td>
</tr>
<tr>
<td>Average premium</td>
<td>£276</td>
</tr>
<tr>
<td>NB price increase</td>
<td>23%</td>
</tr>
</tbody>
</table>
Different customer flavours - The Robin Hood Effect
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Conclusion

• Balancing the outcome for all is challenging
• Unintended consequences will result from the best of intentions
• The answer (in part) will be politically driven
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