# (Re)Thinking Insurance Podcast Season 2, Episode 5: Middle East Special — Gaining competitive advantage in the GCC through pricing

SPEAKER 1: The winner's curse is an interesting concept. And that all came from sort of auction theory, that basically the winning bid at an auction tends to exceed the intrinsic value of the item that's up for sale. And it's a similar concept is that if you win in an insurance policy, then the chances are that you've probably charged too little for it.

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SPEAKER 2: You're listening to Rethinking Insurance, a podcast series from WTW, where we discuss the issues facing P&C, life, and composite insurers around the globe, as well as exploring the latest tools, techniques, and innovations that will help you rethink insurance.

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MATT FACEY: Hello, and welcome to another Special Middle East edition of Rethinking Insurance, our friendly podcast. I'm your host, Matt Facey. And today, I'm delighted to be joined by my guests, Andrew Davis, PPCU leader in the Middle East and Tim Rourke, our PPCU leader in the UK. That stands for Products, Pricing, Claims, and Underwriting. Andy and Tim are experts in our pricing sphere and have been on numerous client sites and on the client side until very recently when they joined us. So welcome to you both.

In today's episode, we're going to explore pricing relevance in the Middle East market and why the experiences of the UK pricing market is relevant to the GCC and how we can compare and help companies be more profitable and streamlined with their pricing processes. And we're going to aim to show how pricing is not complex and how it has wide reaching implications for insurers, peoples, processes, systems, and data. At the same time, it represents an unparalleled opportunity to drive automation and innovation that will deliver systems and processes with proper levels of oversight and governance.

But before we get into the discussion on pricing, I just want to find a little bit more about our guests today. So let's start with you, Andy. So could you possibly tell me what your favorite film is or your favorite book?
ANDREW DAVIS: Yeah, it's a film, not a book. I must admit it, it's the film that I've been more interested in the book. And this is quite a set answer coming from someone in my job. But I'm a huge fan of the film,

Moneyball, and the whole concept of that sabermetrics, which is, given my job, is trying to do statistical analysis to gain advantage that that is what a lot of pricing is.
It does seem like a bit of a unimaginative answer. But I just find the whole thing fascinating. It's entering a new field that's never been thought about before and applying these methodologies in a way that just delivers value in a way that no one ever thought possible before. I just think that whole transformation of things is amazing.

MATT FACEY: I think in terms of diagrams with actuarial consultant and actuarial related films, that's going to be quite high a Venn diagram of crossover. So the same question to you, Tim. What's your favorite film or books? We can get a little insight into who you are.

TIM ROURKE: Well, again, my choice was a book and was turned into a film. So it's The Martian, actually, by Andy Weir. So unlike Andy, my dream was to be an astronaut rather than an actuary. But you know, unfortunately, I've gone to the other side of the spectrum. So yeah, just a brilliant book, well-researched, a real page-turned. I love science fiction, so that book ticked all the boxes for me.

MATT FACEY: You two didn't get very far down the career book, did you? You started both A's and become an actor or astronaut. Didn't go on to B or anything. But that's good. That's all good.

TIM ROURKE: There always is that term that no one ever chooses to go in insurance. You always fall into it. Whether that's the case anymore, I don't know. But it probably was slightly the case for me when I joined 20 years ago.

MATT FACEY: Yeah. Cool, that's brilliant. So thanks both for that. What we're going to do now is just get into today's discussions. So given the exposure that we've had with many of our GCC clients across the region, with regards to pricing, the first question I guess to you, Tim, is where have we seen ways in which the UK market can mirror what we have seen in the fledgling steps that some of the GCC insurers have taken? And how we can use that knowledge to help the GCC insurers.

ANDREW DAVIS: Yeah. Thanks, Matt. It's a good question. And actually, it's one of the reasons why I'm personally so excited to be working with insurers in the GCC, because I do feel that, based on my experience working in the motor industry for a long time, there are lots of similarities to what I've seen in the UK and what I perceive could be the case for GCC countries in the future with regards to motor insurance. And that relates to the nature of the distribution of insurance. It relates to the appetite that insurers have around data and analytics and how that can drive better decision making.

And one of the things that I feel is very exciting is the ability for WTW to help clients in the GCC to propagate that kind of data and analytical journey so that they are ahead of the market and all the benefits that we've seen of organizations within the UK that have used analytics, that have got their data in an excellent position, they are really benefiting from what has turned into an extremely competitive market. And when you consider distribution channels like price comparison websites and aggregators and what you need to do to be successful in trading via those mediums, the importance of analytics and pricing and good underwriting has never become more important. And you know, my aim, really, with our [INAUDIBLE] is to support insurers in that journey to help them avoid the bear traps that many of our UK insurers had to sort of deal with and heal from, so that you can have kind of success.

And it's also very clear to me as well that the people that invested in technology and data and analytics in the UK market have historically been the more successful in the longer term. And I feel that when we go out, when we've been out to the GCC and talked to insurers, there is a real appetite for that type of work. And it's really exciting. And today, really, is about us working with those insurers, with those clients, to help them kind of achieve their aspirations. So for me, that's a really interesting and exciting reason why we see this market as one with such potential. And Andy and I are very excited to support clients in this kind of area.

MATT FACEY: I completely agree with you. Every time we go out, the appetite for people out there, actuaries or actuarial consultants or training actuaries or underwriters, it is huge. And they just want to benefit from, like you say, the potholes that the UK insurers have fallen into over many years.
And in terms of the hierarchy of where companies are and how they do pricing, you can have very simple pricing models all the way up to very complex price optimization models. So could you just give us a quick overview of how you see that kind of spectrum, that ladder or that hierarchical pyramid go in from what some insurers are doing at the minute, all the way up to what is the art of possible?

ANDREW DAVIS: Yeah, absolutely. And I think it's very much a spectrum. It's almost a multidimensional spectrum, because so much of what we do in pricing is just really about getting that insight and understanding the drivers of what happens. So at the most basic level, almost, of pricing, you might have some sort of very broad brush and wide banded groups, a couple of factors, say, look, these, on average, these policies and average costs is a bit more than these policies do.

So we'll charge them a bit more money. And that really is how pricings start, how pricing as this concept has started. It's trying to find where you-- what areas that cost you more money and the areas that cost you less. And a lot from there is, effectively, it's improvements upon that theme. So you start off in that sort of place.

And then you can then build more complex analysis and insights into that. So you can start to split out. So rather than saying people in their 20s cost us this much. People in their 30s costs us this much. People in their 40s cost us this much. You can start to draw curves that have things at different ages.
And that's a generation of understanding, better understanding of risk. You can also then start to look out and say, well actually, different types of claims cost me different types of-- different amounts of money. By doing that, that again, is another sort of abstract-ification out of what you're doing.

And you start to then build up a really, really neat view of what's going on in the world of your claims costs. And you can build those out and do simple or complex modeling forms. And that's one piece we find that there's been, the real start of the pricing revolution in a lot of places.

The other things that we look at, that is, OK, there's a bit more to it, though, than just how much claims are being paid out. As you change your price, you're more or less likely to sell a piece of business. So fundamentally speaking, if you put your prices up, you're going to be less competitive, which means you're going to probably sell fewer policies.

Similarly, if you put your prices down, you're going to sell some more policies, because you'll be more competitive. Now, understanding how that gearing works is another really fundamental key piece in terms building out what you're doing. So that's another piece of the hierarchy of saying, well OK, let's get some understandings of those retail, those commercial drivers of what's going on.

And we can use that then to understand, well, if I put my prices down by a certain amount, my loss ratios are in a different position. This is how much I can afford to cut prices by and still be in a profitable position and maximize my growth of the books. That's sort of where you get to the next stage, this idea of risk price with a retail layer on top of it.

And then what we can do is we can supercharge all this. And actually, rather than trying to do a whole portfolio level, we can try and do this using mathematical optimization approach, where we plug all this in and we say, OK, well, that means for each row of our business, subjects, the things we care about, the size of the business we want, how much we want to limit our movements in terms of prices. What price charge for each individual customer? And when we get to that stage, you have a really good understanding of how much they're likely to cost us and how likely they are to convert or renew at each price level.

And that means we can pick the price you want to charge for each customer in a way that's going to generate us the best amount of profit, because fundamentally, pricing is actually quite a simple state game. What we're trying to do is we are trying to make sure that we are selling as much business as possible at a price that is more than it's going to cost us to generate the total inaggregate profits in what we're doing. And from that, that allows us to invest in the growth of our business. Because often when we do that, as we grow, we can invest in reducing our costs. And we end up in this really nice virtuous circle of growing.

So for a lot of-- sometimes we can approach pricing, you can start approaching pricing very much driving down risk cost approach. But really, the end of this, very often, is using that risk cost, that profitability generation, to reinvest into growth, into basically becoming a larger and more successful insurer.

MATT FACEY: And those all, I completely get it from the start to the endpoint here. Is there any downside or negative points of just doing the simple pricing approach? Because some insurers may not have the appetite or the data to go from that stage all the way up, at the minute. But as far as I've seen it in pricing, it's about getting the right price and the in-depth insight into your portfolio as well. So could you just talk a little bit about the positives and the negatives of doing simple modeling?

ANDREW DAVIS: Yeah, absolutely. I mean, doing the simple modeling side of things is-- as other people move on to also doing simple modeling or more advanced techniques, it becomes almost a necessity, because you need to, as we said, you need to understand what's going on in your portfolio. And if you're not doing that, there's lots of things going on in the world of your policyholders, your customers, that you just don't understand.

And particularly if you're on [INAUDIBLE] distribution world, there's a big risk of what's known as the winner's curse, because if everyone's up there and getting their prices that are being able to be compared, then you're only going to be winning and writing policies in the areas where you've underpriced, because if for the better, cheaper-to-do insurers, people are going to be undercutting you and winning the business. And you're going to just be left on the ones where they think there's something wrong with it. So making sure, just those simple models are working, is an absolute necessity to make sure that you're still in the game, you're still able to be making, be successful, make the sales and return some level of profitability.

Now actually, as all these, as you go into these more complex pieces, they're add on, they're improvements, they're sort of steps ahead. But the biggest benefits, as with all improvements, all journeys, the biggest benefit is usually from that very first step. That's where you can get, if you go from a position not a lot, to just getting these more fairly simple risk models in, that's a piece that really adds that huge amount of benefit.

And then the other bits are then effectively jockeying for position and trying to move a little bit ahead and just put your nose out front to allow you to move from being a mid-tier insurer to a cutting edge one. And you know, and again, a lot of this is about developing out your understanding. So it can be a case of still doing the simple risk models, but doing them with ever-increasing, ever-improving data assets. And that's when the pieces just really trying to drive forward and improve your data assets to improve your simple risk models can sometimes actually provide as much value as moving on to some of the later stages with a not-as-good underlying data set.

TIM ROURKE: Yeah, I think that's a really good point actually, Andy, that a lot of the analytics that the more sophisticated insurers do, and as you say, it is about really understanding that risk, that's all underpinned by excellent data. And a lot of organizations need to think about what they need to collect in the future so that they can be that cutting edge and they can do that great pricing and analytical work when the data doesn't necessarily exist. So I think it's not to be underestimated, the importance of planning your data strategy so that you collect the right information so that you can be as sophisticated and as analytical as you would like in the future. But you're going to have to wait some time while you collect that data to kind of facilitate that kind of work.

MATT FACEY: What I'm hearing from you is that it's, to be the cutting edge insurer with regards to pricing, it can be some simple steps or it can be some big, giant strides. But it sounds like the true cause of the different performance can be hard to tease out. So you talk about that a little bit more and how you

would tease out those differences. So is it a low NCT? Or is it a vehicle problem or another related aspect?
And also, could you talk about the winner's curse as well and the aggregators? Because those are two big things that are impacting the GCC markets. So Andy, do you want to take the first one on how to tease out some of the different performances?

ANDREW DAVIS: Yeah, absolutely. So at the most basic level, you can have a look at the performance of your portfolio and see where it's making you a profit and where it's making you a loss. And simplistically speaking, you probably want to put your prices up where you're making a loss and put your prices down where you're making a profit to make sure things are being levelled out.

And that, again, sort of building on this, that's the simplistic. And we can make it more complex from there, approach. That's almost a starting point. But then as you look at things in a single dimension at a time, look at those drivers, well, exactly as you said, Matt, low NCD might be a problem. But also, younger and newer drivers are going to have low NCD.

So there's a question there. Which one is it? Is it my NCD, or is it my age? Or is it-- it could be certain areas of the country. What sort of things are driving those differentials in performance.
And so one of the ways we do that is using statistical modelling format. So one of the ones that's been very popular in the UK for a while is generalized linear models. And the beauty of them is it means that you're accounting for where there are multiple explaining factors for why things are different.
You can account for them within each of the potential explaining factors to an appropriate degree. And it avoids the problem that you sometimes get, where you do the more sort of initial simpler analysis of double counting things. So you've got double discounting or double loading.

And it means that you can get some really nice views of that. And building these up, now, that is what our software does with emblem and being able to visualize it and deploy it through radar and radar live. So that's one of the things that we really work with people on is using this software to produce in quick time, and also in a very deployable format, ways of turning these insights into new prices.

And the nice thing about GLMs that a lot of people like is that they feel quite familiar when they come out. They are, effectively, some lookup tables based on individual factors. And you have different sets of lookup tables for each element of the thing you're modeling, so each type of claim, for example. And you can then amalgamate all them together into what can be quite a large and complex algorithm.
But each of the individual moving parts is quite easy to fathom. And bringing all that together, that's how we really can make that happen. Similarly then, talking back to the data point, is being able to drive more differentiation. So I talked about the age journey. There's also an area journey.

One of the things we saw in the UK is that we start off with very regional rating, 30, 40 years ago, moving now towards town-based rating. Whereas, now we have rating based on individual postcodes, which in the UK, is like as little as 15 households. And we use attributes of the factors of information that are within

an area, say different areas from different parts of the country are actually similar performance, grouping them together.
And that gives us some really quite neat and very, very powerful ways of bringing in a much more granular view of area rating. What we see in the Middle East is it's a very regional or maybe city-based ratings. So no matter where you are in, say, Riyadh, Dubai, Muscat, Manama, you'll end up with the same area price. And by improving that data and improving that splits, you can start narrowing that down to actually different pricing by neighbourhood, because different people in different neighbourhoods will have different underlying risks.

MATT FACEY: And when utilizing software and technology and data driven analytics to help with the GLMs, Tim, I guess this one to you, how is that used? And how can we utilize and help with aggregators in the market? How can we help companies avoid that winner's curse that Andy was talking about?

TIM ROURKE: Yeah. So it's a good question, Matt. And I mean, it's fair to say that even in the UK market, we still advise lots and lots of insurers about pricing on aggregators and how difficult that is. I mean, winner's curse is an interesting concept. And that all came from sort of auction theory that, basically, the winning bid in an auction tends to exceed the intrinsic value of the item that's up for sale.

And it's a similar concept is that if you win an insurance policy, then the chances are that you've probably charged too little for it. And all of that is driven by uncertainty about what is the intrinsic value, emotion, the types of bidders, and lots of subjective factors. So what insurers have tried to do is to remove that uncertainty.

And this is what Andy and I have been talking about. It is around utilization of data. It's about understanding the risk as best as you possibly can. It's about, not only understanding what you need to charge to cover claims, there's also this kind of behavioural aspect and how price optimization can help you in that sense.

And I think what the technology does, Matt, to answer your question, is that GLMs and robust pricing and underwriting technology allow you to kind of understand an individual, an applicant, more easily in a controlled sense that allows you to implement those refined prices and those underwriting rules so that you do understand the premium that you're charging, you do understand which policies are going to make you money, and you can continually refine that as the market changes. Because one of the very things about price comparison websites and aggregators is they do make the market much more dynamic and much more fluid. And therefore, you need to be able to adapt. And the concept of the actuarial control cycle and being able to kind of loop through these processes is really important.

And I think good technology that's easy to use, visual, allows you to refine it quickly. And again, to deploy all of the excellent work that you've been doing in the modeling is critical. And GLMs are a very good way to support that. And obviously, we are starting to see other methods coming as well.

But yeah, technology and deployment of all of this modeling cannot be underestimated. And you can have the best, you can have massive teams of statisticians and actuaries working for you. But if you can't actually utilize what you've worked on, then you're not really getting the benefit of all that investment.

MATT FACEY: Just in the interest of time, what I want to do is ask both of you your top three ways that Middle East insurers in the GCC can come to building pricing strategies for the future. So what can companies do? Just three things from both of you. So Andy, I'll go to you first. So what three things do you think the Middle East insurers can do to help build in better pricing strategies for the future?

ANDREW DAVIS: Yeah, I think the three things are understand your portfolio profitability. Understand the risk cost of each policy that you're writing. And I think the one that is really a great opportunity is understand how the place where the person you're insuring lives at quite a granular level, affects all those things.

MATT FACEY: Tim, same question to you.

TIM ROURKE: Yeah, I think mine are quite complementary to Andy, actually. So I agree with Andy on those three points. The other thing for me is, understand your market very well and the distribution channels that you have to work within.

I think a good understanding of those channels is critical for success. If you don't understand them, if you don't give them sufficient respect and sufficient time, then they can cause you issues. And great portfolio management and the ability to be dynamic and agile with your pricing to allow for the fact that these markets are dynamic, and things will change. And you just need to make sure that your pricing and your systems and your processes have the cadence that will allow you to be successful in those markets and you're not slow to react. Those, to me, are critical things that need to be borne in mind when you're trading in high velocity lines, like motor.

MATT FACEY: And to ramp up the podcast, really, just one final question. And it is born out of a conversation the three of us had with a client very recently about future proofing and what they can do to get ahead of the game, to get ahead of their competitors. And you both mentioned about data and having the building blocks in place for, not the next three or six months time, but 12, 18 months time, to get the data in place.

What, one thing from both of you, do you think insurers in the Middle East should be doing or take away from this podcast in order to help with their pricing in the future? Andy, I'll come to you first again, if that's all right.

ANDREW DAVIS: Yeah, absolutely. I think it's the-- thinking a little bit more about the behavior, the likelihood to purchase a policy. It seems to be something that isn't really considered that much. Things are very much cost-driven, in terms of their pricing, which is the paying out. Understanding the likelihood of getting the money in, it just feels like the real sort of getting your nose ahead of the game and really big, big game changing ways, the whole concept of retail pricing as we call it in the UK.

MATT FACEY: Tim. Tim, same question to you.

TIM ROURKE: Yeah, I feel that, given how intrinsic good pricing, good underwriting, good portfolio management is for insurance companies to thrive and be successful is to, again, make sure that you've got the things that underpin that, so a great strategy on data, good systems that can collect the data and make the data available, so essentially, a good data strategy, and not to leave things, to have some element of a pricing strategy as well, which goes from anything from what you need to cover to deal with inflation and the high level costs to understanding selective very kind of refined pricing changes. And make sure that there is a strategy around that so that what you're doing and you build all of these systems and you build the teams and you build the capability to allow you to achieve those things.

And I think coordination and orchestration of the support functions around good pricing and underwriting is critical. And if you don't have that, you can have all the brilliant, the best sort of actors and statisticians. But if they haven't got the tools to work with and to implement these changes, it can be very frustrating. And you just don't get the benefit that you could do.

ANDREW DAVIS: I suppose, Tim, on the back of that, its those decisions being made. It risks sounding boring, but it's really very important, that those governance cycles-- or maybe a better way of phrasing is that the really good decision making process cycles to make sure, actually, you can test yourself and say, am I making a decision that's going to improve my situation? Rather than it being a bit of guesswork.

TIM ROURKE: Absolutely. Pricing is complicated. And even though I agree with Andy, there are lots of things that you can do that get you a long way up that kind of ladder. Pricing is complicated. And it does need, without again sounding boring, it does need good governance. It needs good planning.
It needs all of those support things need to be in order. And if you do that, then it creates a culture of excellence in the pricing and underwriting space. And we know what impacts that can have in terms of returns and profitability. It's a tried and tested model.

MATT FACEY: Thank you so much, both. I know we could carry on talking for many hours on this. But I've got to go off and download The Winner's Curse off the internet somewhere and start reading it. It's been so insightful.

And I really appreciate both of your time. So thank you very much. And we look forward to the next Rethinking Insurance podcast. Thanks both.

TIM ROURKE: Thanks very much, Matt.

ANDREW DAVIS: Thanks, Matt.

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