PICKING THE RIGHT BATTLE: LESSONS FROM THE GENDER DEBATE IN MOTOR INSURANCE

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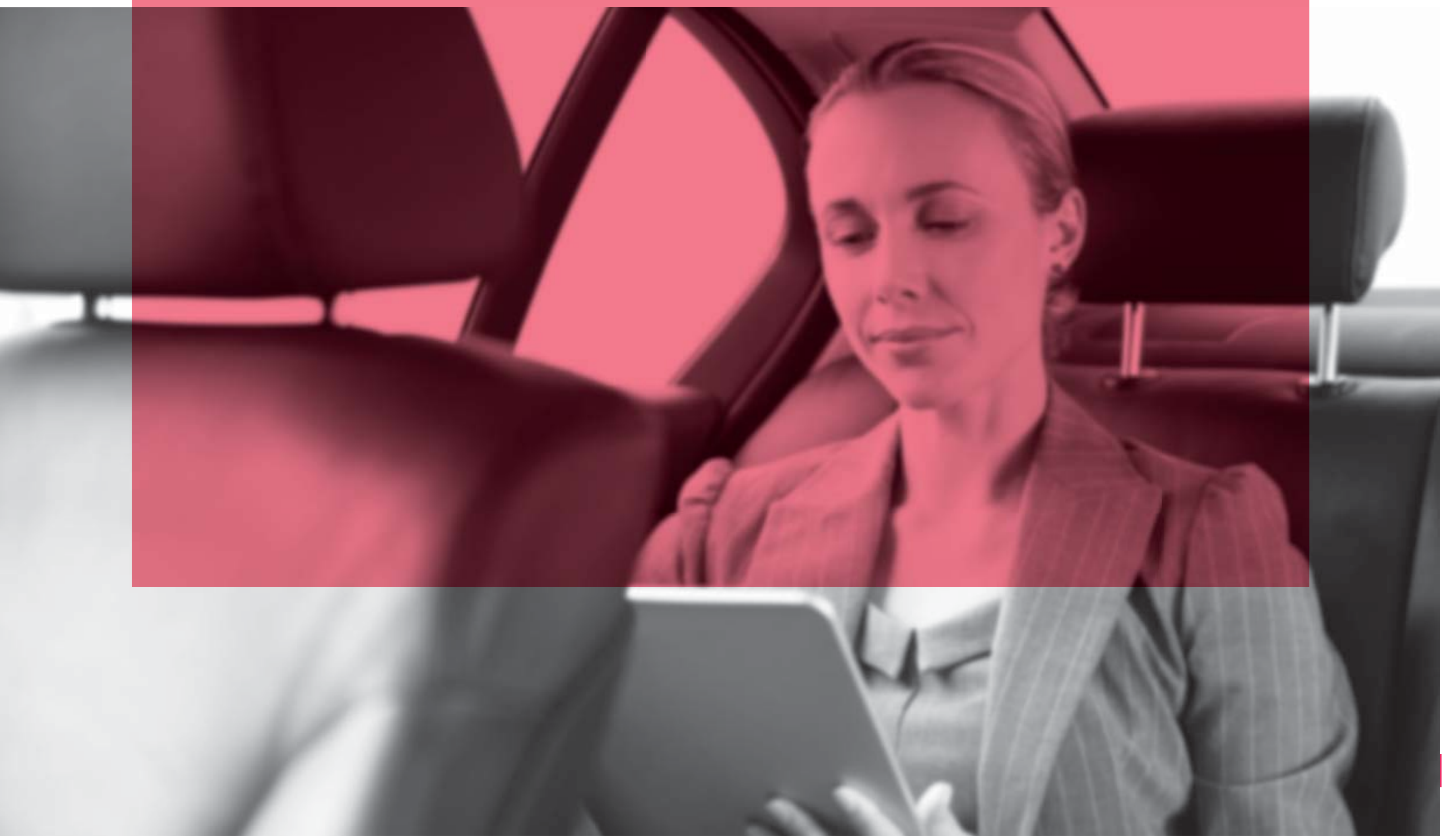


In 2011 the EU surprised many in the insurance industry by severely restricting the use of gender in insurance rating models. Insurers were forced to revise their pricing and sales practices in motor, life and pensions.

The effect was most pronounced in motor, where gender had been such an important risk factor in pricing and underwriting that some firms had built brands around it, such as Sheila's Wheels and Diamond in the UK and 1st for Women in Australia. The ruling triggered shock and considerable resistance – some of the more intemperate reactions describing it as statistically illiterate.

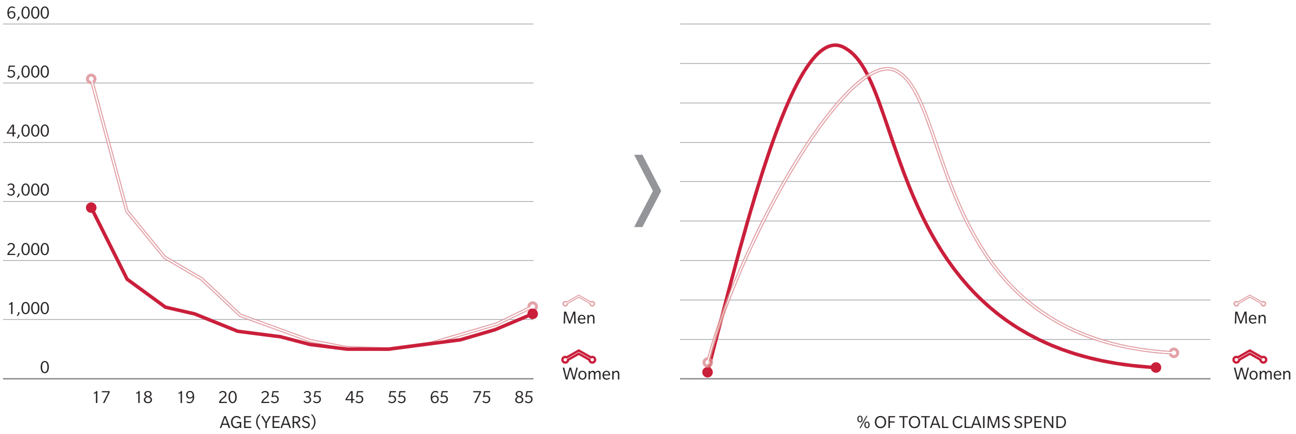
This accusation contained a grain of truth but it also missed the real point.

Motor insurers are in the business of predicting behavior – specifically, the driving behavior that causes damage. Like some other socio-demographic categorizations, gender is a predictor of driving behavior. Women are generally safer drivers than men. If you knew nothing else about an individual, gender would help you predict for the expected frequency of claims, particularly for young drivers. But it is an imperfect predictor. The spread within the gender groups still exceeds the difference between the averages of the groups.

EXHIBIT 1: DIFFERENT AVERAGE OUTCOMES CAN CONCEAL A BIG SPREAD

ESTIMATED AVERAGE PREMIUM BY GENDER (ABI 2011)

FREQUENCY OF TOTAL CLAIMS OUTCOME BY SIZE OF CLAIM (STYLISED)



It is a sign of how little insurers have historically known about their customers that they have relied so heavily on relatively crude proxies such as age, job and gender for predicting behavior. As better data and analysis become available, the importance of these old risk factors is waning. Insurers have already discovered better predictors for behavior. For example, it turns out that credit scores can help to predict behavior unrelated to borrowing. How people manage a credit line is a very good predictor of how they will drive or manage their household security. Indeed, when rescoring models in the light of the new data and modelling environment, one of our clients found that (adjusting for other factors) gender dropped a long way down the list of most significant factors.

"Risk technology" is also developing rapidly. For example, telematics allows insurers to observe customers' actual driving behavior – most importantly, the speed they drive and the rates at which they accelerate and brake (which can also be linked to driving conditions and location). If this technology comes into widespread use, insurers will no longer have to rely on predictors of driving behavior, and hence proxies such as gender will become increasingly irrelevant.

Organizations thinking about issues of gender diversity can learn from this episode in Insurance.

Initiatives aimed at increasing gender diversity in the workplace have triggered significant controversy and resistance in some quarters. Changes to recruitment procedures to encourage female applicants, gender targets and quotas for Board composition, changes to career progression expectations aimed at not disadvantaging women who choose to have children, or changes to working practices aimed at accommodating staff with family commitments (of which women still bear a greater share than men): all have attracted complaints about undermining meritocracy or being costly distractions from getting on with business.

We believe these complaints also miss the point. In the business of recruitment and retention, companies are interested in finding and keeping the widest possible pool of suitably talented staff. But it is not easy to "see through" to the underlying level of talent of prospective recruits, nor to know whether today's pool of talent in the firm is as good as it could be.

In the absence of a perfect metric of talent (or a technology-based fix as in motor insurance), firms must instead rely on predictors. We believe that a firm's ability to maintain gender diversity at all levels is exactly this: a key indicator for whether the firm is doing enough to recruit and keep a broad spectrum of talent of all types (not only women). A firm that can do better at finding and keeping talented women will become a more attractive workplace for its entire staff.

Organizations that work out how to avoid recruiting only "people like us", and avoid inadvertently selecting against women, will be better places to work and will have access to better talent. They will be more open to new ideas; they will expand the range of ways to be productive beyond the old template of "9 to 5 at a desk"; and they will not promote people only on the basis of their willingness to work 100 hour weeks. These firms will have a broader mix of talented and motivated staff, both male and female. Study after study has demonstrated this supports business performance, and will be increasingly important in the future.

In summary, in motor insurance gender has historically had some value as a scoring factor but only as a predictor of actual driving behavior. Despite some adjustment costs, the industry is now moving towards measuring this behavior directly, supported by new technology.

Unfortunately, in the business of recruiting and retaining high quality talent, there is no such technology based "quick fix". So predictors are still useful when building a firm's workforce. Gender diversity is a predictor of an effective workforce. Companies with little gender diversity should not be worried about gender per se. They should be worried because a lack of diversity is a strong indicator that they are failing to select, nurture and promote the best available talent – of any gender.