McKinsey&Company

Financial Services Practice

Winning Share and Customer Loyalty in Auto Insurance

Insights from McKinsey's 2012 Auto Insurance Customer Insights Research

McKinsey&Company

Winning Share and Customer Loyalty in Auto Insurance

Insights from McKinsey's 2012 Auto Insurance Customer Insights Research

Contents

Introduction

The $175 billion U.S. auto insurance industry[1] could be spending its marketing dollars in more effective ways: targeting consumers based on needs rather than behavior; finding the optimal balance between retention and acquisition; and reaching shoppers with the right message at the right moment in their decision journey. These are among the insights from recent McKinsey auto insurance research surveying more than 16,500 consumers on both their shopping behavior and the needs that drive their decisions. The unprecedented scope of this research allows us to examine whether assumptions about how consumers choose an auto insurance policy really hold water. Insights from McKinsey's research include the following:

- The "window" for influencing auto insurance shoppers is open for longer than ever, increasing marketing options for carriers. Conventional wisdom based on the marketing "funnel" has long stated that, for carriers, being a part of the initial consideration set is all-important – their one big chance with insurance shoppers. However, this is not necessarily the case. As they move from gathering information through the quote and purchase phases of their journey (and beyond to post-purchase support), auto insurance shoppers

[1] Direct written premiums, 2012

are more open than ever to considering new brands and dropping considered brands at each step. This news is particularly relevant for carriers that have neither the resources nor the appetite to match the marketing spend of the leading brands and secure a place in the initial consideration set. Furthermore, the McKinsey research reveals that the capabilities and tools required to reach shoppers differ at each phase of the consumer journey, and for each segment of the shopping population. Carriers that can target these segments accurately will unlock a new way to win.

- Channel distinctions are blurring. We know that auto insurance shopping is a multichannel experience (see *The Multichannel Imperative for Property and Casualty Carriers in Personal Lines,* McKinsey & Company, March 2011); but the degree to which shoppers are switching channels – even during the same step in the decision journey – points to a significant opportunity. Carriers that can deliver a seamless cross-channel experience throughout the consumer decision journey will have a distinct advantage.
- There's more than one kind of loyalty. McKinsey research shows that loyal policyholders are not a monolithic group of satisfied customers; a subset of loyalists *do* fit this description, but another subset are identified by the survey as "loyal" in name only. That is, they remain with their carrier more out of inertia than out of satisfaction. Members of this significant minority of "passive" loyalists can, however, be dislodged and represent significant value hiding in plain sight.
- Consumer needs trump demographics and behavioral attributes for segmenting the market. Consumer *behaviors* may shed light on where opportunities exist, but *needs* provide richer insights into what it takes to actually win share. While the need for a strong brand is the most potent differentiator of consumer segments, other important factors include the propensity to shop, preference for a personal relationship and access to a local agent. Low price, it turns out, is a more modest differentiator.
- There are at least nine distinct auto insurance consumer segments. The marketing messages that resonate with each segment vary significantly. Furthermore, the most effective "touch point" or media vehicle for reaching shoppers varies by segment and by stage in the decision journey. To maximize marketing impact, carriers must consider *what* to say to target consumers, *how* to say it, *where* to say it, and *when* to say it.

In the following chapters, we examine the data underlying these trends and insights, and conclude with implications and questions for senior management at U.S. auto insurance carriers.

Insights on Shopping and Switching

According to the McKinsey research, annualized shopping and switching rates have declined to their lowest levels since 2008. Twenty-seven percent of consumers shopped for a new carrier in the prior 12 months (down from 33 percent in 2011), representing $45 billion in direct written premiums (DWP); one-third of the shoppers (9 percent) ultimately switched (down from 13 percent in 2011), representing $13 billion in premium movement.

The most common triggers[2] for shopping were price increases (48 percent), life events such as moving to a new state or changing jobs (44 percent) and new coverage needs (32 percent).

- The frequency of pricing as a trigger is unchanged since 2008, while life changes and new coverage needs are now more frequently cited.
- Some shopping triggers were more likely to drive switching (e.g., poor claims service and new coverage needs) than others (e.g., advertising).

Bundling an auto policy with another type of policy generally improved retention. For instance, the 49 percent of auto policies that were bundled with a

[2] Non-cumulative; multiple triggers may apply

homeowners policy enjoyed more significant benefit, as shopping and switching rates almost halved. By contrast, bundling an auto policy with a renters policy produced negligible retention benefits.

Tenure – the length of time a consumer has been with a given carrier – correlates with shopping and switching behavior. Those with tenure of less than a year are twice as likely to shop as consumers of any other tenure, and account for 31 percent of shoppers. Similarly, 58 percent of switchers were with their carrier for less than four years. These statistics highlight significant churn and underscore the need for carriers to better assess the economic value of retaining different consumer segments over time.

The New Auto Insurance Shopping Journey

Auto insurance consumers that decide to shop move through a journey that involves gathering information, quoting and purchasing (Exhibit 1). Consumers then remain in a loyalty loop until a triggering event thrusts them back into the shopping loop. This journey has become less linear as consumers add and drop brands from their consideration set at different points along the way.

Consumers display distinct channel preferences through their behavior at each stage of the journey, highlighting how the "agent versus direct" paradigm has evolved into a multichannel model. Consumers no longer stick to a preferred channel from start to finish. Many start direct and then purchase with an agent. Some shoppers even use multiple channels during the same stage; for instance, they get quotes from both agents and from the Web.

A map of aggregate consumer journeys (Exhibit 2, page 8) displays this complex reality, highlighting the frequent shifts from one channel to another. Data highlights include the following:

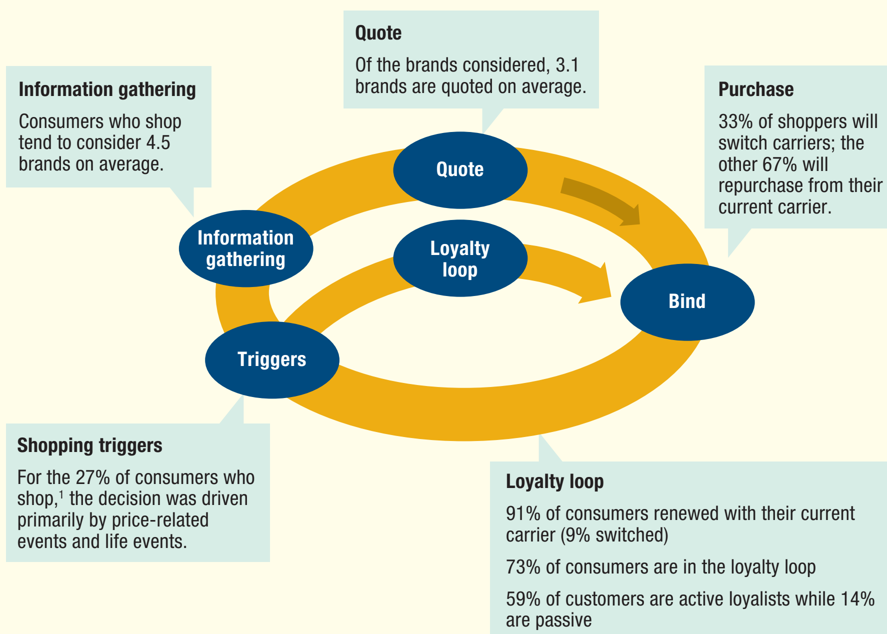
- The majority of shoppers gathered information and quotes using direct channels. More than 80 percent used direct channels to gather information, including 23 percent who gathered information via both direct and agent. The Internet was the most common direct channel for gathering information (with 73 percent of shoppers using it, up from 55 percent in 2008). The remainder used call centers either as a standalone source of information or in combination with the Internet. Finally, 70 percent ultimately quoted direct, including 20 percent who quoted using both channels.

- At purchase and beyond, the majority of shoppers preferred to speak with an agent. Sixty percent used agency channels to ultimately bind coverage. And 60 percent used direct channels for post-purchase support, though over 75 percent spoke with a person (either agent or call center), highlighting the importance of the personal touch during this stage of the journey.

The three most common auto shopping journeys represent 57 percent of all shopping experiences: *all direct, direct info gathering and quote/bind via agent* and *all agent*. The first – all direct – accounts for the largest group (30 percent) of shoppers.

Exhibit 1

Overview of the consumer journey in auto insurance



[1] "Shopping" is defined as considering carriers other than the current one

Source: 2012 McKinsey Auto Insurance Customer Insights Research

The research on auto shopping behavior also revealed insights relevant to the specific stages of the consumer decision journey:

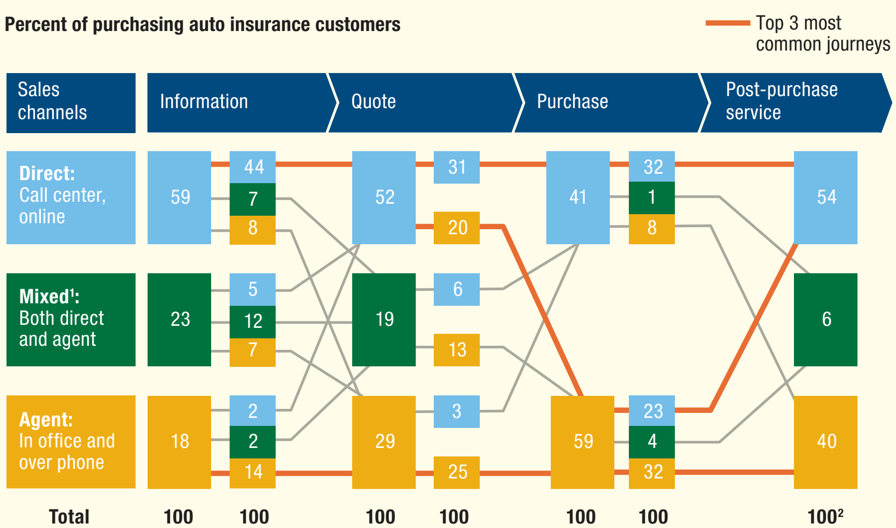
Information gathering

- The average shopper considered 4.5 carrier brands during their evaluation, with one brand added later in the evaluation process, highlighting an increasingly non-linear consumer journey.
- For the general population, the three drivers of brand perception associated most highly with success in consideration directly relate to advertising (i.e., "advertising is memorable," "makes consumers want to do business with the carrier," and is "humorous"). It is thus not surprising that the brands with the largest marketing spend enjoy the strongest consideration. In fact, the top four brands (GEICO, Progressive, Allstate, State Farm) capture more than half of all consideration.
- Shoppers gathered an average of 3.1 quotes, with a range of 2.6 to 3.7 depending on channel selection. For example, those who only went to agents in person gathered 2.6 quotes on average, while those who used a combination of online and agent averaged 3.7 quotes.

Exhibit 2

Shopping for auto insurance has become a truly multichannel journey

Percent of purchasing auto insurance customers



Note: Includes only shopper data

[1] Including online aggregators

[2] Normalized; some respondents may not have had servicing with current carrier at time of survey

Source: 2012 McKinsey Auto Insurance Customer Insights Research

- About 50 percent of all quotes came from the top four brands mentioned above.
- Only 10 percent of shoppers used aggregator Web sites to gather quotes.
- Success in converting consideration to quote strongly reflected convenience, as 7 of the top 10 drivers of brand perception related to it in one form or another. However, two of the top three drivers related to marketing, at least partially explaining some of the success of the heavily advertised brands and the lack of traction for aggregators.

Purchase

- Sixty-five percent of all auto insurance consumers (shoppers and loyalists) – regardless of tenure – purchased through an agent, with an exclusive agent/independent agent (EA/IA) split of 45 percent/20 percent. Thirty-five percent used direct channels (call center and online).
- Of recent shoppers, 59 percent purchased through an agent, with an EA/IA split of 39 percent/20 percent. The direct channel appears to have recently picked up share whereas the IA channel has lost some, driven perhaps by the movement of longer-tenured consumers back into the shopping loop or changing consumer preferences.
- Of the 41 percent of shoppers who purchased coverage through direct channels, 22 percent reported binding coverage through a call center and 19 percent bought online (including the less than 3 percent who ultimately purchased through aggregators).
- Success at the moment of purchase correlated with “relationship” as a key theme in brand perception; agents and call centers were successful because they more effectively address this need by offering a human touch, while online channels (including aggregators) were less effective at converting quotes to bound policies.

Loyalty

Brand loyalty is driven by a wide range of emotional and reputational associations. These associations take time to build and must resonate across multiple touch points. Some consumers are loyal because they are happy with their carrier and have embraced these associations – these are the *active loyalists*. Another set of consumers are loyal not because of any positive associations or a high level of satisfaction, but because they cannot immediately be bothered to change – we call these *passive loyalists*.

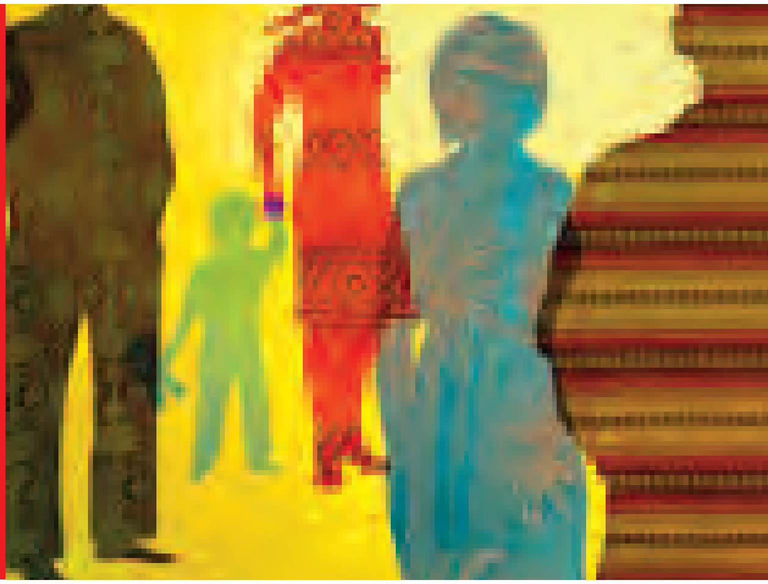
The balance of active and passive loyalists matters, as carriers with higher active-to-passive (A/P) ratios tend to enjoy stronger retention. According to the McKinsey research, the A/P ratio for the entire market was 3.2, with 55 percent actively loyal (representing $93 billion in premium) and 18 percent passive ($32 billion). The A/P ratio for the largest carriers as a group averaged 2.6, with USAA (14.6) and The Hartford (7.0) outperforming peers thanks to affinity programs that drive loyalty, not just acquisition.

When both active and passive loyalists were asked what might trigger them to shop, some triggers stood out as significant across both groups:

- *Pricing increase* was the trigger most frequently cited by both active and passive loyalists (with 90 percent of passive loyalists and 80 percent of active loyalists noting a likely willingness to shop).
- *Customer service* issues also resonated as a trigger for both active and passive loyalists (with 69 percent of passive and 63 percent of active loyalists saying they would shop in response).

Other triggers revealed significant differences in expected response and highlight potential avenues for carriers seeking to dislodge passive loyalists:

- *Recommendation* (e.g., strong word-of-mouth from a trusted source) would drive 70 percent of passive loyalists to shop versus only 47 percent of active loyalists.
- *Life triggers* (e.g., moving) would drive 67 percent of passive loyalists to shop versus only 48 percent of active loyalists.
- *Changing needs* (e.g., new coverage needs) would drive 65 percent of passive loyalists to shop versus only 40 percent of active loyalists.



A Granular View of Consumer Segmentation

While longitudinal data and analysis of carrier brand performance across the consumer decision journey are helpful in providing snapshots of the market, they are not sufficient for making targeted decisions on where and how to focus carrier efforts. Only a perspective based on consumer needs can provide the right level of granularity.

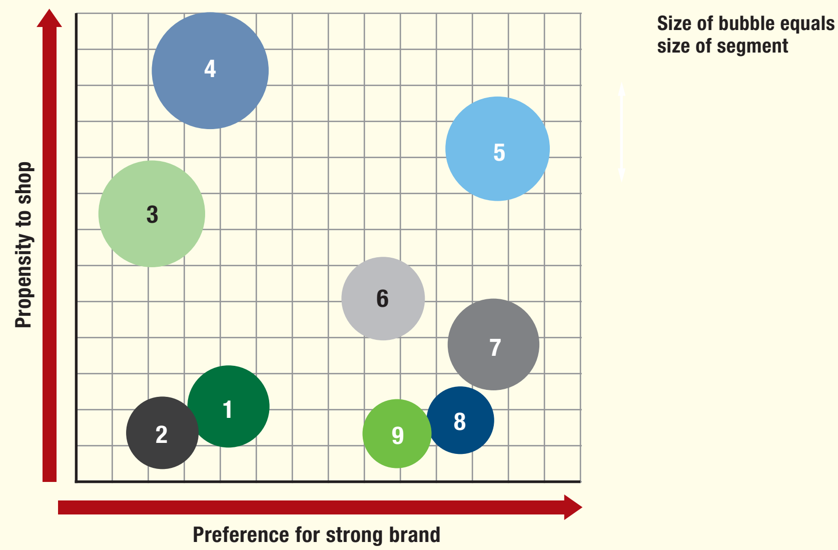
McKinsey's Auto Insurance Customer Insights research is one of the largest studies of consumer behavior in personal lines insurance ever conducted, providing unprecedented insights into the needs-based behavior of different segments. When consumers are grouped by common needs, nine segments emerge (Exhibit 3, page 12).

Of these common needs, the need for a strong brand is the most differentiating for consumers. There are others: propensity to shop, preference for a personal relationship and access to a local agent are all significant. Low price, by contrast, is a modest differentiator, highlighting how lower prices have almost become table stakes.

Customers in the nine segments display a range of distinct behaviors, particularly at different stages of the consumer journey. For example:

Exhibit 3

McKinsey research has identified 9 high-level auto insurance buyer segments, based on customer needs



Segment 4: Active shoppers Actively research options and shop frequently (50%+) Price conscious, though reluctant make tradeoffs between coverage and price Want information and advice	**Segment 6: Price-conscious advice hunters** Want both personalized advice and low cost Biased towards stronger brands Less loyal, with 31% shopping	**Segment 5: Self servicers** Prioritize convenience and expect multichannel access Do not value having an agent Above-average price sensitivity and propensity to shop
Segment 3: Low-price experts Make decisions based on the ability to get the lowest price Willing to reduce coverage and make other sacrifices (on brand, convenience, etc.) to control cost Shop and switch frequently	**Segment 7: High-touch protection seekers** Seek tailored coverage and extra protection options Require a strong brand, though biased for high-touch local agents Want multichannel convenience Willing to pay for expectations	**Segment 9: Branded agent loyalists** Want both a strong brand and a local agent Biased towards exclusive agent channel Loyal, with 70% staying over 10 years, and lowest reported shopping and switching rates
Segment 2: Uninvolveds Largely defined by their lack of preference; indifferent towards auto insurance Do not require convenience, advice or brand	**Segment 1: Independent advice seekers** Prefer advice of a local agent representing multiple carriers Tend to follow agent's advice Not particularly price sensitive	**Segment 8: Affinity-oriented brand buyers** Want strong, established, well-known brands Not interested in a personal relationship with a local agent Do not want to research options or actively shop/switch

Source: 2012 McKinsey Auto Insurance Customer Insights Research

- While the overall shopping rate is 27 percent, the rate varies significantly across segments. Segment shopping rates for monoline auto range from 15 to 50 percent, and for bundled auto and homeowners from 3 to 50 percent. For some segments, bundling reduces shopping rates by half, while for others it has no benefit on shopping rates. This range suggests that there is a significant difference in the lifetime value of consumers in each segment.
- Some segments display a strong propensity to shop, others do not; while shoppers collect 3.1 auto insurance quotes on average, the number ranges from 2.7 to 3.5 quotes depending on segment. In fact, three segments (29 percent of consumers) accounted for 50 percent of quotes.
- Binding channel preference varies significantly by segment; for example, preference for direct channels ranged from under 10 percent to 80 percent. Carriers must operationalize to deliver on segment needs if they hope to perform well in the long-term.

In addition to these findings for each step of the consumer journey, the relative importance of carrier touch points with consumers and carrier brand associations differ both by step of the journey and by segment. For example, advertising strongly correlates with success in consideration, but the specific strength of that correlation varies by segment.

How Carrier Performance Varies

Carrier performance varies both by segment and by stage of the decision journey. Most carriers appeal to a particular segment and win disproportionate share in that segment, while few outperform across multiple segments (Exhibit 4, page 14).

No carrier outperforms its competitors across all stages of the consumer decision journey. Even the fastest-growing carriers appear to have embraced strategies targeted at "winning" specific steps in the journey while ceding others (Exhibit 5, page 14). For instance:

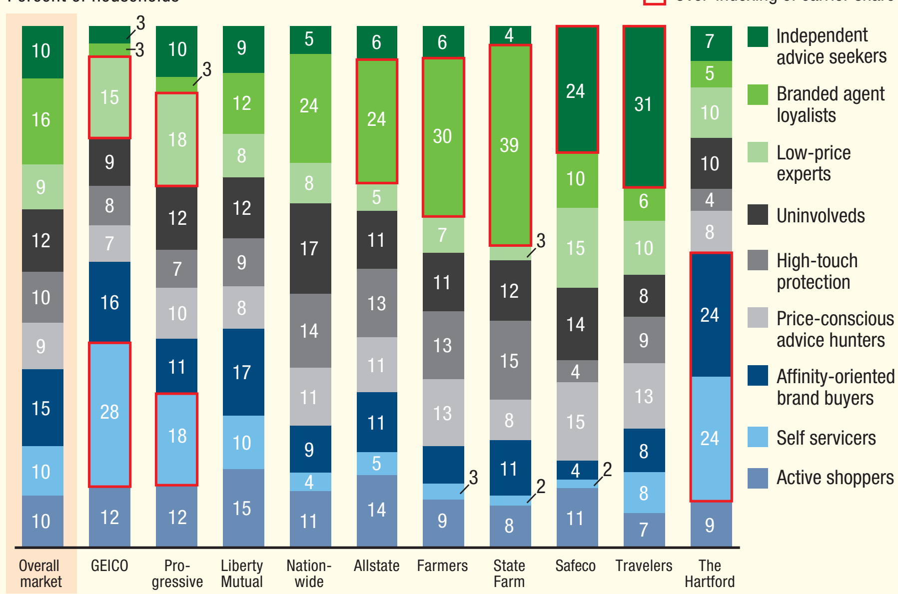
- GEICO's marketing spend helps it dominate consideration, while its focus on price and convenience draws price-sensitive and convenience-focused shopper segments that negatively impact performance in the loyalty loop.
- USAA's focus on fulfilling a broad suite of financial needs and coverage (from a broad set of financial products) to members of the military community, based on superior consumer insights, allows it to outperform at the moment of purchase and in the loyalty loop.

Exhibit 4

Some carriers are winning specific segments, while other carriers are undifferentiated in their focus

Carrier consumer mix, by segment

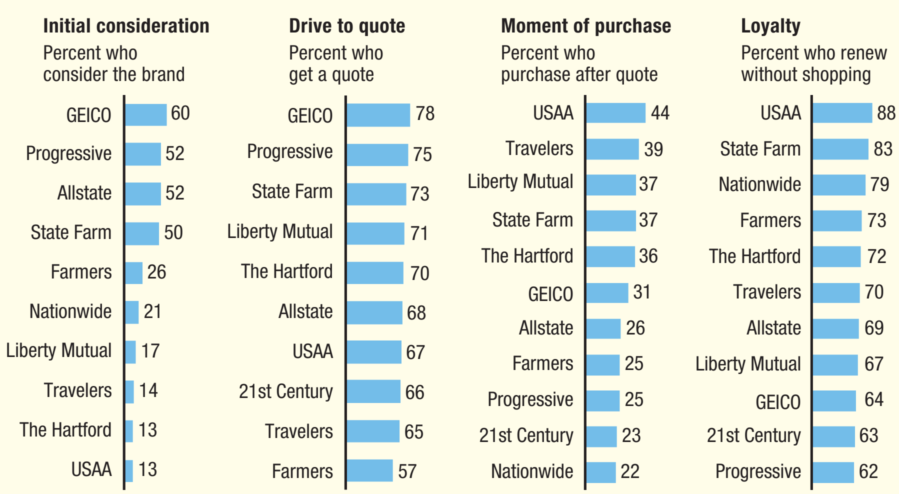
Percent of households



Source: 2012 McKinsey Auto Insurance Customer Insights Research

Exhibit 5

Carrier performance varies along the consumer decision journey



Source: 2012 McKinsey Auto Insurance Customer Insights Research

Implications and Questions For Carriers

The findings of McKinsey's research raise a number of implications and related questions for carriers:

- **Target consumer segments with compelling marketing messages.** Which segments fit best with our strategy and value proposition relative to the competition? What brand equities and marketing touch points are most effective for our target segments? How do we strengthen our understanding of consumer needs, and make decisions on where and how to invest in meeting those needs?
  - *Consumer behaviors vary substantially across needs-based segments, and the attractiveness of each segment will vary from carrier to carrier. Carriers need to understand which segments are right for them, and identify the messages that will allow them to win disproportionate share.*
- **Get more mileage from marketing spend.** What is the optimal level of marketing spend and the right media mix across multiple distribution channels, geographies and consumer segments?

- *As marketing costs increase, so does the importance of marketing effectiveness. The impact of marketing and other touch points vary along the journey, and importantly, by segment. A segment-level lens will allow a carrier to better optimize its spend.*

- Balance acquisition and retention efforts. What is the right balance between acquisition and retention? What strategy, investments and tactics will help us retain consumers?
  - *As marketing costs increase, the value of loyalty grows. However, active and passive loyalty are not the same. What are the keys to reaching the 18 percent of consumers who are only passively loyal, and worth roughly $30 billion in DWP?*

- Build a seamless multichannel consumer experience. What is the role and what are the economics of the online, phone and agency channels as channel boundaries continue to blur? How do we leverage each channel to its fullest while providing the right level of customer choice?
  - *Consumers are increasingly using multiple channels throughout the decision journey and even during a given stage of the journey. Carriers who make this journey a seamless one will gain advantage in both acquiring and retaining policyholders.*

Success in personal lines auto insurance will demand targeted investments in new capabilities to strengthen the marketing organization (see our white paper, *Beyond Price: The Rise of Customer-Centric Marketing in Insurance,* January 2013). The findings of McKinsey's recent in-depth research underscore the importance of the marketing function in auto insurance, and provide new perspectives for understanding how shoppers make their decisions. Putting this information to work will differentiate the winning carriers of the future.

About Mckinsey's Auto Insurance Customer Insights Research

McKinsey's 2012 research on auto insurance shopping combines three perspectives to provide a rich view of the evolving market, the drivers of change and insights on implications. The first looks at more than 15 years of data from past surveys to provide general observations on today's shopping and switching habits within the context of longer-term trends. The second generates insights into the underlying drivers of brand perception and loyalty, and explores what it takes to win at each stage of the consumer decision journey. The third provides a granular view of consumer behavior by looking at the variation in behaviors across different "needs-based" segments.

To learn more about the survey, contact McKinsey_NA_Insurance@McKinsey.com.

Contact

For more information about this report, please contact:

Devin McGranahan
Director
(412) 804-2745
devin_mcGranahan@mckinsey.com

Tanguy Catlin
Principal
(617) 753-2467
tanguy_catlin@mckinsey.com

Sharmila Ray
Associate Principal
(617) 753-2283
sharmila_ray@mckinsey.com

The authors would like to acknowledge the contributions of Justin Budd, Thongchie Shang and Vicki Smith.

Financial Services Practice
July 2013
Designed by Hudspith Design

www.mckinsey.com/clientservice/financial_services