Changing lanes: Car insurance for the new era

An analysis of how shifts in driving behaviour during the pandemic have highlighted flaws in traditional car insurance; with expert insights, data and new research.

Introduction

With 60% of the UK's adult population working from home for at least part of 2020 according to Finder research, car usage is predictably down on previous years. And while there's an expectation that many things will eventually return to relative normal after the pandemic, car usage could prove to be an exception.

In fact, there is a larger trend at play - one that was emerging long before COVID-19 appeared but which the resulting lockdowns have simply accelerated. Car usage was steadily declining for more than a decade in the UK before plummeting in 2020, but car insurance prices have apparently failed to keep pace, and the pandemic has shone a spotlight on the difference.

The Financial Conduct Authority (FCA) decided to intervene during the spring lockdown, requiring insurers to consider customers' latest risk profile, and whether they were due a refund or better suited to another product.

Then, in September, the regulator turned its attention to the "loyalty penalty", finally issuing its proposals in response to the Citizens Advice super-complaint made two years earlier.

How is the sector responding to these huge shifts? While there is innovation, some believe it's not nearly enough, given the huge changes in the way the UK is living, working and travelling. Are we likely to see more charging per mile, for both driving and insurance? Are drivers keen to see more digital options?

In this paper, we've published new research, and gathered data and insights from industry experts on insurtech, how car insurance is changing, and the key challenges and solutions for the sector.

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How car usage has changed

Coronavirus and the resulting lockdowns have cut miles off the average car usage in 2020. An index from pay-per-mile insurer By Miles, based on data from its members, projects the average per car will be around 5,960 miles this year.

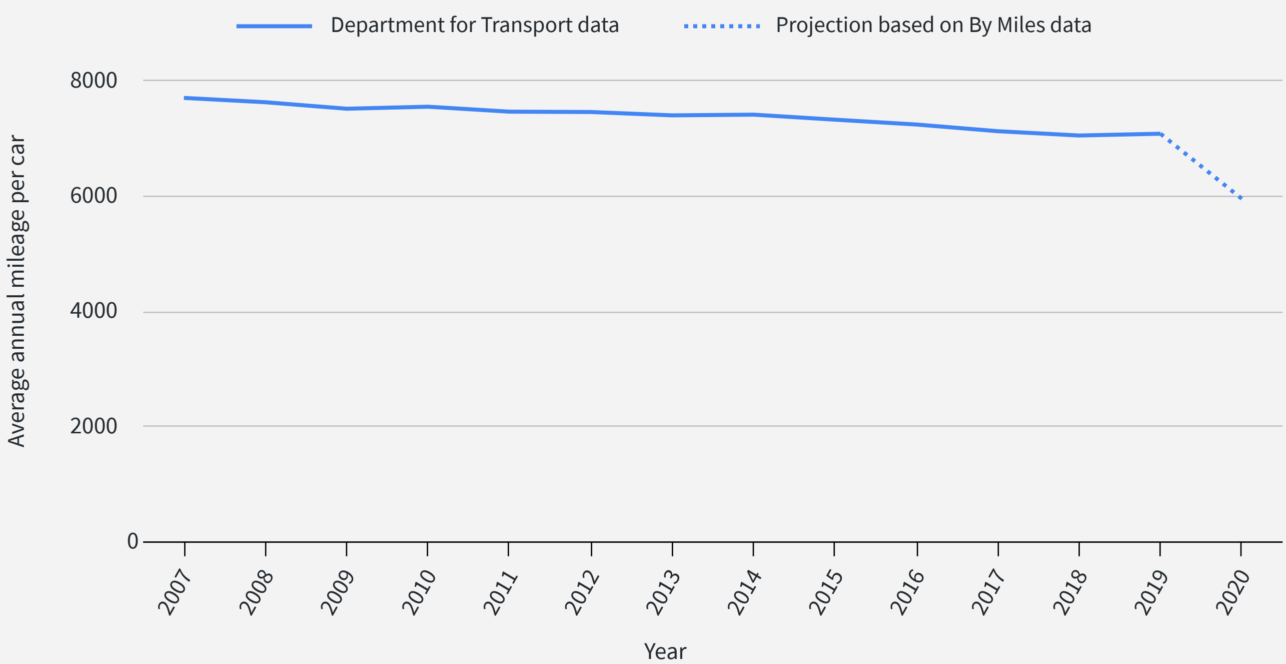
This is 16% lower than the average mileage in 2019, and will likely be even lower following November's lockdown. The miles driven by By Miles members have dropped by a quarter since the first lockdown began, in March.

However, white it's tempting to write this off as a temporary, albeit dramatic, drop-off, car usage was trending downwards since long before coronavirus drove the UK off the roads.

Between 2007 and 2019, the average mileage per car dropped by over 8% in the UK, and it's a similar story when it comes to the frequency of car usage. The average motor insurance customer took 580 car trips in 2019, 13% fewer than they did in 2002, according to Department for Transport (DfT) data.

Some argue that car usage may pick up in a post-pandemic world, as people remain averse to using public transport - but that's unlikely to turn the long-term downward trend, and vaccines may also resolve concerns about public transport .

Average annual mileage per car, 2007-2019



Source: Department for Transport, MOT (class 4) data

Is the market changing?

Car insurance has not been particularly profitable for most providers, but is a reliable source of revenue. Martin Friel is a former head of communications at AXA who is now a journalist and communications adviser. He says: “Motor insurance very rarely makes underwriting profit, but everyone who has a car has to have it.”

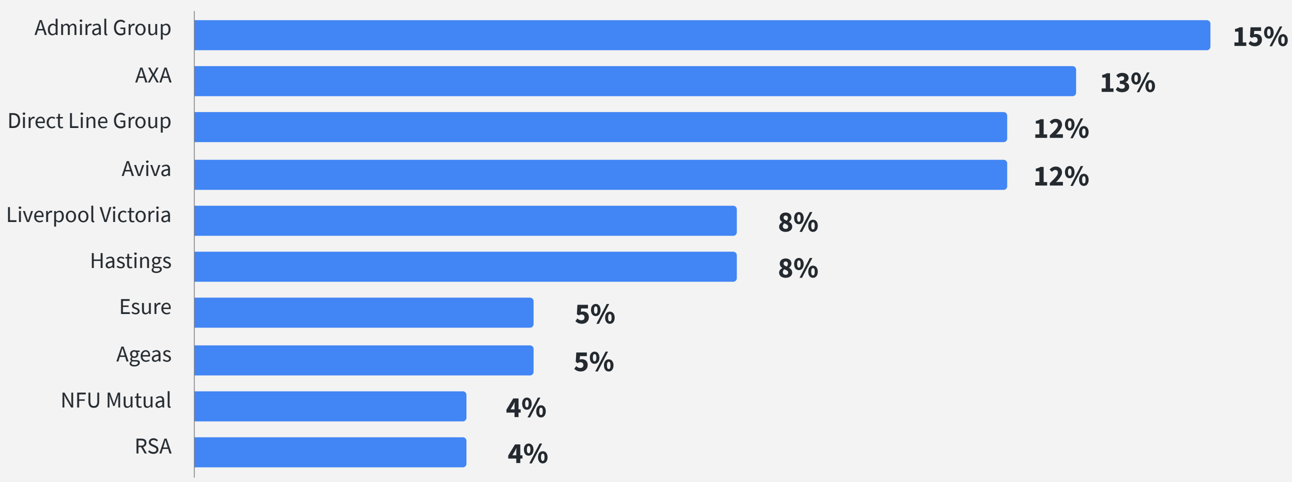
In the UK, the market is dominated by large British and multinational players, offering relatively standard levels of cover, based on aggregated customer behaviour. Over in the current account market, while the large banks also dominate market share, the fintechs are winning the battle for customers, with Monzo and Starling topping current account switching tables. Their insurtech counterparts seem to be having a harder battle.

The 10 largest motor insurers account for around 85% of the UK car insurance market, according to 2020 research compiled from company reports by analyst NimbleFins. And while many large players offer alternative types of policies, such as pay-as-you-go cover and telematics insurance, compared with the innovation seen in banking, the motor insurance sector overall seems years behind.

Change may pick up the pace in 2020, however. As car usage has dropped, the demand for more flexible car insurance has risen; challenger insurtechs have entered the market promising tailored, tech-driven insurance that better meets the needs of drivers using the car less.

Cuvva, which offers temporary and subscription-based car insurance, saw a 60% increase in sales between April and May, as a result of the coronavirus lockdown. Similarly, pay-as-you-go insurer By Miles saw a 75% sales increase in July compared to January, as customers sought out policies that wouldn’t punish them for a COVID-enforced reduction in their car usage.

Largest UK car insurance companies by gross written premiums market share



Source: NimbleFins 2020

The COVID premium gap

With mileage steadily falling over the past decade or so, and likely to drop sharply in 2020, the cost of premiums is in the spotlight. The average premium has risen by around 25% since 2015, according to a tracker from the research agency Consumer Intelligence, while average annual mileage per car fell by around 3% from 2015 to 2019.

Various factors are cited as contributing to the premium increase. Cars have become increasingly hi-tech and therefore more expensive to insure, according to research by the Association of British Insurers, and a change to the Ogden discount rate has meant insurers now pay out more in compensation to accident victims. Standard insurance premium tax rose several times - from 6% in 2015 to 12% in 2017 - too. And record low interest rates have had a knock-on effect on the bottom line of insurance companies.

All this is unlikely to placate customers who are hardly using their car but not seeing lower premiums, though. New Finder research has found that customers could have saved up to 48% on their premium in 2020 if they had taken out a pay-as-you-go (PAYG), per-mile policy instead of a traditional policy.

In our study, we used three scenarios - a low-risk, medium-risk and high-risk driver - to get an average premium for each based on the UK's 10 most popular cars. We estimated that each driver's mileage would be 16% lower in 2020 than 2019's figure. Our high-risk driver would have saved an average of £783 per year on insurance (£845 vs £1,628) and our average-risk driver would have saved £194.

But PAYG wasn't the cheapest for our low-risk driver, whose traditional policy was £204, while PAYG was £305 - around 50% more.

Drivers could have **saved up to 48%** on their **2020 premium** with **PAYG**

finder.com

Source: Finder

The pandemic (and the Financial Conduct Authority) has highlighted the need for providers to be able to adjust cover in line with a change in drivers' behaviour and needs. How responsive is the sector?

Tailoring cover

Views from the challengers are that incumbents in general are stuck in a "one-size-fits-all" rut. By Miles' James Blackham says: "The public have been encouraged to change their habits during the coronavirus lockdown and we don't think it's fair that British car insurance providers are not doing the same."

Freddy Macnamara, CEO of Cuvva, concurs: "Incumbents are in a terrible cycle of doing things the way they've always been done. The one-size-fits-all approach to annual car insurance, for example, might have worked decades ago, but it's no longer fit-for-purpose for millions of sporadic drivers."

A recent survey by insurtech platform EIS found that 42% of insurance customers listed the insurer's ability to offer individual pricing as a key factor when buying insurance; 32% also listed an easy-to-use mobile app as a key factor.

The consultancy ISG recently interviewed nearly 300 insurance leaders across Europe; 90% planned to speed up digital transformation and 95% said customers wanted more digital products and services. Yet only 61.5% planned to invest in digital customer experience and only 20% planned to invest in insurtech. Direct Line is an exception, having launched its own insurtech, Darwin, in 2019, which gives it a digital platform that can adapt quickly to changes in demand.

Although car insurers have generally been slow to offer alternative types of cover, one area of growth has been telematics; 58% of the top 5 cheapest car insurance quotes for drivers aged under 25 are from telematics providers, according to research by the analyst Consumer Intelligence, and there are now over 50 telematics insurance products available in the UK, up from just 25 in 2016, according to research by the ratings firm Defaqto.

Companies have also innovated in making telematics more convenient. In 2016, every telematics policy required the customer to have a black box fitted to their car - an unappealing option for many. In 2020, almost half of the telematics market offers an alternative tracking method, such as a plug-and-drive system or dedicated app, demonstrating the sector's willingness to evolve.

However, insurtechs are keen to leapfrog these advances by offering all this and more, with an efficient and slick experience.

> Incumbents are in a terrible cycle of doing things the way they've always been done.
>
> **Freddy Macnamara, Cuvva CEO**

"With these startups, such as By Miles, offering a different way to insure your vehicle, traditional telematics offerings may need to step up their game if they want to continue to corner this segment of the market," says Consumer Intelligence product manager John Blevins.

Rebuilding trust

Loyal customers pay **£85 extra** for car insurance, **on average**

finder.com

Source: Financial Conduct Authority

Alongside responding to customers' changing needs, the sector is faced with rebuilding trust and overhauling pricing after the FCA published a report and proposals from its long-running "loyalty penalty" market study, in September.

The FCA's recommendation that car and home insurers end the practice of dual pricing is likely to be implemented in 2021. The regulator estimates that the changes will save consumers more than £3.7 billion over the next 10 years.

The announcement led to further publicity around cases of long-standing customers paying far more than new ones, fuelling negative sentiment.

Another intervention by the FCA, in May, concerned reviews, refunds and other measures to help customers struggling financially. The regulator published guidance asking insurers to "consider the value of their products in light of the exceptional circumstances arising from the coronavirus...".

While Admiral and LV won praise for being quick to offer partial refunds to customers, many customers felt the industry had fallen short.

In July, Finder surveyed car and home insurance customers about insurers' communications concerning the impact of the COVID-19 lockdown on their cover. While 39% said their car insurer had been clear on this, 37% said they'd heard nothing and felt left in the dark.

"There have been some motor insurers that have given customers cash back for not driving as much during the lockdown, but what these customers got was chickenfeed in the grand scheme of things," says insurance journalist Martin Friel.

"The...industry is being viewed as having abandoned its customers in a crisis. And for an industry that is supposed to be there in a crisis, that is a huge failure of purpose."

Adapting at pace is no mean feat, and pay-as-you-go (PAYG) insurance may prove unworkable at larger scales. But the key challenges facing the industry involve finding ways to innovate on the current model - not necessarily by a shift towards one new one, but potentially by offering a broader range and better tailoring.

Multiple offers

As By Miles' James Blackham admits: "We recognise that it's not possible for all insurance companies to shift to this model [PAYG] quickly. But something must be done to protect lower-mileage drivers from being overcharged in the meantime."

The challengers themselves also face an uphill battle, and there's no guarantee that flexible, PAYG policies will - or should - ever replace standard cover. Finder research found that PAYG insurance was potentially more expensive for certain types of lower-risk drivers - in our scenario, the older, experienced driver would have paid an additional £102 per year on average on a PAYG policy.

Telematics may not suit all drivers, either. "Telematics have been around in insurance for a long time now and while the adoption of telematics is increasing, it has achieved nowhere the level of market penetration that was predicted years ago," says insurance journalist Martin Friel.

He continues: "There are lots of opinions about why that is but the fact remains, it has under-delivered against expectations.

"I suspect the same will be true of pay-on-demand and temporary car insurance. Some firms are making a good go of it but I'm not convinced that it will become mainstream or the standard way of buying motor insurance any time soon."

Car technology

A further challenge will be keeping pace with the technological evolution of cars themselves.

"1 in 10 new cars sold in the UK are now electric, which comes as a clear sign that car insurance policies need to modernise and offer purpose-built cover to the drivers of these incredibly smart cars," says Blackham. "We think that eco-conscious drivers deserve car insurance policies that reward rather than inconvenience them."

The potential introduction of autonomous - or self-driving - vehicles means that the insurance industry may be facing an adapt-or-die moment. Friel suggests the change even threatens the entire car insurance business model.

"If autonomous vehicles mean a fundamental change to what is being underwritten (is it a person or computer?) and if other firms start insuring drivers, that means a huge reduction in premiums and, by extension, a huge reduction in investment returns," he says.

Freddy Macnamara, Cuvva CEO

"Whether the industry is prepared or not, insurance as we know it is evolving. Consumers are online after all and insurers need to better cater towards customers' needs. The insurance industry is being forced to adapt and digitise for the on-demand generation. It's no longer a matter of if but rather when, if they don't want to be left behind."

James Blackham, By Miles CEO

"Insurance could be at the front line of incentivising positive behaviour change and reducing CO2 emissions, by actually financially rewarding people for driving less. It is now clearer than ever that there's an undeniable link between high mileage and claims frequency, so we urge insurers to pass on the savings they're making onto lower-mileage motorists. When you drive less, you should pay less for your car insurance. It's as simple as that."

Martin Friel, journalist and communications adviser

"Autonomous vehicles promise to completely change the way motor insurance is underwritten and sold - where the liability lies, with the driver or the computer, and is a huge issue and one that the industry has started working on. The risk for insurers is that they get this technical aspect of it wrong or can't figure a way through it, but also there is an expectation that the manufacturers themselves will start insuring their customers directly."

Danny Butler, Finder insurance publisher

"The rising cost of car insurance is a big concern for customers, especially for those whose finances have been hit during the pandemic. Our new research suggests many customers could save hundreds with a pay-as-you-go policy, and we believe more people will start seeking out alternative forms of cover to save money, especially if their car usage continues to drop."

Conclusion

The pandemic has highlighted an apparent disconnect between car usage and the cost of traditional car insurance.

Both incumbents and challengers are taking steps to address the changing needs of their customers, but in general, insurance seems far behind banking in the move towards digital convenience and transparency. Customers' expectations have been raised, and many will be scrutinising their outgoings far more closely in the coming months.

About Finder

Finder is a personal finance website which helps consumers compare products online so they can make better-informed decisions. Consumers can visit the website to compare utilities, mortgages, credit cards, insurance products, shopping voucher codes, and so much more before choosing the option that best suits their needs.

finder.com/uk launched in the UK in February 2017 and is privately owned and self-funded by two Australian entrepreneurs – Fred Schebesta and Frank Restuccia – who successfully grew finder.com.au to be Australia's most visited personal finance website (Source: Experian Hitwise).

For all media enquiries, or for additional comment, contact matt.mckenna@finder.com.

About the author

Tom Stelzer is a writer at Finder specialising in personal finance and investing. He has an MA in media arts and production and a BA in journalism from the University of Technology Sydney.