Medical Xpress

Why the study of behaviour is important for the insurance industry

December 14 2012

In a new Lloyd's emerging risk report, a team of experts from the University of Kent has shown how principles from behavioural science can be used to manage new and emerging risks more effectively.

The team, which was led by Kent psychologist Dr Mario Weick, an expert on behavioural biases and situational influences on judgments, highlighted obstacles in the identification of risks and pointed out how insurers can overcome limitations in human judgments such as encouraging divergent thinking, or rewarding behaviour that contributes to better risk identification.

For the purposes of the Economic and Social Research Council (ESRC) co-funded report, which is titled "Cognition: Minding Risks -Why the study of behaviour is important for the insurance industry," emerging risk is defined as 'an issue that is perceived to be potentially significant, but which may not be fully understood or allowed for in insurance terms and conditions, pricing, reserving or capital setting'.

The report, which can be viewed at www.lloyds.com/the-market/tool … merging-risk-reports, also suggests that in order to better manage risk at a time when new or emerging risks are more frequent than ever before - partly due to new and developing technologies - organisations should focus on risk horizons that are changing rapidly and that are of strategic relevance to them.

Dr Weick said: 'We know quite a lot about the way people perceive risks, and about the circumstances that can hinder or facilitate the identification of risks. However, the evidence is scattered and often difficult to access for people outside academia. There is not enough cross-talk between scientist and the industry. Our report fills this gap and shows that human factors are an important part of managing risks.

'Risks involve uncertainty and wherever there is uncertainty people tend to rationalise their decisions. Acknowledging that biases exist is a hurdle that organisations have to overcome.'

The team, which also consists of Dr Tim Hopthrow, Professor Dominic Abrams and Professor Peter Taylor-Gooby, also emphasised the importance of involving the social sciences and humanities in risk analysis.

Cognition: Minding Risks was commissioned by the Emerging Risks team at Lloyd's. As part of the Performance Management Directorate at Lloyd's, it is the responsibility of this team to ensure that the Lloyd's market is aware of potentially significant emerging risks so that it can decide on an appropriate response to them. The team also maintains contact with the academic community, the wider business community and government.

Neil Smith from Lloyd's Emerging Risk team commented: 'Lloyd's is a world leader in managing specialist and unique risks. At Lloyd's we have a team dedicated to identifying, tracking and managing emerging risks. For some time this team has identified behavioural factors as a key risk facing our industry and financial decision-makers in general. This report highlights some of the main behavioural factors that insurers need to be aware of if they are to manage new and emerging risks effectively.'

Provided by University of Kent