Bancassurance in Practice
Munich Re

Introduction

One of the most significant changes in the financial services sector over the past few years has been the appearance and development of bancassurance. Banking institutions and insurance companies have found bancassurance to be an attractive - and often profitable - complement to their existing activities. The successes demonstrated by various bancassurance operations, although not all of them have been successful, have attracted the attention of the financial services sector, and further new operations continue to be set up regularly.
The report discusses the various observed methods in use today under each of the following headings:

- Contractual relationships between bank and insurer
- Product ranges
- Sales channels
- Remuneration methods and training in bancassurance operations

The focus on Europe is deliberate since most developments in bancassurance up to the mid-1990s took place in Europe. This report is timely, however, because banks and insurers in other parts of the world, e.g. the USA, Canada and Asia, are now developing bancassurance operations. In doing so, they seek to learn from the experiences of European bancassurers.

Entering into bancassurance

2.1 Ways of entering into bancassurance

There is no single way of entering into bancassurance which is (best) for every insurer and every bank. As in all business situations, a proper strategic plan drafted according to the company internal and external environmental analysis and the objectives of the organization is necessary before any decision is taken.
There are many ways of entering into bancassurance. The main scenarios are the following:

- One party distribution channels gain access to the client base of the other party. This is the simplest form of bancassurance, but can be a missed opportunity.

If the two parties do not work together to make the most of the deal, then there will be at best only minimum results and low profitability for both parties.
If, however, the bank and the insurance company enter into a distribution agreement, according to which the bank automatically passes on to a friendly insurance company all (warm leads) emanating from the bank client base, this can generate very profitable income for both partners. The insurance company sales force, in particular usually only the most competent members of the sales force, sells its normal products to the bank clients. The cooperation has to be close to have a chance of success. For the bank the costs involved - besides those for basic training of branch employees - are relatively low.

- A bank signs a distribution agreement with an insurance company, under which the bank will act as their appointed representative. With proper implementation this arrangement can lead to satisfactory results for both partners, while the financial investment required by the bank is relatively low. The products offered by the bank can be branded.
- A bank and an insurance company agree to have cross shareholdings between them. A member from each company might join the board of directors of the other company. The amount of interest aroused at board level and senior management level in each organization can influence substantially the success of a bancassurance venture, especially under distribution agreements using multidistribution channels.
- A bank wholly or partially acquires an insurance company. This is a major undertaking. The bank must carefully define in detail the ideal profile of the targeted insurance company and make sure that the added benefit it seeks will materialize.
- A bank starts from scratch by establishing a new insurance company wholly owned by the bank. For a bank to create an insurance subsidiary from scratch is a major undertaking as it involves a whole range of knowledge and skills which will need to be acquired. This approach can however be very profitable for the bank, if it makes underwriting profits.

Whatever the form of ownership, a very important factor for the success of a bancassurance venture is the influence that one party management has on that of the other. An empowered liaison between respective managements, with regular senior management contacts, as well as sufficient authority to take operational and marketing decisions, is vital. Regular senior management meetings are also a vital element for a successful operation. There must be a strong commitment from the top management to achieving the aims in the business plan.

2.2 Reasons for banks to enter into bancassurance
The main reasons why banks have decided to enter the insurance industry area are the following:

- Intense competition between banks, against a background of shrinking interest margins, has led to an increase in the administrative and marketing costs and limited the profit margins of the traditional banking products. New products could substantially enhance the profitability and increase productivity.

Financial benefits to a bank performance can flow in a number of ways, as briefly outlined below:

- Increased income generated, in the form of commissions and/or profits from the business (depending upon the relationship)
- Reduction of the effect of the bank fixed costs, as they are now also spread over the life insurance relationship
- Opportunity to increase the productivity of staff, as they now have the chance to offer a wider range of services to clients

- Customer preferences regarding investments are changing. For medium-term and long-term investments there is a trend away from deposits and toward insurance products and mutual funds where the return is usually higher than the return on traditional deposit accounts.

This shift in investment preferences has led to a reduction in the share of personal savings held as deposits, traditionally the core element of profitability for a bank which manages clients money. Banks have sought to offset some of the losses by entering life insurance business.
Life insurance is also frequently supported by favourable tax treatment to encourage private provision for protection or retirement planning. This preferential treatment makes insurance products more attractive to customers and banks see an opportunity for profitable sales of such products.

- Analysis of available information on the customer financial and social situation can be of great help in discovering customer needs and promoting or manufacturing new products or services. Banks believe that the quality of their client information gives them an advantage in distributing products profitably, compared with other distributors (e.g. insurance companies).

- The realization that joint bank and insurance products can be better for the customer as they provide more complete solutions than traditional standalone banking or insurance products.

- Banks are experiencing the increased mobility of their customers, who to a great extent tend to have accounts with more than one bank. Therefore there is a strong need for customer loyalty to an organization to be enhanced.

Client relationship management has become a key strategy. To build and maintain client relationships, banks and insurers are forming partnerships to provide their clients with a wide range of bank and insurance products from one source.
It is believed that as the number of products that a customer purchases from an organization increases the chance of losing that specific customer to a competitor decreases. M. Pezzulo of the American Bankers Association quoted the following odds against losing a customer:

- Current account only 1-1
- Deposit account only 2-1
- Current and deposit account 10-1
- Current, deposit and loan 18-1
- Current, deposit and other financial services 100-1

2.3 Benefits from bancassurance for insurance companies
Insurance companies have identifed a number of benefits from involvement in bancassurance:

- Source of new business - previously unreached clients: the bank client base may well be (virgin territory) for the insurance company and so a new source of business. Possible reasons:
  - Geographic: the bank clients are in a territory where the insurer has only a limited presence (if any), e.g. because the insurer agency structure there is limited.
  - Demographic: the bank clients may form a very different group (e.g. by age, sex, purchasing habits) to the one which the insurer has previously courted.

For example, an insurer who previously concentrated on high net worth individuals (HNWIs) can now gain access to a wider range of customers who will not all be HNWIs.

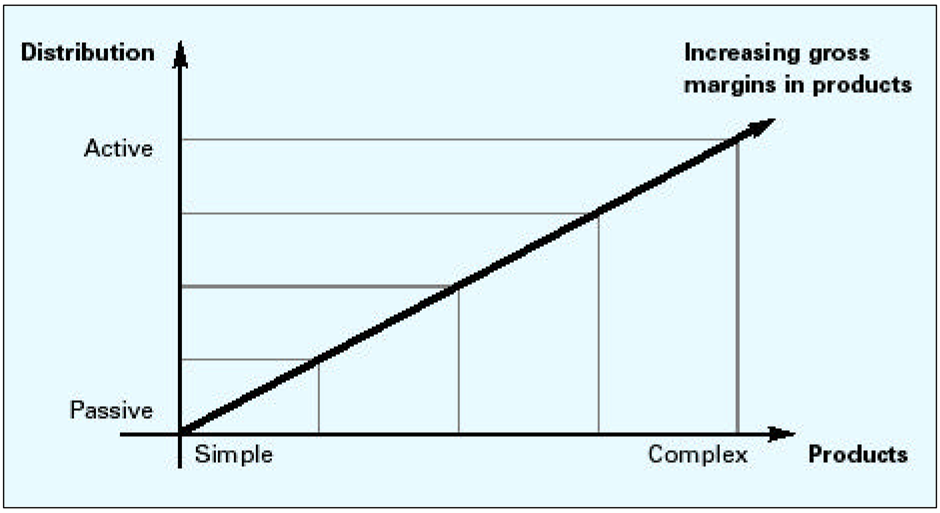
- Source of new business - wider range of products (including banking products): the insurance company hopes to attract further business, from both existing and new policyholders, because of the fact that it can offer a wider range of services than before, i.e. it can give its customers access to banking as well as to insurance services.

- Source of new business - products not otherwise feasible: the economics of the bancassurance operation may allow the insurer to offer products which are not feasible through the insurer existing channels. For example, sales costs incurred under existing channels may force premium rates for a product to be uncompetitive, so the product is not sold. The costs via the bancassurance channel may be low enough to make it feasible.

- Administration - economies of scale: the insurance company can offer to carry out the adminstration activities of the bancassurer business, if for example the bancassurer is a separate company. Combining the bancassurer business with the other business of the insurer can produce economies of scale in administration costs (including capital expenditure). This in turn allows the insurer to improve profitability and to price future products with narrower margins, which helps to make the insurer products more competitive.

Bancassurance products

All life insurance products are by nature products, which belong to the wider financial services sector. For a bancassurance operation in particular, however, the decision on the types of insurance products, which it wants to sell, is very closely bound up with the methods of distribution which it plans to use. This is because
the effort and expertise needed to sell a given product must be appropriate to the skills and cost base of the chosen distribution method. A product, which is very hard for the available distribution channels to sell, is not going to be successful for the operation, whether in terms of sales volumes or of profits.



Apart from the traditional insurance products, bancassurers have developed special products in order to fulfil certain needs, which emanate from banking transactions, or to improve certain products in order to make them more attractive and useful to the customer. These products can be broken down into three categories:

- Finance and repayment products
- Depositors products
- Simple standardized package products

Distribution channels

4.1 Types and characteristics

Some bancassurers started out by selling simple products which could be sold in large volumes but which usually had low margins to cover expenses and profits.
If we compare how products and distribution are related to the profits of an organization, we will come to the conclusion that the more complex the products sold are, the higher the required margins will need to be. The above Figure shows this relationship.

Bancassurers make use of various distribution channels:

- Career agents
- Special advisers
- Salaried agents
- Bank employees
- Corporate agencies and brokerage firms
- Direct response

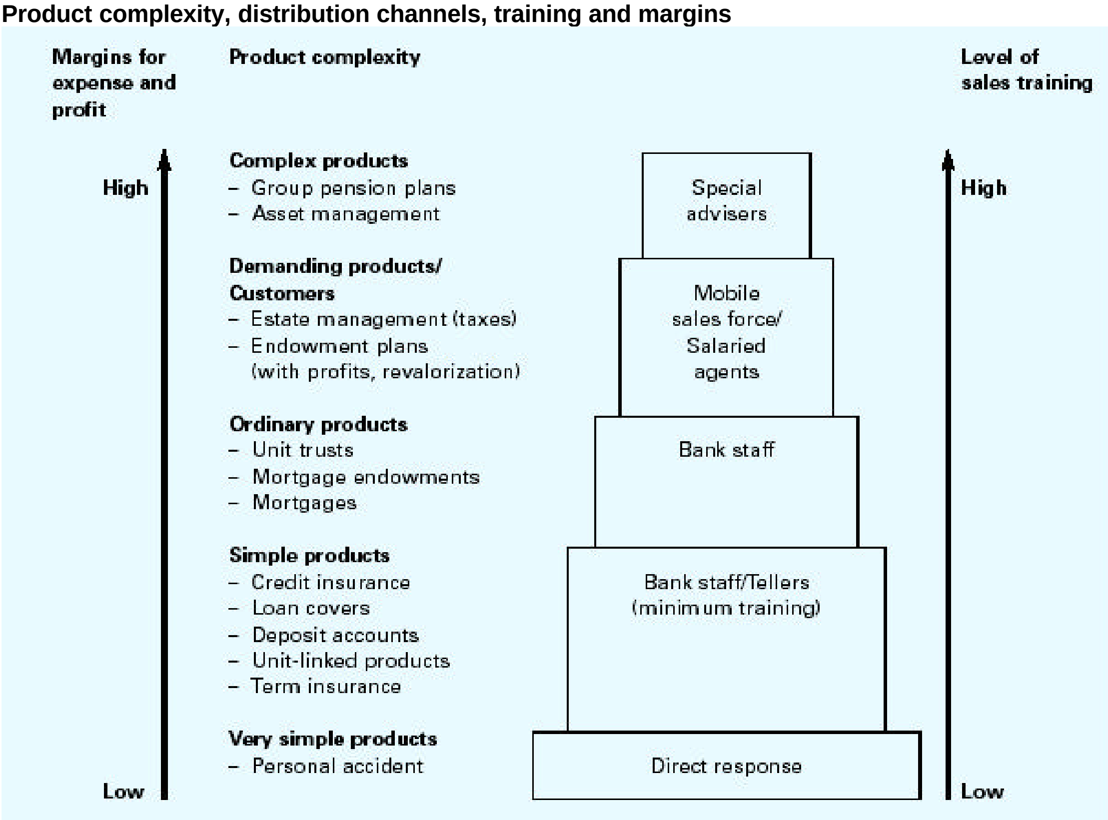
Career agents with suitable training, supervision and motivation can be highly productive and cost effective. Moreover their level of customer service is usually very high due to the renewal commissions, policy persistency bonuses, or other customer service-related awards paid to them.
However, many bancassurers avoid this channel, believing that agents might oversell out of their interest in quantity and not quality. Such problems with career agents usually arise, not due to the nature of this channel, but rather due to the use of improperly designed remuneration and/or incentive packages.

- Special advisers: special advisers are highly trained employees usually belonging to the insurance partner, who distribute insurance products to the bank corporate clients. Usually they are paid on a salary basis and they receive incentive compensation based on their sales.
- Salaried agents: salaried agents have the same characteristics as career agents. The only difference in terms of their remuneration is that they are paid on a salary basis and they receive incentive compensation based on their sales.
- Bank employees: bank employees can usually sell simple products. However, the time which they can devote to insurance sales is limited and a limited target market, i.e. those customers who actually visit the branch during the opening hours.

In many set-ups, the bank employees are assisted by the bank financial advisers. In both cases, the bank employee establishes the contact to the client and usually sells the simple product whilst the more affluent clients are attended by the financial advisers of the bank which are in a position to sell the more complex products.

- Set-up/acquisition of agencies or brokerage firms: In the US, quite a number of banks cooperate with independent agencies or brokerage firms whilst in Japan or South Korea banks have founded corporate agencies. The advantage of such arrangements is the availability of specialists needed for complex insurance matters and - in the case of brokerage firms - the opportunity for the bank clients to receive offers not only from one insurance company but from a variety of companies. In addition, these sales channels are more conceived to serve the affluent bank client.

Product complexity, distribution channels, training and margins



It seems very difficult for a single distribution channel to successfully reach the bancassurer goals and specific target markets. Many bancassurers are using multiple distribution channels.
Multiple distribution channels provide another valuable feature. They enable the enterprise to offer customers multiple options for access.
However, conflicts may arise among the various channels and also within channels under a multi-channel system. To avoid this it is necessary that

- it is clear to all which products each channel may sell;
- colleagues within a channel are motivated to cooperate;
- there is communication of the importance of every link in the distribution process;
- cultural differences are communicated and respected;
- the goals of every partner in the distribution process can be fulfilled by the process;
- the specific role and performance expectations of each channel member are clearly stated, understood and accepted;
- communication between channels is encouraged;
- Channel leadership is strong and committed to success.

4.2 Cultural issues in distribution

The managers of banks and of life insurance companies can come from quite different cultures. There may be differences in the way of thinking and business approaches of bankers and managers of insurance companies. These differences create a communication and implementation problem in bancassurance operations.
Banks are traditionally demand-driven organizations with a reactive selling philosophy. Life insurance organizations are usually need-driven and have an aggressive selling philosophy.
As a result the team spirit is negatively influenced and, since this is a crucial factor for the success of any operation, it has to be confronted.
Cultural differences between the banking and the insurance industries must be understood, respected and lived with in order for the bancassurance venture to succeed.
The development of a single culture is another possible solution but this requires a very strong commitment from the top management. This commitment must be continuously conveyed to all bank employees and life insurance agents.

- By eliminating the sales force, bank employees are forced to cross borders to a different profession where different skills are required

- The products that bank employees offer are usually simple packaged products or pure investment products
- Using only bank employees to sell insurance can severely limit the success of the bancassurer. The bank target market is then only the customer-base of the bank accessible to bank employees,
- Customer service offered in conjunction with the insurance policy is likely to be relatively poor since it is limited to banking hours.

Remuneration packages and incentive schemes

5.1 Objectives of remuneration and incentive schemes

To raise productivity and lower costs in today competitive economic environment, organizations are increasingly setting compensation objectives based on a pay-for-performance standard.
the designer of the remuneration package should seek to develop a package which helps each one in the distribution channels to feel that they get a fair reward for their contribution.

Before proceeding to the design of the compensation package, an organization must consider the following:
The compensation package is perhaps the most important element in a sales organization which will influence the volume of business, the costs, the profitability, the productivity and the customer care.

- financial services providers need to be sure they have the right people, in the right jobs, with the right skills, and at the right price.
- A package therefore needs to be designed to attract and retain the kind of people the company needs in order to develop the kind of sales organization the company wants.
- In developing this package an organization must have clearly in mind the vision of how it wants to be in the future, not just now.
- Before its implementation the package must be clearly communicated and explained to every single person involved in the bancassurance venture.

5.2 Remuneration of agency forces and agency management

Remuneration tools for agents of a bancassurer are commonly similar to those used for other insurance agency forces:

- Initial commissions to encourage sale of new business
- Renewal commissions on persistent business
- Other fringe benefits pension, health insurance
- Guaranteed salaries (e.g. percentage of last year commission)

For managers of agency forces, whose role is not to sell business but to get their agents to do so profitably for the organization, remuneration packages can include further items which reflect this role. Examples include:

- percentage of commissions earned by the agency team,
- persistency bonus (e.g. share of renewal commissions),
- rewards when members of the agency team reach specified targets

In setting benefit levels, distinctive features of a bancassurance operation which need to be remembered are:

- The package needs to be one which will attract agents to work for the bancassurer.
- The bancassurer must be able to explain to the agent the reasons for the particular structure
- For a bancassurer with several channels, the terms must be considered for each channel separately to make each channel attractive to both potential agents and to the operation. One aspect in looking at terms for each channel is to bear in mind the opportunities each channel has for selling business and generating income.
- Some (at least) of the business sold by the agency force is due to warm leads provided by the bank. In turn, the agent has to do less prospecting - and less work - to make the sale. The initial commission paid to the agent should reflect this. The proportion not paid to the agent can be used, among other things, to reward the bank branch and its employees for their effort in making the sale.

5.3 Remuneration of bank employees

Any commission payable by the insurance company is, as a principle, to be credited to the bank profit centre for the bancassurance operation. The bank management sets the commission level for each manager and employee engaged in the bancassurance operation.

- Selling in the bank branches (by employees or by financial advisers):

For simple packaged products: employees could be rewarded with gifts and/or salary increments based on their selling performance in promoting both banking and insurance products. Such performance could be quantified via the use of a points system where by the various products are allocated as a number of points.

- Warm leads:

In return for providing warm leads, the bank will get a share, say 50%, of the normal first year commissions.

A basis is needed for allocating this amount between branch staff (who provide the warm leads) and the bank owners. A possible basis would be:

25%
25%
50%

The structure shown above generates benefits as follows:

- Financial rewards for employees who generate warm leads
- Financial rewards for managers and other staff of the bank branch who have supported bank activities while the assurance business was being generated.

Group awards or bonuses are more desirable when the contribution of the individual employee is either difficult to distinguish or depends on group cooperation.

Training

6.1 Sales force training for bancassurers

a) The sales force will need to have (at least) basic knowledge of the banking products sold by the operation and of the range of distribution channels in force

b) Building up a relationship with bank staff:

The sales agent needs to learn to cooperate with bank employees and must learn how to build effective relationships with people whose job motivation may be very different to his/her own.

c) The bank expectations of customer service: the sales agent and sales manager must understand and be prepared to meet the standards for customer service which the bank expects in respect of its customers.

6.2 Bank employee training for bancassurers

The bank employees will need to be trained in the following aspects of the insurance business:

- Features of the insurance products sold
- How to identify and approach a potential customer
- Basic insurance needs
- Handling basic objections
- Other distribution channels and products
- Expected roles
- Procedures
- Remuneration and incentive schemes
- Cultures
- Customer service

6.3 Continuous training and supervision

Apart from initial training, there should be further training to support the development of the agent or employee. Some ways in which this can be done are:

- Agency meetings
- Bank branch meetings
- Area banking meetings
- In-house magazine
- Training circulars
- Area sales seminars
- Company library
- Video tapes
- Certified courses
- Lectures
- Training material booklets

A training activity record is a vital element for the manager of staff in a Bancassurance operation,

6.4 Quality customer service

Quality customer service refers to every single activity that the company, its employees and the distribution channels undertakes for its customers. In all cases the objective of every person in the company should be to give added value to every transaction or communication, providing additional incentives to customers
and enabling the company to

- distinguish itself from competitors,
- improve its image among customers,
- keep its existing customers,
- attract new customers, and
- Create additional sales among existing customers.

In a Bancassurance venture quality customer service is even more important because the bank refers its customers to the insurance company. The bank relationship with the customer can be damaged by poor service from the insurer.

For this reason bank employees must be well informed about the customer service standards set by the insurer when they refer them to their customers. At the same time the insurance company staff (including the administrators who will deal with the customers questions in future) must be aware of the standards expected by the bank on behalf of (their) clients. These service standards should be written down and agreed upon between the bank and the insurance company.