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## PRODUCT UNBUNDLING STRATEGIES

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1. What strategies will evolve in the 1980's for the development and marketing of services and products?
2. To whom will these services and products be offered? Individuals, groups, companies, government units.
3. What services will be marketable? Insurance needs analysis, financial planning, claim payment, money management, risk assessment, investment advice.
4. What products will be developed and enhanced? Universal Life, ART, annuities, non cash value whole life.

MR. LAWRENCE P. ENGLISH: Since we have done very little to publicize the name CIGNA Individual Financial Services Company, I want to talk a little about who CIGNA is and what CIGNA Individual Financial Services Company is. In 1982, the Connecticut General Life Insurance Company, a large stock insurance company with strong domestic presence in group insurance, group pension and individual life insurance, merged with the Insurance Company of North America to form CIGNA Corporation. At the time, it was billed as a merger of equals and was certainly the largest merger to affect the insurance industry. CIGNA Corporation by any measure is one of the largest insurance institutions in the country. At the time of the merger, it had assets of over 30 billion dollars, premium income in excess of 10 billion dollars, operating income in excess of 650 million dollars on a pro forma basis for 1981, and more than 40,000 employees.

CIGNA Individual Financial Services Company came into existence at about the same time as the merger. But I can say that the only thing one of them had to do with the other is this: they were both born out of the enormous amount of change that is taking place in the life insurance industry, or financial services industry if you will, in the last couple of years.

The best way to describe CIGNA Individual Financial Services Company is to ask you to picture the agency department of the Connecticut General Life Insurance Company. Add to this agency department of Connecticut General, a Broker/Dealer. Our Broker/Dealer was formerly known as the CG Equity Sales Company and is now known as CIGNA Securities. Add to that all of the training and support mechanisms that are associated with sales and distribution operations and you have CIGNA Individual Financial Services Company. It is essentially the distribution arm of the old Connecticut General Life Insurance Company.

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As you probably know, Connecticut General had been in the life insurance business for a long time and has enjoyed over the years a very attractive position in the individual life insurance market. In the latter part of the 1960's, the Connecticut General adopted a marketing strategy which proved to be quite successful. This strategy was born when our agency manager in Philadelphia created a dual thrust at the marketing of life insurance. It was based on a philosophy and a process. The philosophy that was adopted by our agents was a philosophy we called "serve first." It essentially said that our agent's objective when he called on a customer was to serve that customer's needs. It was built around the conviction that if, as agents, we did that well, we did that consistently, our commissions and compensations would take care of themselves. Hand in hand with that philosophy went the process that we used to market our products. We referred to it as the Estate Planning Process. It essentially involved an analysis of an individual's estate: his wills, his trusts, his plans for the continuity of his business, his plans to pass his assets on to his heirs, etc. From this analysis, recommendations were prepared as to how plans to accomplish his objective could be best structured. And, of course, these recommendations usually included life insurance products to help smooth out that transition.

That process and that philosophy allowed us to carve for ourselves a very unique position in the market. We were focused on what would in today's vernacular be described as the up-scale market, an affluent market, one that was predominately small business owners. We were able to sell policies in that market which had a high average policy size, had excellent mortality, had very good persistency, and created very good earnings for our agents and agency managers. Because of this system, we were able to recruit the best and the brightest people who wanted to come into the life insurance business. We were able to give them the best training and the best support. We were able to hire very expensive but very good management talent in our field organization and we were able to run a very profitable and a very attractive business.

Somewhere along the line, things began to change. It is difficult to pinpoint the exact time when things began to change rapidly, but I would like to talk about the changes that we experienced and then talk about the Unbundling Strategies we are employing to cope with those changes. First, and probably the most significant change that we have had to come to grips with, is the change in the very nature of our customers. We realize that today the customer with whom we deal is vastly more sophisticated than the customer with whom we dealt twenty years ago. He or she has access to more information. He or she has access to more sophisticated advisors. They are constantly being bombarded with information from everyone, from Sylvia Porter to Phil Donahue, on the value of permanent life insurance, term life insurance, etc. That consumer has become significantly more demanding, wanting to know more about the products and services he is getting for his money.

Changes in economic conditions also affected our business. Obviously, the high inflation and the accompanying high interest rates caused enormous disintermediation, which put tremendous pressure on our existing book of business and continues to put pressure on our existing book of business. The real impact, however, is inflation and the impact that it had on the desire of people to save, the desire of people to buy the basic product. Inflation basically destroyed the underlying value of the non-participating policies we were selling and caused our market to begin to shrink.

And then finally, changes in the competitive environment. Changes in the competitive environment were brought about by very talented and enterprising people who realized that if you approach the business without a distribution force, that if you concentrated on developing a product and building the commission into that product, and that if you used the distribution force of career agency companies, you could put together pretty good specialty products, sell them at very competitive prices and offer very attractive commission payments to agents. As a result of that, we began to see large amounts of business which otherwise would have been coming to us as a career agency company being written in a number of Brokerage or PPGA companies by the very career agents whom we had recruited, financed, trained, and developed. These business practices were devastating to us.

Take the intersection of these three massive changes: a much more demanding customer, chaotic economic circumstances and an intensively much more competitive environment. Superimpose these on managing a large block of non-participating inforce business and a very expensive career agency operation and you see the circumstances that the Connecticut General realized that it was in in the latter part of the 1970's. Fortunately, our management at that point in time had the foresight to begin doing something about it: to begin studying the situation, to begin analyzing the situation and to begin formulating plans for the future. Those plans were developed during 1980 and 1981 and we began to implement them early in 1982. We continue to aggressively work to implement them today.

We decided that the same set of economic circumstances that had created chaos for our business had also created a marketing opportunity for us. We decided that we had an asset in our field organization: in its degree of sophistication and in the fact that all our field representatives are registered with the National Association of Security Dealers and licensed with the Securities Exchange Commission. We had that asset and we had an opportunity in the market for something known as financial planning. We realized that we could no longer compete in the marketplace loading the cost of this enormous distribution system into the price of our insurance products. That distribution system simply was not going to work any longer: too many competitive products, too many sophisticated agents and, frankly, too efficient a market for us to be able to get away with that any longer. We had to develop other sources of revenue. We had to develop other businesses on which we could off load the expense of our agency system so that we could have competitive products.

The best way for me to describe the strategy that emerged from this business is to tell you that we intend to build a brand new business. We formed CIGNA Individual Financial Services Company in the first unbundling step. That unbundling step recognized that as an insurance company, we were basically in two businesses. We were in the business of distributing financial planning and financial products and we were in the business of manufacturing financial planning and financial products. These two could be, should be and indeed today are separate free standing, bottom line profit centers within the Connecticut General. The job I have with CIGNA Individual Financial Services Company is most analogous to that of Agency Vice President. But, as I mentioned at the outset, this includes much more than the normal Agency Vice President would have to say grace over. That was the first step. Then we had to recognize that there were other businesses that this distribution entity could get itself into in order to develop new sources of revenue, and new businesses on which to off load some of its very high overhead costs. When I talk about overhead cost, you must envision the network we have: an expensive agency operation, heavy staff,

and very sophisticated support mechanisms. We have regional design offices staffed with anywhere from three to six attorneys located around the country who basically help our agents in the design of cases and work directly with customers. A very, very large expense net that we have to cover.

What new businesses are we going into and how do we intend to operate this now separate, independent, off loaded distribution entity? The first is financial planning. We believe that there is a market for fee based financial planning. We believe that affluent individuals in the target market, in which we had been dealing in the past, are willing, able and, indeed, eager to pay for sophisticated financial planning. We went into the fee based financial planning business in five marketplaces as of August 1, 1982. We are in that business on a pilot basis. We are experimenting and trying different things. We are trying to develop different software techniques to support our agents in that business. I can only report to you at this time that our results have been very encouraging. We are able to sell this financial planning service. We have a long way to go before we will be ready to introduce this on a national basis, but right now the results look very encouraging. It appears that it will be a good revenue source, that it will be a good profit source for the distribution entity, and that it will be able to carry an enormous amount of the overhead that had previously been covered in the loads built into our life insurance products.

We recognized that there was another business that we needed to get into. We recognized that we could not operate, and I submit that no career agency company can long operate, on the premise of its agents giving them only a part of their business. It simply costs too much to train, recruit, develop, house, benefit and support career agents to allow them to spend half of their time working for you and half of their time working for someone else. It is our intention to ultimately receive revenue on any sale any of our agents make. Now obviously we are not in that situation today, but we are in the general agency business and we are brokering term insurance and other products. We will continue to broker other products with our agents receiving a commission, our manager receiving an overwrite and our company receiving a contribution to profit and overhead on each of those sales. This is a business we must get into. It must, obviously, be handled very delicately. We don't intend to put competing products in our general agency with products that we intend to manufacture in our own shop. I don't think that would make any sense at all. But we do have a very rigorous process for identifying products that are needed in our business. Products that our agents need in order to be objective in their financial planning work are given to our manufacturing entity first to determine whether or not it wants to manufacture that product. If it doesn't choose to manufacture that product, I, as head of the distribution company, am able to go out and negotiate with a brokerage company an arrangement to sell that product. A rather revolutionary idea that I think is beginning to catch on around the industry. I suspect it will spread very rapidly among those companies who decide to continue with a career agency orientation.

We have enhanced our securities business. The business we intend to be in the future will be built around a solid core of financial planning; a complete array of insurance products, whether manufactured by our company or accessed outside; and a complete array of investment products, whether manufactured or accessed from the outside. CIGNA Securities, our Broker/Dealer, will move over \$100 million in investment products in 1982. We are on a very aggressive growth track for the investment end of our business. I am talking not just about mutual funds, obviously, but tax sheltered, tax advantage investments. These latter investments are a very big part of our financial planning business.

We have gone into yet another business. We have always been in the affluent sector of the market, basically concentrating on business owners. We have never done very well in the corporate executive market, probably because corporate executives do not have very much of an appetite for permanent life insurance and that was the core of our formal process. They do have a voracious appetite, however, for financial planning and they do have a voracious appetite for investment products, particularly tax advantage investment products. We are developing a separate aspect of our fee based financial planning business, which will be marketed on a group basis as a perquisite for the senior officers of large corporations. I am pleased to say that we were successful in selling that notion to Mr. Kilpatrick, and CIGNA Corporation's executives were our first customers for that separate business. People are very excited about the work that we are doing in this area and we are very optimistic.

As a result of these separate businesses, we believe we will be able to put on the street competitive insurance products in our own portfolio. We believe we will be able to maintain our current book of business or to exchange that book of business into new products which we are aggressively trying to sell. We believe we will have a future. In fact, we are committed to the fact that we will have a future. We don't know all of the details of how this financial planning business is going to work, but we do know that there is a market. We are excited about the merger because the merger has given us the financial and the management strength that we need to execute this program.

We will be introducing a new product series in the next few months and this has basically been the first opportunity we have had to test this concept of distributing and manufacturing. We went through a very rigorous pricing process. The way I looked at it was that I should be able to get from the manufacturing entity whatever distribution allowance I could get for a comparable product in the marketplace. The way manufacturing looked at it is that they would set their profit standards and assumptions and they would solve for the distribution allowance. That is, whatever is left over. They would also have to set the market price. We have reached the negotiating level somewhere in between those two aspects. But, obviously, the price of this product is not going to include distribution allowances at anywhere near the level that we had to spend in 1982 to support our business. So we are putting this pricing strategy and this process into effect.

Our future business will be customer related and will be based on financial planning, insurance products and investment products. It is a bold, very aggressive strategy. It is, obviously, a very high risk strategy but it is one we are very, very excited about. We believe we have the financial and the management resources to pull it off and we think we are going to do so.

MR. ROBERT L. LINDSAY: Because the environment sets the stage upon which corporations as well as individuals must perform, it cannot be ignored. The essential question that we all have is: Is your company willing to anticipate change and take some risks, but also in the process, hopefully reap the rewards? Or will your company follow the mainstream and decline as many companies will in the 1980's?

It is a much harsher environment that we are now facing than we have faced in the last twenty-five years. In the past, many mistakes have been punished very lightly and this is mainly due to the fact that the economy has been rising and there have been enough resources for everyone. But now our mistakes are being punished very harshly. I won't dwell on the environment too long but just want

to mention some of the factors that will influence companies and their planning processes because I think these factors are important to the actions that you will take, both with respect to home office services as well as field services.

One important fact that is facing us now is taxation. The industry is embroiled in a grand dispute over how much and who should pay the tax bill. The mutuals argue that their share of the tax burden has been oppressive and is at a level never contemplated when the 1959 Tax Act was enacted by Congress. The stocks argue that the mutuals must bear a proportionately larger burden, otherwise the stock companies will not be able to be both competitive and be able to provide a reasonable return on their shareholder's equity. My biggest concern is the possibility that the ultimate tax act will put the industry at a competitive disadvantage with other elements of the financial services industry.

Now some of these companies outside the life insurance industry have taken steps to obtain a foothold in the life business. A recent example is Citicorp, which has acquired a company in South Dakota, which under the present laws, can actually sell life insurance. The resources which these outside companies can put to bear on a situation are enormous and, if tactically placed and executed well, can give some life company CEO's insomnia for years to come. They may march on the industry even in the absence of a tax fiasco. After all, these giants seek the same things the life companies strive for: a customer base and optimum use of resources, both financial as well as management. It is my contention that the industry will be seriously impaired if, (1) the total tax burden on the savings element becomes oppressive or (2) if the inside buildup on policies is taxed.

The second environmental factor which is extremely important is regulation. Actually there are two phases to this factor. One is regulation as it affects life insurance companies, and the second is deregulation as it may benefit bank holding companies and other financial institutions. Can your company effectively compete with the major banks and credit card companies? Have you analyzed your strengths and weaknesses compared with these new players? It is important to go beyond looking at your company as a life insurance company and comparing it with other life companies. You must go beyond and look at the whole financial services industry. Now is the time to become very serious about planning.

The third aspect is inflation, which has had a serious impact on reception of the public about our products. At this point, inflation has abated somewhat. Over the long haul, with the government funding enormous deficits, you can't help but believe that inflation will raise its ugly head again. But, of course, it's likely to happen right after companies have lengthened their investment portfolio.

The fourth factor is replacement, which has had serious impact upon companies both in terms of future profitability as well as the ability to match both assets and liabilities. The question is how should you plan for the future. It depends on the lines of businesses that you are currently in and what you plan to be in the future. If your company relies heavily on the individual product line, you should change your way of thinking about this line and visualize the life line as a declining industry and plan accordingly. In declining industries, the cost of production and distribution are the key factors to success. There have been many articles written in the Harvard Business Review and other periodicals about managing in declining industries. It is well worth our while to dig those out and study them carefully. If your company is heavy in the group product line, competition has always been a factor in limiting profits per unit; fortunately these lines are still in a growth phase.

The environment will shape the types of companies that we will have in the industry in the next ten years. If present trends continue the survivors may fall into one of the following categories: select group of career agency companies, companies which offer multiple product lines, and mass marketing companies. Mr. English mentioned where his company is headed and it is essentially a career agency company.

For those companies which will offer multiple product lines, we can distinguish between product providers and product distributors. Product providers are essentially price and idea driven. They must have very efficient operations and be on the leading edge of product development; otherwise, they will lose their market share. They must provide excellent field support with illustrations, technical advice, etc., in order to win business from personal producing general agents. Also, they must have excellent fundamentals in terms of persistency, expense results and investments.

The second category is the product distributors. The key here is to provide income to the sales force so that that sales force can survive. Here it is essential to provide income streams other than for the individual life insurance lines. This is why some companies have entered the personal lines property and casualty businesses, stock brokerage, etc., to provide additional income to their agents. The challenge is to find the new coverages and to provide these new coverages at a long term profit. It is interesting to note that some of the multiple lines companies have been very successful both in terms of growth and financially. This success may depend to a large extent on where their sales offices are located. Those that have clustered into the central cities have not done as well as those companies that have themselves out in the suburbs, largely because the quality of business is entirely different.

The third category is mass marketing and by mass marketing I don't mean the traditional group lines but rather soliciting business directly either through the mails or via two-way cable TV or computers. The keys to success in implementing this strategy are access to lists of prospects and expertise in mass marketing techniques. It is interesting that essentially the insurance expertise is secondary to having these two factors. Many firms outside of the insurance business have specialized in this type of market for many years. They certainly will have an edge when it comes to introducing life insurance and related products through this media.

Turning to the more traditional forms of mass marketing, we may see the industrial insurance companies seeking to shift sales and service from the home to the work place. They are finding that it is more efficient to go to the place where the people work and sell coverage through payroll deduction plans, rather than going to the home and selling the coverage and servicing it there. Essentially, mass marketing is a very efficient vehicle. We will see more and more products sold this way. A perfect example of this is the IRA market where many companies have decided not to sell IRA's on an individual basis, but rather try to package them on a mass marketing basis. We will see more products sold this way which means less compensation for career agents.

Let's spend some time discussing the unbundling of home office services. Our normal focus as actuaries is to look at products rather than services. This is also true of home offices in general. However, the question is: if the product environment is hostile, are there other ways of generating income or providing services to the public that can increase the viability of an organization? The same characteristics that will operate for a company that is going to be

successful in the product area also pertain to services. That is, you must have an efficient operation. You must have an access to the market. You must have good fundamentals. And perhaps most importantly, you must have the management who will act quickly and try to anticipate change.

One can list home office services that are now provided for our regular life, health and annuity operations which are transferable to other operations. Probably the most obvious one is data processing. In order to operate life insurance efficiently, we must process an enormous number of checks, payments, claims, etc. Having this ability, we can transfer it to other insurance companies or to outside financial corporations which provide similar type services. The reason that data processing can be unbundled is because many companies place data processing in a separate core center, which charges back for its services. So it is only natural that you compare the cost of these services with those in the outside market. Many companies, when they first introduced large computers, had excess capacity. The natural thing was to sell the excess capacity in the marketplace. Some companies are now selling existing systems, or renting them out, to other companies. Why should 1,800 companies design and develop a separate computer system for processing claims or processing policies? It makes a great deal of sense to narrow down the number of companies doing this and to provide packages for those companies who cannot afford the time or cost to do it themselves.

Investment management function is another obvious service that can be unbundled. A company can set up a separate investment subsidiary that would provide investment services to other organizations. Life insurance companies have a slight edge in the sense that they have managed long term portfolios for many, many years and have quite a bit of expertise in this area. We have good examples here in the past of companies providing advisory services to mutual funds, real estate investment trusts, etc. Also, some of the major pension writers provide discretionary asset management on specific pension cases. With legislation, insurers could also provide trust services for individuals and estates. It is also possible that some of the larger companies could provide investment services for the smaller companies, assuming that the conflict of interest aspects could be resolved.

Overall, the strategy of the company is really to increase its income or reduce its unit cost. One way of doing this is to seek ways to sell services in order to increase profits. One good way of getting started within a company, is to use a charge back system, not only for EDP but for all possible functions. Then, the managers of the various operations will get used to seeing an income and expense stream for their operations.

What's required is imagination and leadership. The question is, what expertise does your company have and can it be marketed? And then the final question is, how can you best package this product and market it on the outside?

MR. BRUCE WINTERHOF: Before talking about strategies for unbundling of products, it would be worthwhile talking about a couple of concepts. First, it is worth defining unbundling. There are really two aspects to unbundling: one is that you separate your product into pieces and market different pieces of that product; and the other is that you separate the product into pieces and repackaging it. If we look at the group insurance marketplace, we can see examples of both strategies. In the group insurance marketplace, the administrative services only, minimum premium funding options and other methods of providing insurance coverage are very popular. An example of the repackaging alternative is to provide benefits



on a cafeteria basis where the employees are allowed to select the benefits that are the most desirable given their situation. In the case of pensions, we can see the same thing happening. We have both deposit administration and group annuity contracts, which are totally packaged, and we have guaranteed investment contracts, which are highly specialized and represent total unbundling. In the case of ordinary insurance, examples of unbundling are not as common. In the last two years we have seen a proliferation of Universal Life, which is really the first and best example of total unbundling in the ordinary life marketplace. In it, we separated the term insurance element and the savings element of an ordinary life policy. The two pieces have allowed the policyholder to choose various combinations of term and savings according to his needs. Again, I think it is important to keep in mind what we mean by unbundling. It's really not just separating parts and pieces, it's also repackaging.

The second concept that I want to introduce has already been touched by the previous two speakers. It is how we view our business. Peter Drucker said it best. He said that business has two functions: one is innovation and the other is marketing. In the past, life insurance people, especially in the ordinary line, have been very strong in marketing but not as aggressive in terms of innovation. What we will see in the 80's is more product innovation. On the marketing side, we will continue to see market segmentation through sales. We will see new distribution channels and methods. Selling over the TV and other marketing methods will be available to us in the future. Technology will create that for us. On the innovation side or the manufacturing side, we are going to see a number of changes in the way we package our products that we are currently offering. We are going to see a number of new products, new services and new coverages.

The third concept is a conceptual way of thinking or viewing the products that we offer. It is helpful to look at the products that we offer as a sum of pieces. We could write a formula down on a piece of paper which is the summation of various components of a life insurance policy. We have the insurance element and an investment element. We have a loan element. We have a disability income element, waiver of premium, we have spouse coverage and we have family coverage. In the group marketplace, we have life coverage, accident and health coverage, dental coverage, property and casualty coverage, and in some cases legal insurance. In the pension marketplace we have investments, administration, and reports required for the pension marketplace.

It is helpful when you are thinking and talking in terms of unbundling your products that you view your products as a sum of various pieces. You allocate the total cost to various pieces to determine whether you can offer that piece on a competitive basis and a profitable basis. In terms of developing a strategy for product design, repackaging and unbundling, the first thing that you have to do is identify the driving force for your situation. Driving force is somewhat hard to define but, in my mind, it means the starting point for every decision that you make. In some cases, it is your marketplace and, in other cases, it is your internal administrative capacity. In some cases it is your technological abilities. After you have identified the driving force for your situation, you can then develop actual strategies for segmenting or separating your product into pieces and repackaging it according to your strengths and weaknesses.

As a final step, you can identify the resources that you do not currently have. A good example would be some insurance companies today acquiring corporate entities which are necessary to market the investment vehicles that they believe are saleable in their marketplace. Another example is the acquisition of systems

and personnel. This is often done through acquiring outside software or by acquisition of other companies.

In terms of setting your actual strategy, there are a number of internal considerations involved in determining the product packaging. The first consideration is your market segment. The question is what volume of insurance dollars and savings dollars does your market segment have. In the case of the sophisticated marketplace, there is a good deal of savings dollars available to us as investment dollars. In the case of lower income marketplace, there are fewer savings dollars available, especially with the effect of inflation in recent years. So, in that kind of marketplace, we would tend to offer a product that emphasizes the insurance element.

The second internal consideration that you want to keep in mind is your distribution method. Mr. Lindsay has already outlined three distribution methods. One is the traditional agency marketing operation. He describes different variations of that in terms of control, such as the career oriented field forces or the PPGA/Broker field forces. You need to identify how sophisticated your marketing arm is and what its abilities are to market various investment products and insurance products. You have to determine what is compatible with your agent's capabilities.

The second distribution method is through mass marketing. In that case, generally the product package is more simple. You cannot sell a product that is so sophisticated that you cannot introduce it to the consumer through the method of mass marketing. Generally your mail solicitations are fairly simple.

The final consideration that you should keep in mind in terms of determining the packaging strategies is your company's own abilities. Consider your financial size measured in terms of surplus and available capital. You have to look at your administrative capabilities and you have to look at the people you have. As I said before, if they are inadequate to implement the strategy you have chosen, you need to acquire the items you need to overcome the deficiencies.

There are a number of packaging strategies that you may consider. One is the cafeteria type policy. I have labeled it cafeteria policy even though it is sold on an individual basis. What this policy really provides is multiple options to the policyholder. In the case of an investment oriented marketplace, it would provide multiple investment options. Several years ago there were variable annuities available with multiple investment options. These are no longer available, but there will be variations of multiple investment options and products available in the future. The second kind of cafeteria policy would be a blanket insurance policy. This kind of insurance policy would package together life, health, auto, legal, dental and other insurance benefits into one product. Currently there are many regulatory hurdles to combining all these benefits into one policy. At some point in the future, because of the natural demand for this kind of policy, we will be able to overcome those regulatory hurdles.

We have recently developed a product which combines life insurance, disability and retirement into one policy. The benefits and premiums for this product are tied to the income of the insured. It has been a very successful product and it represents a kind of first stage cafeteria policy.

A second type of product packaging strategy is the specialty product. There are many companies today that market specialty products. Examples of this type of

product strategy are credit insurance, guaranteed investment contracts, mortgage insurance, travel accident insurance, and other similar products.

The final product strategy, which is going to be popular in the 80's is companion products. This is a product which you design to be marketed with other products. An example of this kind of packaging strategy would be marketing term insurance with investment products, such as tax-exempt unit investment trusts. Another example would be marketing term insurance and waiver of premium or settlement options with IRAs that are sold by banks or savings and loan institutions.

Finally, I want to talk briefly about the objectives you might have when you decide on a packaging strategy for your products. These are my own opinions and I think I could have expressed the same feeling ten years ago. The first objective is that you want to transfer any risk to the policyholder which is not controllable and predictable. Examples of this are the disintermediation risk and the cost shifting risk. In the case of disintermediation, we have been able to manage it pretty well recently by introducing policy loans at variable loan rates. This transfers the policy loan risk directly to our policyholders. We still suffer from the possibility of policyholders withdrawing their funds when our interest rates are low and new money rates are very high. A second example of transferring risks is in the individual and group health areas where the insurance industry has suffered from cost shifting recently. In this case, many writers of insurance benefits are switching to products which provide some co-insurance element and high deductibles in order to transfer part of the responsibility for keeping costs low to the policyholder.

The second objective for product packaging is to transfer services to the policyholder; or not sell services to the policyholder, which another institution can provide at a lower cost. Again this goes back to the concept of looking at your products as a summation of various pieces and identifying those products and services which you can provide on a profitable and competitive basis. A third packaging objective is to make certain that your profits match your risks. Specifically, the risks built into the package design that you choose should not be so great that your profits are inadequate. The final product objective is to make sure that the product is adjustable. This means adjustable for the buyer and for the company. In the case of the buyer, the packaging strategy should include various options so that the product is not inadequate or inappropriate in the future. In the case of the company, it may be appropriate to include some kind of experience rating mechanism. For example, in Universal Life we determine both current term charges and interest charges. At some point, we will also try to pass on the market valuation risk to the policyholder.

In summary, this package unbundling and rebundling represents a number of challenges for insurance management. First of all, management must identify its company's strength, evaluate its marketplace and distribution methods and, then, design products which are appropriate. The second challenge that the actuary will face in the 80s, is to evaluate the risk in various packaging alternatives which he is considering and establish appropriate profit objectives. In the future, instead of pricing profit into the product, the actuary is going to have to determine whether he can make an adequate profit on the product that he can sell. The third challenge will be that we, as actuaries, need to develop products for which little experience is available. We will be pricing products using assumptions with which we feel comfortable but for which we have little experience.

MR. WILFRED A. KRAEGEL: Mr. English, what are some types of products that the new CIGNA organization has set up that are actually selling? What kind of unbundling have you done in the product sense?

MR. ENGLISH: In the product sense, the first thrust of unbundling will be a new portfolio of products which we will be introducing this spring. This portfolio will essentially contain a new flexible ordinary life product and some current interest type options to go with it. We introduced a Universal Life product earlier in the year. That should really be billed as the first product priced on an unbundled basis. The fee based product itself, of course, we think of as an unbundled product. Our investment product portfolio included in 1982 a real estate trust, some private real estate offerings, some equipment leasing offerings, things of that nature. This investment portfolio will be enhanced further in 1983. That is basically what we are talking about.

MR. GENE ECKSTUT: Does the fee basis for your estate planning support all your branch office expenses or do you still have to put some of that expense into your plan costs?

MR. ENGLISH: No, it does not, and it is not anticipated that it will support all of our branch office expense. We will still have some loadings in the life insurance products and we will get some support from the investment products that we are selling as well. At this point in time, I cannot really comment on how much of the overall overhead will be borne by the fee based product. We do not have sufficient data at this point to know what market price we can charge for it. We are not sure what manufacturing implications or additional costs will be associated with manufacturing that product, nor have we decided how much we are going to pay our agents.

MR. WINTERHOF: Mr. English, in your pension products, do you offer a similar fee structure for your clients?

MR. ENGLISH: No, the fee package we have been selling does not zero in on the employee benefit packages, it zeros in on the individual's own financial needs: accumulation, estate planning, business continuity, things of that nature. We deal with our group pension division in the same way as we deal with other manufacturing entities of the Connecticut General. We have a selling agreement with them, that is, we sell their products and they pay us commissions and allowances.

MR. ARCHER L. EDGAR:\* Mr. Lindsay, I think you made a statement that individual life insurance is considered a declining product.

MR. LINDSAY: If you look at it in terms of the growth in reserves less policy loans relative to the growth in inflation, I would say it is declining.

MR. EDGAR: I question your statement from the viewpoint of why are all the banks and other financial institutions trying to get into a declining industry. Also, the demographics of the population indicate that individual life products have a great future. I believe a little bit like Jack Miller does. In his presentation yesterday, he stated that the industry has a great future. The individual insurance business performed better than the economy did in 1982, although it was a bad year. It was a year in which we saw many IRAs sold.

\*Mr. Archer L. Edgar, not a member of the Society, is Director of Manpower and Market Research for LIMRA.

In 1982, Dean Whitter direct marketed an offer to 15 million people to purchase IRAs on their Sears credit cards, and they sold 64. At the same time, Prudential went out with its sales force and in three months they sold something like \$35,000,000. Basically, what I am saying is that there are about 20 or 30 companies that are bearing the brunt of the distribution system right now, and that the distribution system, so far, has been a freebie for everybody else to tie into. The banks and stock brokers who want to get into it are getting into it because they think it's free out there. The people of the 30 companies that have carried this cost are on the right track when they begin to flex their muscles a little bit and say they want to be paid for this resource.

MR. LINDSAY: No one has a perfect crystal ball future. My comment on the performing industries is if you look at the growth in reserves less policy loans, which is one measure of growth over a long period of time, and tie that in with the Consumer Price Index, do you really have real growth in the basic assets underlying the life business? As far as other industries getting into the life business, it is just part of the mad scramble that is going on in the financial services industry to get market share and to be able to cover the cost of operating a business. Is the whole market growing significantly?

MR. EDGAR: In January, sales were up 20%, premiums were up 20%, policies were up 30%. If we walk away from it, the other people are going to get into it.

MR. LINDSAY: I won't argue that you won't have ups and downs in a particular period, but what has been the long term trend and what is the likely trend?

MR. ENGLISH: If you want to look at the traditional participating, non-participating whole life insurance business, we see that as a declining business. If you look at the financial services business (which would include all of the new kinds of products that are coming out: current interest products, universal life products, term insurance products, other investment oriented products, financial planning type products), we see that as a very exciting growth business. I don't know about the industry but our premiums were not up 20% in the first part of this year. They were down considerably. We are seeing lots of significantly increased lapses. Were your numbers net of lapses or were they total premium?

MR. EDGAR: The numbers were new annualized premiums as best as we can do. I think there is some double counting because some of this is replaced business. I have heard a quote that there has not been a new policy written in California in five years. I was not questioning the form that the product would take. I realize there is going to be unbundling in a lot of different forms, but I just think there is still a future for insurance.

MR. ENGLISH: That is the key factor. I agree with Jack Miller. I think this business, this industry has a very, very exciting future. If I didn't, I wouldn't be in it.

MR. KRAEGEL: I am trying to get a better handle on the changes taking place in the distribution system at this time. Mr. English, do you find that the people you have performing these services tend to be: life insurance salesmen who have branched out into investment areas; investment people who have moved over into the life insurance areas; or new people who haven't known either one before and are picking up both to some degree?

MR. ENGLISH: In our organization the answer, initially, is life insurance people who are branching out into investment products and fee based financial planning. We are basically taking our old agency operation and converting it into this new system of distributing financial planning, investment products, and insurance products. There have been a number of brokerage firms who have tried to branch out into the life insurance business and into the financial services business. They have had varying degrees of success. I have appeared on panels like this with people from the investment end of the business, and they get angry sometimes when I make the following comparison. Our people are relationship oriented, whereas the traditional stockbroker has been more transaction oriented and, as far as the future is concerned, it will be more of the kind of people we have brought into the life insurance business who will be the distributors of the sophisticated financial products and services. This is because it will be a business built on long term relationships and not built on transactions. The stockbrokers agree with that basic premise, but they feel that they are becoming more relationship oriented themselves.