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"NON-TRADITIONAL"/MASS MARKETING SALES TECHNIQUES

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This session will analyze current and possible future "non-traditional"/mass marketing techniques, examining their potential for enhancing present day, insurance marketing methods. The discussion will touch upon:

- -Mass Marketing's impact on the current agency sales system,
- -the problems encountered in implementation, and....
- -suggestions for ways in which current delivery methods can be complemented by techniques which seek to improve:
  - -Product delivery,
  - -Front-end market research, and....
  - -Company financial results.

MR. CRAIG M. BALDWIN: I'm sure you are all acutely aware that today's work environment has changed dramatically during the past five to ten years. Gone are the days when the company actuary could sit in his often referred to Ivory Tower, pricing products and reporting the financial impact with little involvement in the day to day functions of the marketing, administration, investment and data processing operations of his company. Today's highly competitive, technical world requires that the actuary become actively involved in all aspects of his business.

By no stretch of the imagination is mass marketing or direct response a new discipline. The economic changes which have taken place in recent years, in addition to the current search for ways to more effectively service and compensate agency operations, have heightened its importance as a marketing medium, especially for those companies which seek to remain on the cutting edge of the insurance marketing arena.

Our goal today is to present you with some food for thought, in addition to providing you with some ideas which you may find helpful in assisting you in dealing with the marketing operations of your company.

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MR. JAY M. JAFFE: During the past year, I've had the opportunity to put together some thoughts on how direct marketing can complement an agency force. I've been wrestling with this subject for a number of years, back as far as 1970, when I first became involved in the direct response business. The remarks I am going to make are presented with the idea of stimulating discussion. When I am finished, I hope that you will ask any questions which you may have, and express your opinions and ideas. This topic is certainly filled with questions and issues which we can not fully resolve today, but we, as actuaries, are certainly right to discuss them.

It's my opinion that an agency force and direct marketing are not at opposite extremes, but are compatible. I hope as we proceed you will reach this conclusion, or at least be able to formulate your own ideas as to how this concept could work in <u>your</u> company. It's even possible you'll get to a point where you will agree with me - the combination of direct response marketing and other forms of non-traditional marketing will be necessary for the agency force of the future.

A lot of this work began, and I would like to acknowledge him, with Neil Lund who is sitting in the back of the room. We've known each other for several years and Neil is in large part responsible for this presentation.

It's very misleading to think of direct response marketing as the business which only offers graded benefit, whole life policies, modest amounts of term insurance, hospital indemnity plans, or supplementary health products. It's a false image of direct response marketing. You will find as you analyze your companies and the whole industry in general, that there are three areas in which direct response marketing can complement a traditional distribution system. The first is lead generation. The second relates to products that an agent will not normally sell. The third is in the area of developing new customers. In none of these situations will direct response marketing conflict with your traditional agency force.

It's always helpful, in a meeting of this type, to start with a definition. I'm going to use the following definition: "Direct response marketing is that branch of insurance marketing which is designed to evoke a response from a prospect without the prodding of an agent". This is not the only definition, but it is the one on which I will base my remarks.

There are various media that can be used in direct response marketing. The one with which you're most familiar is Direct Mail. But let us not ignore four others. We have Telephone, this being perhaps the most important one of the future. We also have Television, Radio and Print (which would include magazines, etc). You should also keep in mind, that these five areas are not mutually exclusive. A campaign can involve more than one of these media. A typical example would be an 800 number used in conjunction with a television ad or a newspaper supplement. Looking into the future, we are going to see, in my opinion, a considerable number of electronic advances. This is going to increase the possibilities for different forms of direct response marketing. However, we are not going to look far into the future this afternoon, we're just going to deal with these five.

Let's talk about lead generation. Perhaps the primary reason that agents fail in the insurance business is the lack of qualified prospects. I don't know if a qualified prospect is worth his weight in gold, but certainly I know that a good lead given to a competent agent will result in a sale.

As an aside, for those of you who have not as yet had the opportunity to see the Pulitzer prize winning New York show Glengarry Glen Ross, it's all about salesmenship and sales leads, and I would recommend you go see it. It's a marvelous show, and I also think it would be a tax deductible expense for your companies to send you to New York to see it. Get two tickets, some expense money and a hotel room. It's probably far and away one of the best experiences that any person in marketing can have, and would be especially interesting for actuaries who are interested in what's going on in the lead generation process. You will enjoy it, and it certainly will be a fun way to spend a weekend in New York.

I am now going to discuss the use of a Direct Response Insurance Department in generating leads for an agency force. Direct response should do several things for them. It should help to develop potential clients in addition to generating leads from existing clients. It's my opinion that lead generation is really a science in itself. Potential clients are very helpful, obviously, for an agent. When he can get the good qualified lead, the agent should be able to go and close those leads at a much higher ratio than the ones on which he has simply cold called.

A good example of the developing of potential clients which I've witnessed, revolves around no-load mutual funds. The company advertises and sells a no-load mutual fund through the mail, then turns over these new customers to their agency force for follow-up life sales.

You also have to remember that your own customers, your existing policyholders, are your best leads. They are the ones you should attack first. That's the second part of this presentation. You all have existing clients and direct mail can be used to improve your relationship with them - to optimize the amount of business that you can get from this source.

Looking into the future, and I wouldn't do too much of that, I think you're going to find the agency of the future includes an individual called the lead specialist, skilled in the techniques of direct response marketing. I don't know how big the agency has to be before you're going to find this individual, but they will be there. You are going to find that many of these people will be geographic specialists also. There will be differences in the Chicago market as compared to the Toronto market, the Los Angeles market in comparison to the Dallas market, the rural market, etc.

There will be people who know these individual markets at the individual agency level. Your Home Office will have to be able to support these operations too, since there are going to be many functions which will be common to the lead generators. You will not need to duplicate the total operation in each area, but each will have its own unique features. Economies-of-scale will dictate the central functions of your mailing operations.

Next I would like to address the marketing of products which agents won't generally sell. An agent's objective should be to maximize his income with the least amount of effort expended. One of the ways an agent can do this is through a direct response insurance program with his insurance company. You will find that the company is willing to sell certain products that the agent is not willing to sell. The agent can develop this attitude for several reasons. First, the commission dollars involved may be very small. Secondly, some products may be too complicated for an agent and he won't sell it simply because he does not understand it. If we can get over the customer presentation hurdle, we might still be able to use that customer to generate more sales. The third reason is that some products are difficult to service and an agent doesn't want to get involved. He doesn't want to be involved in the situation where he cannot provide service to his customer and therefore jeopardize his business relationship.

And, believe it or not, number four is the ego issue. There are many products which, some agents believe, lack prestige. I'm not orientated that way, but I believe there are many people who are. When an agent chooses not to sell a product, it doesn't mean that his clients don't want the product, and that's the point to keep in mind. A direct response marketing program that's run by the company, on behalf of the agent to offer some of the products not normally sold by the agent, might be just what the doctor ordered for the agent who is seeking to increase his commission income.

With that, a company and an agent can establish a cooperative direct response insurance marketing venture, which would probably work something like this. The company would assume the expenses and the agent would have to agree to participate in the program. The company must notify the agent of the timing of the mailings so that the agent isn't caught by surprise. The company would have to assume the responsibility for processing the applications and, lastly and very importantly, the company is under obligation to pay the agent a commission, even though the agent may not have done all the work. It is this kind of cooperation which can foster successful programs.

I know one program that existed where an agent was able to make $55,000 in new first year commissions in one six week period as a result of this type of activity. I think that's pretty significant. The amount of commission the agent will receive will, of course, depend on the program. It could be a reduced or a normal commission. This is something you would have to wrestle with within your own companies, depending upon the particular product and the distribution costs. As examples of products suitable to this approach there is hospital indemnity, there are the various P&C products which may be available through a subsidiary of your life company, there is Juvenile Life which can be sold to the younger members of the policyholder's family, No-Load Mutual Funds which you might use to get the customer's money in-house, and IRA's which quite often involve very low commission for the agent but must be so to make the product profitable from your point of view.

The most difficult of the three roles that we outlined earlier for direct response insurance marketing to fulfill is developing customers outside of the agent's markets. Certainly this is the area where there is a great deal of potential and if it's successful, it can lead the company into entirely new areas of operation. A company and its agents generally target a marketplace and their agents are active only in a portion of that marketplace. These market segments can be defined in terms of geographic areas, income brackets, age brackets, etc. A company's agents working only in a limited area reach only a small percentage of most markets. Let's assume that the total marketplace is 100%, and a typical company would have less than 1% of the marketplace. A typical agent would therefore have a potentially huge market in which to operate. The opportunities are tremendous!

In developing direct response marketing, the one thing you don't do is use a shotgun approach. It will prove to be very costly and your venture will probably fail. My experience tells me that the sensible approach is to select market niches in direct response marketing and become experts in these smaller markets. This strategy has been successfully used by several companies to develop duel marketing personalities. There is no conflict within these companies because neither marketing section, the agency nor the direct response area, has anything to fear from the other.

The following are examples which I think demonstrate that there aren't any real, major conflicts between these two types of marketing. We have Capitol Holding with its National Liberty. We have Allstate marketing to Shell Oil. Even the mighty Prudential is involved in a major, major undertaking with the American Association of Retired Persons.

Generally, it may be the company's most successful agents who do not oppose direct response marketing operations. These are the agents who will ultimately recognize the value and use of direct response techniques. One company I know of recently tested the use of direct response to bolster sales in a large metropolitan area where they had a small agency force. The test went well and, as it turned out, those most interested in future programs were largly the more highly visible agencies in other major metropolitan markets. In other words, they were not turned off by the combination of direct response marketing and agency type operations.

MR. LEONARD N. SAMSON: I think a good place to start is with an outline of what I plan to cover. What I call my road map. The topic is direct response marketing with a focus on direct mail.

We will start right off with another definition of direct response marketing. This is the accepted definition created by the Direct Mail Marketing Association (DMMA).

"Direct Response Marketing is the total of activities by which products and services are offered to market segments in one or more media, for informational purposes, or to solicit a direct response from a present or prospective customer to elicit a contribution by mail, telephone or other access."

Let's explore this definition and I think you will agree there is more there than meets the eye.

- "Direct response marketing is the total of activities by which products and services are offered to market segments."

Based on the definition, direct marketing is a marketing system or distribution system. It is not an industry, although many people believe it is. It is not an alternative distribution system either. It is an additional system that can be used by itself, or in conjunction with other distribution channels.

A little over a year ago that point was driven home to me by Don Frahm, the president of The Hartford's P&C companies. During the competitive bidding process for the American Association of Retired Person's (AARP) endorsement of an Auto and Homeowners program, I used the term "alternative distribution system." He said, "You mean additional, don't you." He was sensitive to the agency issue, but he was correct in stating that direct response is not an alternative system.

- "From a present or prospective customer." Your companies all have existing customers or insureds. Therefore you have built in, or internal affinity groups to capitalize on. This list can be used to sell upgraded coverages, or cross-sell related or unrelated products.

  The only larger list, or market segment available to you, other than your own customer file, is the potential or prospective customer in the open marketplace. Direct response marketing can provide for a cost effective approach to reaching that market. We will discuss this in greater detail a bit later.

- "By mail, telephone or other access." The distribution system is multifaceted. We will talk about the techniques in a moment, but the techniques can be used singly, for example -- mail only, or in combination -- mail and TV.

- "For informational purposes, or to solicit a direct response." This is the objective. We want to generate an inquiry or a sale.

But what really is the bottom line? To quote Bob Stone "... underlying all direct marketing success is the ability to trigger a direct action, a measurable action at the right cost." That's right, a cost effective and efficient distribution system. We will talk about this again.

First let's look at the techniques.

Print includes magazines, newspapers, co-ops, flyers and pick-ups. Print also includes any other printed media dispersed on a widescale basis, other than direct mail. (Did you ever wonder why so many lawyers smoke? In the 1960's matchbook covers offered people the opportunity to become a lawyer through the mail at home. That's right, print direct response. So if your lawyer smokes, check his or her credentials.) The most common, and most widely dispensed, print direct response is in the magazines and newspapers. Here we have the use of ads, bind-in cards, free fall inserts, or pre-prints.

Broadcast includes television and radio. Use of, and expenditures for, this direct response media have grown dramatically over the years. It can be used as a direct sale medium utilizing mail or phone follow-up to close the sale.

The wave of the future is two-way response TV/Cable. This was tested in 1977 when QUBE was introduced in Columbus, Ohio. Developed by Warner Communications, QUBE is best described as a two-way response medium. It makes use of the great signal-carrying capacity of cable television. The home viewer can communicate directly with the station by means of an on-line computer hookup. As I said, it was first tested in 1977 and has subsequently been tested in various markets and formats. It will probably be available for commercial use in another five years.

Telemarketing is the use of telephone either as a support tool or as a direct sales mechanism. It can be used on an inbound or outbound basis. Telephone as a marketing medium has also grown dramatically over the last several years. This is true because of technological advances, general acceptance of the telephone as a sales mechanism, and the rapid increase in costs for other direct response media, relative to phone costs. It also functions as the only selective, targeted, person-to-person mass medium existing today. Print and broadcast are outstanding examples of mass media, while direct mail offers the marketer pin-point selectively. The personal sales visit remains the number one person-to-person approach. But only telephone combines all of these attributes.

In all of our recent project work in direct response, as well as future work, I contemplate factoring in the use of telemarketing in combination with other direct response media. It's hard to conceive of developing an overall direct response marketing strategy that does not in some way factor in telemarketing. Whether it's used to close a sale, prospect for qualified leads, follow-up or reinforce direct mail, receive direct response inquiries to TV, radio, or print media, or convert inquiries into sales, telemarketing will be the marketing tool of the 80's.

Direct mail is nothing more than an envelope stuffed with various components such as a letter, brochure, application, purchase form, business reply envelope or other printed material that is mailed into a household. Its sole purpose is to generate a lead (hot lead) or a sale. Between 1963 and 1976 the cost of a mail kit including postage (3rd class) went up 108%, and went up another 110% in the next seven years. It costs about 15-20 times as much to reach a person with a direct mail package than it costs to reach a person with a 60 second TV commercial, or a full page ad in a newspaper. Then why do I consider direct mail the best approach? Why is it the most used approach? What are the advantages of direct mail?

The first advantage is segmentation. Through careful list selection and segmentation criteria, direct mail can give you pinpoint selectivity, unmatched by any other advertising medium. You can literally pick households one by one, providing greater marketing and underwriting control. I will get back to this point a little later.

Next, as a general rule, customers acquired by direct mail tend to be better customers, in terms of repeat business, than those acquired by space or broadcast advertising.

Direct mail is a direct medium and has virtually no competition. In other advertising media, the advertising tends to be an adjunct, and not the main reason a person is watching a TV program or reading the magazine. Most of us go to the bathroom or kitchen (not necessarily in that order) during a commercial. In direct mail, the advertising arrives all by itself to be opened, and read, at the recipient's leisure. When it is read it has nothing to compete with it for the prospect's attention.

Another advantage of direct mail is its unlimited formats. In direct mail your message is not limited to 60 seconds or a 7"x10" page ad. You can use large, lavishly illustrated brochures. You can have many components. You can use pop-ups, self-mailers or fold-outs. Action devices such as premium offers, plastic cards and on and on. You are only limited by imagination, technology, and budget constraints.

Personalization and customer involvement are also important advantages. Even though you may mail millions of packages you are still mailing individual packages that are personalized. You don't mail to occupant or resident. Direct mail approaches the prospect on a personal level. Customer involvement is achieved through a wide choice of devices -- action devices such as tokens, stamps, rub-offs, plastic cards, sealed envelope questionnaires, quizzes, including the pencil to respond. Some people call these gimmicks. Call it what you like. They work if you use them.

A major benefit of direct mail is the fact that it is probably the most testable medium. You control when the mail is dropped and who gets which test package or product. You can use as many splits as you want. You are not limited to A/B splits, or no splits at all. All this translates into an ability to easily test and analyze results.

But what's the bottom line? Where's the beef??

With your ability to analyze results, and the other advantages discussed, Direct Mail should generate a higher number of responses and lower acquisition costs. The name of the game. Now I said should. I will talk on that issue in a moment.

First, let's look at the Direct Mail Process.

As is the case in any marketing effort, the first step is the creation of a strategic plan. The strategic plan should be a written document stating the objectives. Overall goals, as well as specific goals, should be set. These must fit into the overall corporate strategy and philosophy.

The goals must be prioritized as well.

- Next, the product - What is it, what does it do, how does it work, what does it cost, what are its features, what are its benefits, what makes it better or different, and what are its weaknesses?

- Competitive products - Who and what is the competition? How does your product compare in features, benefits and price?

- The market - how big is it, what share do you have, who buys the product, who needs the product, what are the demographics and psychographics?

- The media - In addition to Direct Mail what other marketing techniques will be utilized in combination and/or support?

- The budgets - staff, dollars and time?

Once this "easy step" is complete, we are ready to move on to the creative process. The creative process generally will start with a brainstorming session(s). With all that we know about the product: how do we organize it, position it, emphasize the features and benefits?

We then move into developing copy, art, photography, layouts, in addition to developing production costs and time schedules.

At the same time we must identify and generate our market segments. In other words list selection. You rent, buy, or build lists from which you will market.

You then segment this list(s) or file(s), you merge them, you purge them, manipulate and massage them, overlay and enrich them. The end product -- your mailing universe. A highly refined and productive list.

With all this great planning we know it's going to be a success. Right? Wrong!! If we can't execute the campaign it's going to fail. What do I mean? Produce it and get it into the mail. This means pulling together all the necessary production resources. Paper, printing, forms, envelopes, computerization, binding, lettershops and finally, the mail drop.

If we are lucky enough to get this far, we may yet get to the sale. If we get a response, if we can convert it (into a sale), if we can fulfill the product, we have a sale. All this means is that we get the premium.

Direct mail marketing is not for every company. Nor is direct response marketing for every company. At least not on a wide scale basis. There are some critical success factors that should be considered.

Let's go through some of these factors.

The success factors can be broken down into Product, Market Segment and Company Characteristics.

First, the product characteristics. The three most critical factors are price, uniqueness and simplicity. With a greater degree of competition and availability, I believe price becomes the driving force. Product uniqueness is next. However, "monkey see, monkey do." It does not take long before your competition is marketing the same product. But the most successful (insurance) direct response marketing companies will continue to try to differentiate the products. The "bells and whistles" that may get them a leg up. Finally, product simplicity. The more complex the product, the harder it is to explain. The harder it is to explain, the harder it is to market. Therefore simplicity, fewer exclusions, deductibles, coinsurance clauses, complex benefit structures, will translate into more positive copy and sales.

The next set of factors relate to the market segment or the group being solicited. Other than price (and I'm not sure of that), the market segment itself is the most critical factor.

Affinity is the key group factor in direct response marketing. With my clients I see this all the time. Response rates from unsegmented, high affinity groups such as AARP have been five to ten times greater than those achieved from highly segmented but low affinity groups (Social/welfare, association, religious groups, trade groups, business groups (banks)). Exclusive availability will provide a competitive edge. I had a client that rented lists from a bank. The bank also rented its list to seven or eight other insurance companies. My client wanted to know why they weren't achieving the results they projected and needed. Even though the price was somewhat competitive, it was entering a household with six other similar offers within a short time frame. This is seasonality - the optimum time to mail. As a result, the prospect, when faced with six or seven decisions, will say no.

A large and growing group is preferred so that it can sustain long-term marketing efforts. Large numbers achieve economies-of-scale. A growing group will help minimize file wear-off and response rates can be maintained.

Next, good underwriting characteristics. Not every sale is a good sale. Who wants to market health insurance to a parachute jump club, professional wrestlers or construction workers. Adverse selection can kill you even if you think much of the underwriting can be handled through product development, pricing and screening. It is important to have a group with favorable underwriting characteristics.

Finally, segmentable groups are very important, using sophisticated, multivariate techniques based on demographics, psychographics, file enrichments, etc., we can segment and prioritize the file producing higher response rates and lower acquisition costs -- profit.

The final set of success factors relate to company characteristics.

1. Capital
   Mass marketing entails large up-front marketing expenditures to generate new business. Sufficient capital is necessary to take advantage of profitable marketing opportunities, effectively build a marketing base of prospects (internal prospect list) and insureds, and adequately test alternative approaches.

2. Functional Skills
   Ideally, key functional skills will exist in-house. To the extent they do not, a company may be able to develop the capabilities or purchase them from others. The key functional skills are:

   A. Efficient Administration
      Traditionally a high volume, low unit premium business, insurance mass marketing profit is very sensitive to "fulfillment" and administrative efficiency and costs. Over the long run, this factor will take on even greater significance due to increased price competition.

   B. Marketing/Copywriting Skill
      The ability to properly position the product for the prospect, prepare sales material, do campaign planning, and use market segmentation, etc. requires specialized skills in mass marketing. Effective marketing skills significantly enhance the profit and growth potential of a mass marketing operation.

   C. Effective Underwriting Screening
      Insurance marketing will always entail an element of risk of which the mass marketer must be aware. Because of the nature of mass marketing, i.e., high front-end costs to generate a response, it is always preferable to minimize the need for post-response underwriting. But whether it is through product structure, market segmentation, or underwriting screening, the need to guard against adverse selection must be satisfied to ensure a profitable mass marketing venture.

3. Image

The image of the insurance company has not played a large role in the growth of insurance direct response marketing until recent years. Most direct response marketing of insurance products has been by relatively unknown insurance companies that have relied heavily on the endorsement of organizations or individuals who themselves possessed high visibility and a good image. However, all agree that an insurer with a good image is a positive feature. The image of the company has taken on greater significance as the more widely known insurers expand into mass marketing.

To close and summarize, let's go through a direct response checklist.

Product Selection and Development: we talked about this in the strategic planning area as well as with regard to the critical success factors. This is where a company can make it or fail.

Direct Response Techniques: after products are developed the distribution technique(s) to be used must be identified. This should be the lowest cost, most efficient means.

Creative Development: we talked about this in the Direct Response process. This includes the execution of a campaign.

Testing: the lifeblood of direct response. Finding the right product, the right market, the right package or ad, at the right acquisition cost.

Fulfillment: within 24 to 48 hours or you can lose the sale.

Budgeting and Analyzing: be able to budget and analyze your results.

Customer Service: we did not talk about this very much, but this is critical. You must be able not only to fulfill the product(s), but service the business as well -- on an ongoing basis. You do not breakeven in year one. So you have to retain that customer.

Personnel and Vendors: knowing the functions is important, but you need to be able to work with internal and external resources. A direct response marketer will be a premium executive if you want to succeed in direct response.

MR. GEORGE C. COLLINS: The presentations you have just heard lent strong support to the tenet that not only can direct marketing be non-conflicting with the traditional career agency system but, in many cases, is designed specifically to support it.

Having said this, then why do so many of these marketing programs fail? Why are so many insurance and financial services companies signing on to the concept and then abandoning it so quickly?

One reason is that many have not been able to achieve their initial objectives in terms of all or some of the following:

Cost per policy issued, profits and/or return on investment. Still many more have been unable to overcome the negativity put forth by their agents; "negativity" I might add that verges on insurgence.

During the next few minutes I would like to review some of the typical problems inherent in establishing a self-supporting, self-contained, full capabilities, response marketing unit.

Direct marketing, response marketing, direct mail, target marketing - whatever term you use - the definitions describe a discipline. Disciplines have their own distinct rules which, if not followed or incorrectly applied, can and most likely will cause success to be elusive.

At this point, I think it important to point out that response marketing is not a new means of distribution, it has been around about a hundred years. What <u>is</u> new, is the application of the sale of insurance products to response marketing.

Herein lies much of the reason for its failure within many companies. To be specific, many organizations alter the basic principles of response marketing in order to make it conform to insurance products of a traditional nature, the reverse situation is what should have occurred-the products should have been modified to suit the distribution system.

The basic ingredients required to establish a successful response marketing unit fall into six (6) main categories.

1. The first of these is <u>commitment</u> - which by definition means to "devote unreservedly". Ideally to devote the time, money, and energy as required.

   This is not to imply that all other company projects should be shelved, or that response marketing should be given a blank check. What it means is that the response marketing program should be assessed and judged on the comparative cost of generating policies by other means, as well as its potential return on investment, as would any other business venture.

   Having done this, the company should commit the necessary human and financial resources for Systems, Actuarial, Underwriting and Administration support. Establishing an independent profit centre without assuring company-wide support can lead nowhere quickly!

   In addition, the commitment of these resources must occur according to a specific timetable. Many elements go into a successful direct marketing program, and if not accomplished by specific target dates, the project can die before it ever gets off the ground.

2. The next requirement I call "infra-structure sign-on".

   Again and again I've seen major insurance companies embark on a direct marketing exercise without informing the various subdivisions and support groups from the start. This can work to cross purposes, preventing the positive application of direct marketing techniques. Even before a decision to proceed is made, the various department heads should be involved in examining the implications of a direct response program.

3. Essential number 3 - Informing the agent.

   Contrary to popular belief, agents do indeed know what's going on in the Home Office - in fact, the quality, quantity and speed at which information is obtained through their internal espionage system has never ceased to amaze me. Therefore, it's a must in direct marketing to give some preliminary explanation to agents before any lengthy Home Office reviews and meetings take place - preferably as soon as the program is approved and certainly, before the first test is launched.

   I don't advocate replacing the traditional selling methods with direct marketing, and I do believe that the professional career agent will never become obsolete, although, it would be ridiculous not to acknowledge that the number of product lines and their customer profiles will never be the same again. Rather, it is my belief that each can support and be beneficial to the other. There can be no worse environment for direct marketing than one in which hundreds of individuals (agents) are working against an additional distribution system (direct marketing).

4. On to response marketing requirement Number 4 - Planning.

   Direct marketing is so much more than just mailing an insurance product to a prospect. The planning and allocation of time to see that the product is properly designed, and all the steps necessary for implementation are accomplished, is vital.

   The worst example I can offer is the situation where a mailing is successful, but because of inadequate planning, respondents do not receive their policies, premium notices, or any acknowledgement of their applications for 4, 5, or even 8 weeks.

   One company, that shall remain nameless, still cannot overcome a procedure which results in their applicants receiving policies only after first and second premium notices have been sent to their homes.

While we're talking about planning, I'd like to take a second to stress that direct marketing exercises should not be treated as sequential. The steps necessary for putting together a program can be worked on simultaneously. I can't tell you how often I've seen a mailing held up for lack of one element - say legal approval - that could have been accomplished weeks ahead, but instead was handled on a critical path basis.

5. One very key factor in successful response marketing is <u>costing</u>.

The special costing and actuarial concepts employed in response marketing have been touched on today, but frequently it's this area that causes difficulties and delays. Let's look at some of the pitfalls associated with costs -

A) First, <u>inadequate budgeting</u>. Direct marketing exercises that don't, from the start, take into account the full cost of a 5 year marketing plan will have start up costs associated with them that will make the whole concept appear unreasonable.

B) Second, <u>timing</u>. Missed campaigns cannot be made up. If a five year budget is based on gradually increasing mailings to a known universe of prospects, for example, mailing three times a year, then the loss of one mail date sets the whole project - and expected income - back as much as 6 months - while other expenses continue.

Direct marketing is unforgiving in allowing for catch-up procedures. You simply can not employ some of the traditional catch-up measures, such as involving more agents or running a sales contest in direct marketing.

C) <u>Response levels</u> further complicate the costing problem. Studies of profitability of insurance sales via direct marketing rely, of course, on the premium generated. But one factor that is often overlooked in start-up situations is the effect of seasonality on response rate, and therefore, on premium income.

Insurance, much like the sale of other products through direct marketing, has certain peak response periods associated with it. Although these can change around the world based on local holidays and the involvement of agents, response levels vary from a level that might be considered 100% down to 20% depending on the mailing dates.

Traditionally for insurance, January is considered 100% and December 20%. A delayed mailing - say a postponement from September to the low month of December - without adjusting cost projections - or decisions that do not take seasonality into account, can result in drawing the wrong conclusions from response marketing tests.

D) The effect of subsequent sales, too, are often neglected in the costing of direct marketing.

In examining the costs associated with the marketplace of the late 80's, it is essential to consider every direct marketing sale as one in a series. Rare is the product that can be sold by mail, generate enough profits and have such a low lapse rate that additional sales of other products and upgrades to the same customers are not a required part of the costing.

Many direct marketing insurance companies, in fact, rely on those secondary sales for most of their profits. That makes sense when you consider that response rates from a list of previous buyers of insurance by mail can be up to 5 times higher than responses from customers who have not purchased by mail before... or that upgrades offering extra quantities of the same insurance to existing policyholders can have take-up rates as high as 50%

6. Finally, a most essential response marketing ingredient - Product development.

It's exciting for me to address actuaries today because I hope many of you will, in the months and years to come, become involved in designing new direct response insurance products. They are very much needed. Too often we're relying on 50+ Whole Life plans, 24 hr. accident covers, small amounts of 5 year term, hospital indemnity plans, 50+ auto and homeowner coverages, RRSP's and IRA's.

The world of universal and variable life, annuities, special women's products, travel insurance, and savings vehicles is awaiting your attention, but remember not until your direct marketing unit has its foundation built with basic products.

Again, I would like to reinforce that this distribution system is not new. What's new is its application to insurance. Our job is to develop insurance products and services that fit the discipline. And many industry leaders have already.

Shearson/American Express didn't purchase IDS without realizing that their lead program mails over 25,000,000 pieces a year to support their agents. Prudential in the U.S. quickly capitalized on the 14,000,000 plus senior citizen names available for endorsed insurance offerings through AARP. Metropolitan Life hasn't gone into a joint venture with National Liberty without thinking about the technology that they are acquiring... The list goes on.

Direct marketing has achieved respectability worldwide in the insurance community, and many have been able to overcome the problems associated with its implementation. All new methods of reaching our ultimate customers must be explored and careful attention to detail will make direct marketing one of the major methods of selling financial products in the coming decades.

MR. WALTER W. SIEGEL: The middle of last February I was placed in charge of a small direct marketing group. We have a couple of years worth of experience in this group. My question is this, is there some literature or publication which you could recommend that I turn to as a source for measuring my results? This would be helpful to me in allocating what money I am going to spend the future.

MR. JAFFE: Do you mean, is there a published source which states your results have to be an X percent return? Or, are you looking for guidance in comparing your returns to other product ventures?

MR. SIEGEL: I would say both of those. I am really struggling at how I can begin my task.

MR. JAFFE: I would recommend certain things to you. Not only is the Society forming a non-traditional marketing section which is going to get into some of this, but there are other trade groups around which hold meetings you might want to attend. There is the DMMA now meeting in Chicago, don't all rush out to a plane, but that's going on and part of that group is the DMIC (The Direct Mail Insurance Council) and you might become acquainted with some of its members. There are several books, good direct response marketing text books or informational books, that are out that provide good background and good general reading. The key thing is, I believe, that you're going to have to take your situation and look at it very individualistically. I don't think you can broadly generalize, because I don't know what your profit parameters are. There are definitely ways of determining whether your business is profitable or not, but it has to be done looking at your situation and your cost structure.

MR. ANDREW M. PERKINS: I would like to touch on a couple of your comments with respect to why direct marketing might be appropriate in some circumstances. You mentioned complicated products. I was under the impression that a complicated product might require agent involvement to answer the customers questions, help explain it, help service it, especially in circumstances where there is flexibility in the product (i.e. options for the customer to choose from) that are difficult to present, say, in a mailed piece or advertisement. I wonder, therefore, if you can explain why you feel that a complicated product might be better marketed through a direct response technique.

MR. JAFFE: Several reasons. One is that you may have an agency force that itself does not understand the product and finds it difficult to convey to the public - they make more out of it than need be. I have seen some marvelously simple life insurance demonstrations done through direct response which make it possible, without the aid of face to face contact, to generate universal life sales which are considered by many to be too complex for direct response. I think it is possible to break that product down to a very simple form. There are ways of combining some of these things. A complicated product to one agent may not be a complicated product to another. Automobile insurance to a life agent can be very complicated. It can be something that they just will not sell, there are too many options, such as in homeowner's insurance. You can do these using direct response, using the assistance of the telephone and the mail. When you put them together they really make a very simple presentation.

MR. SELIG EHRLICH: You've stated that a direct response marketing program can help promote products not actively sold by agents for reasons such as small commissions or lack of prestige. Of the typical direct response products mentioned, IRA's seem to fit the bill especially for agents of a multi-line company. You've also said that a necessary ingredient for the program to succeed is active agent participation. How do you get agents to actively participate in the program, if in fact they have been unwilling to sell the product to date for just these reasons?

MR. JAFFE: One of the things you could do, and I've seen it done successfully, is use the technique of finding a small number of agencies who are willing to work with the Home Office. As soon as their colleagues find out that you've developed a program with these agencies that is developing X dollars worth of commission, other agents will call with interest in the program. That's a very good technique to use. Find a couple of test areas. Find a couple of people that are a little more receptive to new ideas and concentrate your efforts on them. If you can develop a successful operation with that small group, they, themselves will disseminate their success story to your field force and you then have everybody asking for it, rather than you pushing the unknown. Not only that, but it allows you to work out the kinks. It's extremely difficult to start a program for a company and implement it for hundreds or thousands of agents without having worked out all of the bugs before you introduce it. You therefore should start small, and then, if it's successful, word will get out.

MR. PAUL F. DELLA PENNA: What importance would you attach to being among the first companies in direct response in your market? Some of the people in my company think that it's important to be the first because the market is not well developed in Canada. Their feeling is that if we wait too long, other people will get there first and our efforts won't be as effective.

MR. COLLINS: I guess like anything else, that's an envious position to be in, first in the market. But I'd rather do it right, let other people make the mistakes. More companies have failed at direct response marketing because they've hurried into it. I'd rather make sure it was done correctly (i.e. with the proper budgeting, planning, etc).

I was involved with a firm in the U.S., one of the top companies in the U.S., and I know they allotted a budget of $100,000 to look into response marketing. Not $90,000, not $125,000, but $100,000 - to them that was the right amount. In the end if it had failed, what would they have learned - that $100,000 did not give them the answer? And if it had succeeded, where would they go from there? The bottom line? - I don't think being first is the all important issue.

MR. JAFFE: I disagree. I think my disagreement though is positive, not negative. If I were in a situation as you described, I think being first is very important in order to establish market position. There are many groups who can only deal with one company. Therefore, to amplify a little bit on what George is saying - "do it right," but my feeling is do it first, and do it right, don't wait around!

MR. BALDWIN: One additional comment. I don't feel you can always be assured that you are the first one in any market. I think front-end market research will tell you whether you are the first or not. It could be that there are several other companies positioning themselves in your marketplace, but in a different manner.

MR. WILLIAM J. BUGG, JR.: What sort of range would you expect to see in response rates. Could you give some examples? ....What's low?

MR. JAFFE: Response rates are driven by many factors - nature of the product, complication of the product, price, etc.

MR. BUGG: Would you expect reasonable rates of return on an IRA solicitation?

MR. JAFFE: No, since you can get a better deal from a bank. The bank can essentially sell it as a no-load product.

You, on the other hand, can't add the cost of distribution on the same way that a bank does and come out ahead. The bank will take all of its acquisition costs and spread them across all product lines. In an insurance company, as you know, if you start adding the cost of an IRA program directly to the program itself, there is no way you can sell it as a no-load product. If you have not as yet examined this, it is a very simple exercise.

MR. BUGG: I am still having a problem establishing the proper gauges for measuring success in direct response. Can you give examples of what would be considered reasonable response levels?

MR. COLLINS: The question of "appropriate" response rates is a difficult one. What you're really talking about is profit level. After all, that's what counts! It's the cost per policy issued, not the number of people responding per thousand pieces mailed, that is the real measure of profitability.

MR. JAFFE: To more directly address your question regarding response levels, companies like J. C. Penney and Sears & Roebuck can exist in the U.S. with response rates of .2% and .3% for a traditional life or hospital cash program. Other insurance companies are getting .9% to 1%. The profit structures of the two are probably identical. Response rates are very deceptive. Acquisition costs are what's important. How much of the first year's premium can you afford to spend to put that policy on the books? Certainly, if you need a response rate of anything close to 3% or 4% in the U.S. using a mailing piece and no agent involvment you are in trouble.

MR. SAMSON: Just a quick war story. We had a client who wanted to test direct response in an auto coverage product. They kept asking, " what response rate do we need". We kept saying you have to look at allowable acquisition costs. We did some testing and research for them and came up with what we thought they could achieve. They, however, never developed the back-office to fulfill and service the clients. Since we underestimated the image of the company, response rates were higher than expected. The company couldn't wait to tell us, "you're wrong, we're not getting X percent, we're getting a little bit better than that". Their conversion rate, however, cut the net response rate by 75% because of their inability to fulfill, their inability to quote on line. The bottom line here again is not the response rate, it's your unit acquisition cost. What's your allowable acquisition cost? - that's what you have to focus on.

George mentioned some companies. Of the companies he mentioned, some have internal resources that some of you do not have. J.C. Penney, for example, has its credit card file, a tremendous universe. It's a file with very favorable demographic and psychographic characteristics. With this type of raw material to work with, they can generate very predictable results. Their concern, however, is still with acquisition costs, as it should be.

MR. THOMAS C. FOLEY: Each of you mentioned marketing complicated products through direct response. Can you point out a success story of someone who is doing this now? I'm talking about a Universal or a Universal Variable life type product. Is not what's going to happen in the next few years to the product and to various marketing techniques going to allow this variety of product to be successful.

MR. COLLINS: I just want for a second to again touch on those words "complicated product". Let's leave the specifics of insurance and talk about response marketing and direct marketing in general. You can't sell something through direct marketing that isn't unique or different. If it can be purchased down the street, certainly most people are not going to go through the trouble of buying it by mail. If an agent is calling on an individual every week and has exactly the same product they will buy it from an agent. It has to be different. Not necessarily complicated in terms that an actuary would look on as complicated. That's a marketing definition of complicated. From an actuarial point of view the product can be very simple. Like whole life insurance for someone over 50. It's just regular old whole life insurance.

The universal life, variable life, or the new savings vehicles which are entering the market today have not seen much direct response activity. That is because in a response marketing venture, as Len pointed out earlier, you can't allow the consumer to make too many decisions. Without the benefit of an intermediary, an agent, the consumer will not singlehandedly go through more than one or two decisions in a mailing kit purchase. They'll make a decision on some supplemental insurance, but the number of variations available in universal life or variable life by its very nature typically prevents sale by mail. I think, however, that it will be done. Someone will make the breakthrough necessary for this type of sale. The Hartford is conducting an experiment on the West Coast using the telephone to sell universal life. They are doing quite well, but that's using an intermediary. A licensed agent is on the phone and although that's using direct marketing techniques, I wouldn't say it was a "pure" direct response venture.

MR. JAFFE: We seem to be addressing the same thing from slightly different points of view. George, I would call that direct response marketing, although there is an agent. First of all, that agent is a specialty agent, probably trained in the techniques of how to use the telephone and direct mail. It's a different type of direct mail. USAA is successfully marketing universal life through the mail, through the media, and through their representatives. It's a two step process, but it is direct response. There is no agent who comes and sees you personally, nobody has to scratch on a piece of paper, nobody has to present the ledger sheets, it's all done via the mail or telephone. It's done extremely efficiently and it seems that they have a very unique marketplace. They have also adapted the products to the marketplace.

That's another point I want to make. I don't think if you're going to use direct response, no matter whether it's one step, two step, whether it involves telephone, mail or other media, you need to limit the number of bells and whistles in order to obtain the proper market penetration. You can only get so much on a piece of paper. You can only get so much content in a TV ad. You can only get so much expressed during a telephone interview. You can't emphasize every feature. You have to pick and choose those which you feel are important to the sale.

MR. CLAUDE THAU: Would one of you like to comment on the thesis that the affinity groups, at least several of them, are getting wise to the profits of direct response and are going out to insurance brokers to get anywhere from a dozen to two dozen companies to quote on the same deal. They are, therefore, making this into a buyer's market. If you're dealing with that type of scenario, what ability will a company have of holding onto the business in the future?

MR. SAMSON: When you said "to bid on it", are you talking about going out for bids to find an insurance company to be the endorsed carrier? I've done that with many clients, not just AARP. What it does is get the best deal for the member and that's what my affinity groups are interested in. In all honesty, they want to provide the best product to their members. The best product may mean lowest price or it may be determined by product features. This can be done while still providing an incentive to the insurance company.

MR. JAFFE: If they proceed to squeezing all of the profit out of the programs, which is what I think you are asking, they will have but one alternative left, that will be to have their own insurance companies. They will probably be mutual insurance companies which are taxed rather unfavorably under the new tax law. Given that, they will eventually demutualize and the whole thing will become a vicious circle. I think you are presenting an interesting thesis. That, however, I feel is just part of the cycle of the marketplace.

MR. THOMAS P. GILLETT: I'm interested in some comment from the group regarding people joining affinity groups simply to purchase insurance. As an example, perhaps it is the Joggers Association with a $10 annual fee. The insurance company factors in that they are "joggers" and offers a fantastic package. Would you have any comments on the dilution effect of offering an insurance product to these "affinity" groups?

MR. COLLINS: I was an officer of Colonial Penn prior to its losing the relationship with AARP. Len's firm was the firm that was asked to put it up for bids. Why did that take place? Partly because the association and the insurance company became too close. In many cases the insurance that is available through groups like that, isn't the best the group can obtain since the group is controlled by the insurance company. While it may be a trend, I'm not concerned with it.

MR. GILLETT: Are you saying then that it's not a good idea to market through an affinity group with an inexpensive fee such as the Joggers Association?

MR. JAFFE: If you look at it another way, I don't think the affinity for the insurance endorsement is going to be great. I'd rather market to a group that had the highest possible fee (anyone but the Society of Actuaries). The members would then believe in the endorsement. If it has a low fee, your response rates, profit, and acquisition costs are going to reflect it.

MR. ROBERT LYLE: One point which hasn't been touched on is the importance, in terms of results, of the endorsement of the affinity group or financial institution. I was wondering if one of you might comment on the degree to which success may ride on the sponsorship of this type of organization.

MR. JAFFE: Let's look at traditional selling methods. The combination of a fine salesman with a fine company is a strong endorsement. In response marketing, we're going in without an agent. We want the strongest possible endorsement for insurance just like the one the agent more or less has in his pocket. The strongest endorsement will be one that's of a financial nature; a bank, a loan company, something that's telling people how to manage their money and their future. We always rate them as the highest possible affinity groups. After that, we move to groups that have an affinity with some other portion of the prospect's personal life. This would be your AARP, retired officers, various associations, veterans groups, etc. In summary, the level of endorsement is of paramount importance in response marketing.