RECORD, Volume 24, No. 3
New York Annual Meeting
October 18–21, 1998

Session 56PD
Bancassurance: A Global Perspective on Customer, Products, and Distribution Methods

Track: Nontraditional Marketing
Key Words: Economics, Finance, Marketing

Moderator: JAMES B. SMITH, JR.
Panelists: JACQULYNN ABDELLA
JOHN O. NIGH
JAMES B. SMITH, JR.
Recorder: JEFFREY A. KLANDERMAN

Summary: The discussion approaches bancassurance from both the insurer's and the banker's perspective and covers the following topics:
- *Insurance products—what are the proven and emerging product lines?*
- *Bank distribution subchannels—what methods of distribution or subchannels are banks using to sell insurance and why?*
- *Matching of customer needs, products, and subchannels—what is the optimal matching for maximum profits?*
- *Marketing support—what competitive advantages does marketing support offer bankers and insurers?*
- *Profit-sharing arrangements—what different types of profit-sharing arrangements are in use between banks and insurers and how have they evolved?*

Mr. James B. Smith: During this panel, we will be discussing Bancassurance: A Global Perspective on Customers, Products, and Distribution Methods. I'd like to introduce our speakers at this time.

Jackie Abdella is with the ING Group in Amsterdam. She's in the corporate actuarial area in risk control and has oversight responsibilities for all the worldwide insurance operations within the group. Incidentally, ING is the result of a merger of a bank and an insurance company, which seems appropriate given our topic today. ING is an integrated financial service company.

John Nigh is a principal with Tillinghast-Towers Perrin. His responsibilities include the Latin American operations with offices in Rio De Janeiro, Sao Paulo, Buenos Aires, and Mexico City. John's areas of expertise include mergers and acquisitions, reinsurance, bancassurance, underwriting, and financial analysis.

Jackie will be presenting the European perspective in our discussion, and John will be presenting the Latin American perspective.

And I am in the Birmingham office of KPMG Peat Marwick. I'll be dealing with the U.S. perspective on bancassurance. I'm a consulting actuary in Birmingham, and I deal with both product and distribution channel development for insurance companies and banks. I want to thank Jeff Klanderman who's a new FSA at this meeting and serving as our recorder. Also, Carl Meier who's the vice chair of the Nontraditional Marketing Section, is the one that really promoted this meeting and my thanks to him for that. The Nontraditional Marketing Section and the Product Development Section agreed that there will be a seminar preceding the May meeting in Atlanta that will deal with the issue of bancassurance. That seminar will include more detail on some of the topics that we will cover.

I'm going to kick this off with a U.S. perspective. Bancassurance, for me, is a very exciting topic. I think it's also very timely given the sales volume that is now being generated by banks, the publicity of the Travelers/Citicorp combination, which has now been approved, and also the progress in the legislative arena. The HR10 legislation came very close to being passed by Congress, but it simply ran out of time.

One way of looking at bancassurance is to develop a new word to describe it. We oftentimes think of it as co-opetition which is a combination of the words cooperation and competition. I think that's pretty symbolic of what we may have here because insurance companies obviously have a lot in common with banks, but there is an underlying element of competition for similar customers. In terms of a co-opetition arrangement or the Bancassurance arrangement, there are at least two parties. On the one hand, there are banks, thrifts, and credit unions, and, on the other hand, there are insurers. There are also other parties that may be involved. Oftentimes, a third-party marketer gets involved, and sometimes a third-party administrator does as well.

Bancassurance includes all types of insurance. When you talk to a banker and you indicate that you have an insurance background, they can gravitate to all sorts of areas outside life, health and annuities, not the least of which is property and casualty insurance. You can also get into some other areas like title insurance and private mortgage insurance. So there's really a broad range of products.

In looking at the U.S. landscape, I thought I might start out very briefly talking first from an insurance company's perspective on why bancassurance makes sense. Then I'll speak from the perspective of the bank itself.

Bancassurance for an insurance company provides an additional channel of distribution, but I think what is more important is it provides a channel where there's very frequent customer contact. Because of that customer contact, there's a high degree of trust in that distribution channel between it and its customers. An insurance company would look at bancassurance to provide some incremental customer penetration. This is not only penetrating additional customers for the insurance company, but it's also a penetration of some unserved and underserved customers to which the bank may have greater access. There also the matter of improved pricing dynamics from the point of view of an insurance company because there are multiple relationships between a bank and a customer. The persistency should be high and the lapses should be lower. That may have a very positive effect on pricing of the products.

From the perspective of the banker there are certain drivers that are both analogous to the insurance company's perspective and somewhat different. One of these is the issue of reduced margins on the bank's traditional banking products. Banks are experiencing pressure on spread much like insurance companies. Consequently, the bankers are looking for additional ways to supplement their reduced margins. Furthermore, they're looking at ways of protecting their customer base. This is a defensive posture. Banks are very concerned about disintermediation by other banks, by insurance companies and by broker dealers.

I also want to mention that many banks are looking at providing a range of one-stop full financial services to their customers. Bankers envision that a customer could not only have the traditional banking products, such as checking, savings, and loans, but there are also a variety of insurance products that would complement some of those transactions. An annuity looks similar in many respects to a CD. Automobile insurance is a natural complement to getting an automobile loan, as homeowners' insurance is to getting a home loan. These are some of the complementary benefits.

A nonfinancial benefit for the bank would be to provide more services to the bank customer. An obvious benefit from a financial perspective is additional revenue. Linked with that is the issue of the bank trying to make its relationship more complex with its customer. I'm talking about having more relationships and making it more difficult for that customer to leave the bank, which, in turn could lead to lower defection rates.

To give you an idea of the expected gross revenues that a bank might have, a survey that was released just a couple weeks was based on interviews of several hundred banks of all sizes, and determined that with the bank sales last year 70% of the sales dealt with annuities, 10% with credit insurance, another 10% with property and casualty on the commercial side and about 7% with personal lines property and casualty. As I said it's relatively new information, but again it shows that the annuities are the big play. With the 10% on commercial property and casualty, and 7% on the personal property and casualty lines, you can see that these are growing areas of interest.

What roles might the bank play and what roles might the insurance company play? Traditionally, if we can use that word for a relatively new market, the bank has been the source of distribution, whereas the insurance company has been the risk holder and the manufacturer. By manufacturer I'm referring to both pre- and postfunctions of servicing the business. What we're seeing now is more of a blend where the bank continues to be a distributor, but they're taking on some of the manufacturing functions. An example is a bank opening a phone center that covers insurance products as well as its traditional banking products. Some banks are looking to get involved with some of the non-cash transactions, and I suspect at some point they'll be getting involved with some of the cash transactions as they might relate to insurance. Of course, the future configuration, as in the Travelers example, is where the bank holding company might accommodate all three functions: the risk holding, manufacturing, and distribution.

I want to touch on the matter of market triangles. When defining a market, you use three components. You have the customer products and channel. The customer is the one that obviously generates the financial need. The product then fills that need. The last thing to be determined is how do you channel the product to the customer. The obvious reason for wanting to align these three components is to maximize the profitability, to maximize the sales penetration, and also to satisfy the customer.

I would like to give you some examples of some market triangles. The most productive opportunities at this point are older savers who are looking for ways to accumulate savings on a advantaged basis. They purchase fixed annuities from platform personnel. *Platform personnel* is a bank term for those people that you would find in a bank lobby. They would be people who sit behind a desk, who might write a CD, and are typically knowledgeable about 50 to 60 bank and insurance products. They sell insurance on a part-time basis, along with all these other products. There are more banks now that are moving into variable annuities either through their broker/dealer, or by having some of their platform people being Series 6 or Series 7 licensed.

There are other examples of market triangles. Some of you may work with multiple-line companies. Some of you might consider a joint venture with a multiple-line company to be able to present an entire package of insurance products to the bank. As a bank looks at these market triangles, they're going to be looking at ways to phase them in. Quite typically the banks would already be in credit insurance, so that's a non-issue, but they might be looking at starting with annuities. Some banks don't want to start with annuities as they feel much more comfortable with property and casualty, so they go that route.

Now let's look at the three pieces of the market triangle. Once again the triangle consists of the customer, product, and channel. Let's look at the customer first. There was a survey done in the last couple of years that showed some factors that influenced customers as they considered purchasing insurance from banks. The top three factors were trust, convenience, and one-stop shopping. I do think that the convenience and one-stop shopping are very much interrelated. It's also interesting to note that low price ranked relatively low. I think that's fortunate in the context that banks are not looking for the lowest commission percentage. They're not necessarily looking toward the very most value to their customer, or to increase revenues, or to provide a convenience sale and maybe a one-stop shopping sale. As banks look at products, they're not looking for the lowest-priced product. That's not to say that they're looking for products that don't provide substantial value, but the products do not necessarily have to be the most competitive.

One study determined the likelihood of a customer purchasing life insurance through a bank segment (private banking, new investor, personal banking, convenience customers, value customers). Given these customer segments, which were based on income and age, the bank was able to develop various demographic and physiographic characteristics that help them determine the financial needs for that customer segment. When the customer comes into the bank, the bank is able to pull up the customer on the screen. Table 1 includes the customer's profile segment information and some ideas of what types of bank and insurance products this person might be receptive to.

TABLE 1
LIFE INSURANCE CUSTOMER SEGMENTS

Segment	Likelihood
Private Banking	13%
New Investor	14
Personal Banking	11
Convenience Customers	16
Value Customers	11

One other segment that I want to mention is the segment dealing with the unserved and the underserved market. These are some statistics from the ACLI MAP study, and it shows the percentage of the American public that does not have a personal life insurance agent. The percentage is pretty high. It is hovering around 70% at this point. In 1989 it was at about 69%; in 1984, it was 59%; and in 1979, it was 60%. Many of the potential insurance customers are people with a banking relationship. I had a banker once say 70% sounds high for the higher net worth people. Wouldn't the percentage be much lower? I looked into that and for household incomes of over $75,000 the percentage without an insurance agent is 57%. It's still a very significant percentage.

The top categories of insurance policies sold by banks include fixed and variable annuities, credit and mortgage life insurance, and accidental death. There are also products that aren't on this list that can be very important to a bank. They can provide a good source of revenue without a lot of external marketing. Examples include title insurance and private mortgage insurance. Private mortgage insurance is sold when the down payment on a home loan is less than 20%. There are other products that are more specialized like environmental risk insurance, where the insurance will reimburse the lender, which would be the bank in this case, if there's an environmental risk that puts the loan into default. So there's a wide array of insurance products that banks are looking at.

Where were insurance premiums sold by banks in1996 as opposed to 2001, as a percentage of the total market? Annuities have taken off already. During this period of time, the bank share of the annuity market might double. For life insurance, the growth might be five times higher and for property and casualty ten times higher. This begins to paint a picture of the growth areas. Of course, with credit insurance you can see a fairly level percentage of the market total because it is a more mature product.

The fixed annuity market is one that has represented large percentages of the sales through banks because you don't have all of the registration requirements and training requirements that exist for a registered product. The bank sale of this product has been increasing over the last couple of years; however the product, in general, has been decreasing in dollar sales because of the low interest environment that we've been in. In the area of variable annuities, the banks' share has grown. Many of these banks have a broker/dealer operation where the variable product fits nicely with product offerings of their registered representatives.

I did want to mention that some of the property and casualty products that are being sold represent a real opportunity for a life insurer because, in some cases, banks are really looking for the whole package. They would like to be able to sell a wide variety of life products as well as property and casualty products. There are insurance companies that either can do that within their own organization, or they're looking for some joint venture arrangements that could allow them to offer the whole spectrum of products.

In terms of life insurance, the percentage of the total market being sold by banks is relatively small (maybe around 1–2%). Annuities are a natural step for a bank to move from the sale of CDs into the sale of annuities, particularly fixed annuities. Life insurance, being a mortality-based product is a bit more difficult because of the sales training. Banks are leaning more toward writing tickets for life insurance and passing the tickets along to the insurance carrier. The carriers then follow up with the applicant over the telephone where the application is completed and medical exams are set up.

The banker has some further concern about the outcome of the underwriting and the outcome of the settlement. The settlement outcome is more of an issue with property and casualty. The underwriting outcome could be adverse to the bank and its relationship to the customer.

I also want to mention some of the various subchannels of bank distribution. This is the third piece of the market triangle. Banks are not a monolithic channel by any means. There are probably 20 plus bank subchannels that I've seen in the U.S. Some of these involve bank employees. We've already mentioned the platform personnel. Dedicated specialists are those people that spend 100% of their time selling different types of insurance products instead of selling traditional bank products. Sales can come from different areas within the bank. The trust department has access to high-net-worth people, as does the private banking area. You can also get sales or referrals from the consumer lending and commercial lending departments.

Some bank employees might be part of a bank-owned agency that might be an operating subsidiary of the bank or the bank holding company. Sometimes sales are done by third party marketers who are either regional or coast-to-coast. Sometimes sales are done through a joint venture with a local insurance agency.

The bank's preference for distribution channels will depend on its culture. Oftentimes, in starting up, banks will lean toward a third party marketer since the marketer has the expertise. The bank may then internalize the operation once it hits critical mass.

Other banks prefer to purchase an insurance agency with an existing block of business. The marketer may serve simply as a manager of the marketing and sales effort and not provide the insurance agents. There are other situations where the third-party marketer not only manages the insurance agents in terms of marketing and sales, but also provides the agents. There are a lot of different combinations in the way in which these distribution channels can be structured. Many of these third-party marketers have been purchased by insurance companies in the last couple of years because the insurance companies are wanting to capture more of the insurance role.

Direct marketing on the Internet is an area that banks are exploring for the computer-literate customers of the bank that already do a lot of their banking transactions via the PC, mail, and telephone. This may allow the banker to tap into the unserved and underserved markets.

Having talked about the market triangle, I want to list the variety of profit-sharing arrangements between an insurance company and a bank. I've included in profit sharing-arrangements trailer commissions and renewals because that is a type of profit sharing. There are other traditional arrangements, which include leasing arrangements where the insurance company leases space in the bank lobby.

- Trailer/renewal commissions
- Leasing arrangements
- Proprietary mutual funds
- Convertible life and annuities
- Fixed life and annuity asset management
- Contingency commissions
- Commission factoring
- Experience-rated agreements
- Reinsurance
- Joint Venture
- Agency acquisition
- De novo agency
- Acquisition of an insurance company
- De novo insurance company

There are some nontraditional approaches that might include the management of assets on the bank's fixed life and annuity products. There can be some experience-rated arrangements between a bank and an insurer. This would not be reinsurance, but it would share the outcome of the experience, maybe just on the upside, or maybe on the upside and the downside.

Reinsurance is another avenue for profit sharing, but it's limited, except for some grandfathered banks, to credit insurance.

I might mention that a de novo agency, from a bank's perspective, means a new agency, but it doesn't necessarily mean new agents. Because bankers are very interested in using agents with experience, oftentimes the head of that agency will be somebody with ten or more years of experience and a lot of the agents would have five or more years of insurance selling experience.

There is an incremental approach to profit sharing. A bank doesn't usually go from being a distributor to being a manufacturing and risk holder. Banks will take certain steps that, for them, seem natural, and will allow them to get gradually involved in the insurance business. Some of these steps obviously are passed or stepped over, but sometimes the banks will just go from one step to another as it gains its experience and feels more comfortable on the basis of their experience.

Ms. Jacqulynn Abdella: It's now time to take a look at the European perspective on bancassurance. The developments in that market, especially since the early 1990s, have been quite significant. To give you an example, the growth in France has been absolutely phenomenal. A few years ago, bancassurance wasn't a significant channel and now you see bancassurers accounting for over 60% of the new premiums. In the Dutch market bancassurance is categorized by large mergers between banks and insurance companies. Based on my experience during the past three-and-a-half years in the Netherlands, I've found that the European market differs quite a bit from that in the United States. I hope that in my presentation today I will be able to highlight a few of those differences, because I think a lot of these are the key reasons why bancassurance has had the success it has had in Europe. Before continuing I want to make a little clarification on what I mean when I talk about bancassurance. To many people this term purely means the distribution of insurance products through a bank. However, in my perspective, the definition is much broader. It includes things like strategic alliances, the mergers between insurance companies and banks, each one a holding company, moving all the way to fully integrated financial service companies. I will take this broader view.

One of the things that I've found is that within the European market the statistics that are available are quite limited. The focus of this session is on customers, products, and distribution channels. For such information to be valuable, you really need to understand what has been happening in the European bancassurance market. Thus I'm going to try to highlight the information by looking at the rise of bancassurance in the European market and looking at the structures that have taken place. What have the driving forces been behind the product? Then I'll take a look at how the insurers are responding. I'll then highlight the status of bancassurance in certain European markets. Finally, I'll give my view of what the future holds.

First some general comments. The development of bancassurance within the European market has varied significantly from country to country. The maturity of the market, customer preferences and demands, and regulatory factors have all led to different forms of bancassurance across Europe. Although the future may lead to one unified Euro market, the past has been quite unique. I caution against making any generalizations on Europe, but examining market penetration will give you some ideas. As I've already mentioned, bancassurance in France has been quite successful. Over 60% of the new life sales are written by banks. Emerging markets have also shown very strong potential. Typically there are vast segments in these markets that are underserved and banks have been able to capture them. In the mature markets we're tending to find that there are more established relationships with an insurance agent; products tend to be more complex and bancassurance is not seeing as significant growth as it used to see.

Now let's look at some of the structures that bancassurance has taken. The first one, which I really consider the pre-bancassurance stage, is distribution by banks of products of various insurers. This has been common practice in Europe for several decades.

The next stage in the structural evolution is the development of strategic alliances. The strategic sense is that of a distribution alliance. These alliances have allowed for the combining of marketing and other activities between the partners. Sometimes these alliances are reinforced with cost share holdings. This tends to create more financial incentives for the deals. The alliances can be both the distribution of banking products into insurance and also the distribution of insurance products through banks. The latter method of distributing insurance products through banks has been much more successful than the other way around.

One of the difficulties with such alliances has been determining how to distribute the profits. Also there can be difficulties with cultural differences between the partners. For example, we find in the U.K. market that when you begin with alliances, banks are not opting to set up their own insurance companies. In other markets, banks have just gone directly with their own Greenfield operations. A stock start-up approach has been cited as being the most successful. This is especially true when banks have done their homework and choose their target markets well. Such an approach is most easily accomplished in a market where the insurance is still just emerging. You tend to have fewer relationships already existing, the products can be much simpler and the banks have much greater ease entering the market. Another advantage of setting up your own operation is that you can organize your structure such that you can avoid some of the cultural differences that happen in a merger.

Alliances and start-ups are tending to be most practical when your main goal is purely expanding the products that a bank can offer. When your ambitions are much greater than that, you tend to move to things like mergers and acquisitions. Another structure that's been somewhat common, especially in crossborder relationships, is the joint venture. Typically a bank and an insurer set up a joint venture to start up a new operation. An advantage of this is that the banks gain the expertise of the insurer.

Finally, let's move to an integrated financial services group. At this stage the opportunities and objectives become much more far reaching than just selling the insurance products through banks. There are many opportunities for synergies whether this be in staffing expenses, product production or asset management. ING is one example of such an organization. Within ING, the main objective is to play a role in every stage of the flow of funds, whether it be retail or wholesale. In my view, the future lies in being able to serve customers via their desired channel with the products they need. This will require multi-channel distribution and the ability to creatively combine insurance and banking products to fit the consumers domain.

Let's consider the forces behind the rise of bancassurance in Europe. First there was a relaxation of the regulatory barriers that kept banking and insurance separate in the late 1980s and early 1990s. Banks can now take a much more proactive approach to the insurance market, including ownership of insurance companies. Banks have many offensive and defensive reasons for doing this. The fact that banks can own insurance companies is one of the major differences from the U.S. market. I'm going to go briefly through these offensive and defensive motives since Jim has covered some of them already.

We've covered the fact that the distribution via the bank channel tends to be much cheaper, which I call superior distribution economics. You basically get warm leads, you have a higher hit ratio and you have much more customer contact, which tends to result in much higher productivity for the effort. I've seen some studies that show selling insurance through a bank can be up to 50% cheaper than via the traditional insurance agent in Europe. There's also a huge growth potential for the European market and this comes from two main factors. First, the demographic changes where the population is aging and tending to save more. Second, is the retraction of social security benefits or social security programs that the governments have typically provided. This is leading to much more private funding of retirement savings. Finally, one of the other motives for banks to enter is that they've had access to markets that typically insurers have not been able to get to. An example of this has occurred in France and also some of the emerging markets where there are vast segments that have been underserved by the insurers. Insurance has tended to be something more for the wealthy while the middle class tends to go uninsured.

There are also defensive motives and I think Jim has also hit on these. There are declining profit margins via competition so banks are seeking new areas for revenue. Then you get into the question of whether banks are seeking a new area for revenue. Is it better that they own the insurance company and get all the profits or that they enter some sort of alliance and share the profits, but have much cheaper start-up costs? The second reason is that consumer preferences are really shifting away. Bank's clients are going away from just wanting savings deposit type products and moving much more into other forms of savings-oriented long-term life insurance or other investments that tend to have a higher yield. This shift, as we see in Europe, tends to coincide with demographic changes and changes in retirement savings patterns.

Another driving force behind bancassurance has been the advance of information technology. Banks have vast amounts of information on their clients and the advance in technology has allowed them to tap that information and really use it to do effective targeting of clients and get much better leads.

Another factor in the European market that really cannot be overlooked is the privatization of the postal banks. Postal banks tend to have huge client bases; nearly everyone has an account at the postal bank. These offer a vast market potential and it has really been one of the areas where we've seen the banks enter into direct marketing distribution.

There are many forces that have led banks to look into bancassurance which have created some advantages. We've already mentioned banks have large customer bases and access to a lot of information. They have effective cost distribution, and they have the direct client access Jim has referred to. The banks tend to have better image and brand recognition. The perception of the public is much more positive towards a bank as a financial service provider than it has tended to be toward the insurers. One comment I wanted to make about direct client access is that I think you tend to see the access declining somewhat as you have electronic banking and Internet banking emerge. For instance, you can bank through the internet. I think that trend has been much slower in Europe than it has been in the U.S.

Banks tend to have superior sales and marketing experience and also the effective targeting of the customers based on the quantity and quality of the information they have. One other advantage that the banks are bringing to the market is as they come in as a new entrant, they have the ability to take a fresh look at the market. They can take a look to see who their customers should be, what products they need, and how they can best get those products to the customers.

In order to understand a little bit more about the rise in bancassurance, I thought I'd take a little step back and talk about what the markets have been like in Europe. I think we should categorize them into three stages because the stage of development of the market has really affected how effective the bank's penetration into the life insurance market has been. The first stage is what I would call an emerging private, life and pension insurance market. In these markets, state-funded pensions still are very common, although in many cases they're underfunded. Markets such as France, Spain, and Italy are examples of such markets. It has been relatively easy in these markets for the banks to enter and capture market share. There are typically vastly underserved markets, and they can be reached with very simple products sold directly through the bank branch. The simplicity of products has also allowed the banks to get into insurance and have sort of a learning curve to figure out what really works. In some cases they needed to add a specialized sales force. We have found that in such markets start-up operations have been the most successful.

The second stage is where you start seeing the pension markets deregulate. What you see is there is more demand for private savings and an increase in the demand for life insurance products. At this stage the customer is in need of and really starts demanding advice in their financial planning. We find the insurers in an opportune position to provide such advice. They understand the more complex products and they've been in the business of providing this kind of advice before. Insurers are also better prepared to react competitively when the banks start to enter their market. A specialized agency force in the bank is typically needed at this stage to sell the kind of products that are required. Strategic alliance, joint ventures, and acquisitions tend to hold more promise in such markets, because they allow the bank a steeper learning curve.

The third stage is what I would call a mature private pension market. There are large private pensions existing, especially in the group property and casualty corporate lines. Typical markets in this case would be the U.K., the Netherlands, and Switzerland. There's a high demand for pension products. Strong relationships exist with the insurance advisor and these factors make it very difficult for banks to enter this market. Approaches are varied. In the U.K. we see banks entering with start up operations, where in the Netherlands you see large mergers and acquisitions taking place.

Let's consider the products that have been offered. In the early 1990s when bancassurance was really starting to take off, the products were very simple. They were long-term insurance savings type products. One thing you should note is that endowment business is much more common in Europe than in the U.S. Before I left, I rarely encountered endowment business and when I first arrived in Europe I was quite surprised to see it. These products are very easy for a bank to understand, and very easy for the bank to turn around and sell to their clients. Typically, sales can be handled through the branch office. You might have a specialized sales force.

Personal lines property and casualty business was viewed as being very different from a bank's normal everyday activities and therefore, was not originally sold. Over time the range of products has expanded, extended, and moved more into providing financial advice. This is mainly in response to consumer demand, and the emergence of the life insurance markets in general. Property and casualty coverages now tend to be offered. Distribution channels have been expanded to include branch offices. Specialized sales forces, direct marketing, and telemarketing are quite common. The challenge now, and I think this will continue, lies in identifying the right products for the right distribution channels.

I would like to talk a little bit more on products. Typical life products tend to be more retirement, savings and tax and estate planning oriented. You commonly see flexible life. You'll also see unit-linked or what you would call variable life products. These products tend to be much simpler than products in the U.S. and don't have nearly as many features.

On the property and casualty side, all personal line products, including health and motor are now offered. The real expansion into property and casualty products has been aided by the advance of technology. It has allowed things like automated underwriting. You can call a center for claim handling. It has really taken things that the bank wouldn't have considered a normal activity and made it much easier for them to do.

The responses from the nonbancassurers has been pretty typical. They've improved their efficiency and the image of their distribution force. This has been helped by technology advances. Some are looking at alternative distribution channels such as direct marketing. There is much greater pursuit of a strong brand and image recognition, and attempts at cost reduction to try and get on a more level playing field with the cost of distribution of the banks. One thing has been the move into what I call assure-finance, which is the selling of bank products through insurers. As mentioned before, this approach has been much less successful.

Let's examine some of the markets and what has been going on there. As previously mentioned, France has been one of the success stories. All major banks are active in the long-term insurance savings market. They own their own insurance subsidiary. The banks generate over 60% of the new life premium in that market. The principal success story has been the bank's ability to attack the middle income market. This was a market that was not previously served by the insurance companies. The success has been much smaller on the property and casualty side. There's much less penetration by the banks partly due to their lack of expertise and partly due to the fierce competition in that market. Those that have entered the bancassurance arena have done so via a joint venture.

Spain and Italy are emerging markets. They have shown substantial penetration with around 30% of new life premiums coming through bank channels. Property and casualty sales in Spain have also been fairly good. Joint ventures have been the common way to enter the market.

The German market is somewhat unique. In a strict sense, bancassurance has been much less successful there. This is mainly because of the market structure. Many long-standing close links between insurers and banks characterize the market. Therefore, in a sort of cooperative effort, they've limited themselves to sort of cross-selling products, but don't go a whole lot further. From a consumer's standpoint, they're still getting full financial advice. You tend to hear this market referred to as the "all finanz" market model. In the end, the result has been very low penetration by the banks, and the growth potential is viewed as limited.

I think the Dutch market serves as one of the better models for looking at integrated financial services. Since regulatory barriers were eliminated in the early 1990s there have been many mergers of which ING is one example. ING was the result of a merger between National and Interline and an NMB Post Bank, United One. Other examples are AMEV and AG Group combining in 1990 to form Fortis Group. You've seen Aegon, a Dutch insurer that has started up its own banking subsidiary via direct marketing. There's a very active link between banking and insurance in the Dutch market. It still remains to be seen how well some of these financial conglomerates are actually going to integrate the insurance in banking operations since the Dutch market is a fairly mature market, especially in the private pension market. Group property and casualty corporate lines are quite strong in the pension product area and there are many strong relationships with the financial advisors. If you just look at the penetration of the banks as far as the distribution channel for insurance, it has been quite low. I think it's more the move toward integrated financial services that makes the Dutch market unique. One other key item about the Dutch market is that it has been able to get quite a significant penetration in the property and casualty lines. It's one of the highest in Europe which translates to about 15% of the gross written premium coming through the bank channels.

To offer a bit more on the ING experience and explain how we are set up, we basically embrace the strategy of providing full financial services. The products are currently distributed through multiple distribution channels including bank branches, title agents, independent brokers, direct marketing, and post offices. A key workstep is in creating a balance between all those distribution channels. Brokers have tended to view entering into multiple distribution channels as a threat to their business and they're not real receptive to the idea that you're going to directly contact their clients and approach them via another distribution channel for a different kind of product. One of the better bits of advice I can offer is don't underestimate the reaction that your agency force could have.

For products distributed via the bank channel, what happens is that the banks pay the commission and then it's left up to the branch manager to decide how that is then funneled down through. The bank takes responsibility for marketing and sales while the insurance company has responsibility for product development and the back office.

One other key additional point is that the integration is just not in the distribution channels. The integration goes further into management of the company, including risk management and asset management. There is a real attempt to become a more fully integrated company.

The U.K. market is also a mature market, and as I've mentioned, the developments have been a little bit interesting. Originally, most banks entered the market by setting up an alliance with an insurer. I think it's probably the Financial Services Act that has led most banks to now have their own insurance subsidiary. The Financial Services Act basically dictates that agents need to either be a company representative or completely independent. Therefore, banks could no longer offer the products of a selected set of insurers. They either had to offer everything or only one. Many banks opted to just sell the products of their own insurance company and set up their own insurance operations.

In some of the cases, banks use specialized staff that sit within the bank branch. In the other cases, they use specialized staff that sits outside the branch office. There are really varying styles of doing this in that sometimes these people are employees of the bank and sometimes they're employees of the insurance company. A lot depends upon the culture of the company. The building societies in the U.K. have tended to stick with alliances that are a sort of by-product of the reaction of insurers.

As the banks started setting up their own companies, the insurers started to see a big outlet going away. As a result, they were much more competitive about trying to keep the building societies. Insurers were offering the societies very good commissions if they would stay and tie directly to them.

Initially, you found banks quite successful in entering this market; however, that growth is sort of stagnating. One possible reason for this is the strength of other distribution channels. The independent financial advisor channel in the U.K. tends to be very strong. The client tends to be quite sophisticated and really desires expert advice and they prefer to receive it from someone they consider independent. Another thing to note about the U.K. is that they tend to be quite innovative in what they're thinking about. I was reading an article that stated they have now started to place kiosks in railway stations and other places where you basically have an interactive video screen for the selling of insurance.

I'll briefly touch on Eastern Europe. I think it's an example of where markets are truly emerging and privatizing; therefore I see it as having large potential for bancassurance. The products can be relatively simple. People have not seen a lot of insurance products. The markets are just starting to privatize, so it's definitely a time when you can get in and take advantage.

So now what does the future hold? When I look at Europe, one of the things I see is continued market growth. I believe I've touched on most of the reasons. Another thing I think you're going to continue to see is product expansion. The products are going to become increasingly complex. They're going to move more toward wealth management. You're going to see a need for more specialized sales forces within the organization. The corporate life and pension market is going to become more important. What you're finding is that now that banks have been in the business for a while, they find this market much less threatening. Banks understand insurance a little bit better and can make the shift to more complex products a little bit more easily.

Another key product line is going to be the personal lines property and casualty business. As I've mentioned earlier, technology advances have allowed for things like automated underwriting. Claims handling tends to be outsourced whether it's via call centers or put off to a third party. Technology has made it much easier for banks to do business they previously considered not in their realm. They're also very well positioned because they are the lenders of the financing in home and auto situations. Right there you know when to make the sale of the insurance. The other thing I see is that there will continue to be a movement toward multi-channel distribution. In fact, I believe the real trend is going to be toward being an integrated financial services provider. You're going to see more market consolidation with the customers becoming much more accepting of the idea of one-stop shopping. There always used to be a need for some independent advice, but recent surveys show that customers are much more willing to accept one-stop shopping. Customers are really looking for full financial advice and the successful company is going to be the one that can take the normal product chain, sort of unbundle it, and rebundle it to meet specific consumer needs. The consumer is getting much less accepting of hearing that this is the product I have available. They're getting much more demanding as far as wanting the product to fit their specific need.

The challenge is going to be the integration of the two cultures of banking and insurance. It isn't always easy. I'll briefly cover what we can learn from Europe. Some of the key things are their success drivers and the ability to target the right product or the right company. I think that's obvious; Jim addressed that as well. However, one of the other key success drivers has been this ability to have it start out real simple; I don't quite know that necessarily exists in the U.S. market. Other things contribute of course, the banks reputation and the ability to tap the information that's available. One thing that has definitely been seen is that bancassurance has been much less successful and much slower growing in more mature markets. I think that the European experience in that sense is quite different from the U.S. market. Finally, things need to move toward integrated financial planning.

Mr. John O. Nigh: There's a lot of repetition here, but that should be expected because bancassurance has similar themes and objectives throughout the world. The success of bancassurance is quite different throughout the world, and the common approaches undertaken in certain segments of the world are also different. My focus will be on Latin America. At the end of my presentation I will cover a number of actual case studies covering joint ventures that were actually formed in Mexico as well as Brazil.

As both Jim and Jackie have commented, both insurers and banks have objectives of creating additional distribution outlets, particularly for the insurance companies. Banks are seeking to recycle their customer base to create additional revenues and additional profits. We've heard two definitions of bancassurance. It can be whatever you want it to be. The definition that I will use is that it's the development and distribution of life and nonlife insurance products to banking customers. Jackie touched on assure bank or assure finance products, which is a secondary objective in some of these situations. They include the distribution of the financial institution's products to other customer bases including the insurance customer base.

France is currently leading, and is projected to continue leading, in the percentage of life insurance distributed through banks. Holland, Spain, and Belgium show very strong results as well. According to the same source, by the end of this decade, which will be after the end of the year 2000, 60% of new insurance sales are expected to be generated through not only banks, but also other financial institutions. The traditional distribution methods of insurance companies will be losing ground. Insurance revenues for banks and financial institutions are projected to increase to 15% of their total revenue by the end of the year 2000 from their current 2%. We can see that there is a strong movement to capture insurance sales through bank's customer bases throughout the world.

Most of the banks in the United States are distributing annuities at 80% of the top 50 with 32% distributing universal life, 24% term, and so on. We expect that in the European front the countries of Spain and Italy will make significant inroads on France, but France will continue to lead the charge.

Jim covered many of the reasons why bancassurance makes sense for the insurance company, the bank, and client. I'll cover a few of these at the risk of being repetitive. The insurance company gains access to another client. Hopefully the acquisition costs will be lower. It's hoped for and many times it is the case that the persistency of the client will be better. You can capture a relationship with an insured at a younger stage in life. For those of you who have teenage children, you know that the first thing the child does when he or she turns 16 is open up a checking account. These teenagers usually get the funds to put into that checking account from mom or dad. However, that does allow for the insurance company to create a relationship earlier. The insurance company can capitalize on the bank's better public image in many situations and leverage that better public image through it's advertising.

What are some of the reasons why a bank would enter into a bancassurance arrangement? They're able to once again take a look at and re-establish contact with their client. Through profit-sharing arrangements and/or capital raising through some of the situations that I'll cover later, they're able to increase the profitability of the branch network. Banks can leverage their image of quality, leverage the value of the client, and, as mentioned earlier, increase revenue. In some instances, a bank can lock in the customer. By having more products sold to the customer, you better immunize yourself from encroachment from competitors. Banks can generate revenues by linking sales and insurance to bank products. This is certainly the case in Latin America where you are allowed to force insurance sales. For example when a customer would get a mortgage loan or an automobile loan you can require that the person purchase insurance. Oftentimes it's purchased through the affiliate of the bank. Finally, you can diversify your business by having different products with different cycles and different risk profiles.

On the other side, hopefully, the client gets lower prices for its insurance products through a bancassurance venture. As Jim mentioned, there is more of a one-stop shopping atmosphere. There is easier access to more direct service. It's allowed in Latin America. In places where it is allowed, you have more convenient payment methods. They include a direct deduction from checking accounts or even savings accounts. The client has more numerous points of contact and finally more confidence that's built or generated on the part of the customer in the insurance company simply because of the relationship that exists between the insurance company and the bank.

Some of the key ingredients for success relate back to some of the objectives that the bank, insurance company, and the client achieve as well as the benefits that they receive. I will note three here. First, provide attractive products by building long-term relationships with the customers. Second, establish an effective and cost-efficient distribution system. Third, establish an operational environment that provides sufficient profits that also may cover the capital requirements.

Let's discuss a bancassurance venture. There's a wide spectrum of distribution channels that can be undertaken. Many of the ventures that you'll see will incorporate two, three, four or maybe even all of these. They range from telesales moving all the way over to corporate relationship sales. As we move from left to right on the spectrum, we encounter increased product complexity. In telesales, you are looking for the simplest product that can be sold over the telephone and through direct marketing. Similarly, there are sales over the counter, at the branch, through the broker or agency relationship, and then finally sales from the corporate relationship. Corporate relationship sales could involve payroll deduction sales to the employee base of the corporate client or corporate coverages to protect the assets of the corporation.

I would like to address what I think is the total spectrum of distribution arrangements that exist or can exist. The first one is simply a straightforward distribution arrangement where the bank is acting as an agent or broker on behalf of the insurance company. The second is what I refer to as the reinforced distribution arrangement where there is some ownership that exists between the bank and the insurance company creating, at least on the part of management, a higher level of motivation to make the bancassurance venture more successful. The subsidiary distribution arrangement, where the ownership by the bank of the insurance company is complete, is 100%.

Joint venture is what I've seen more often than not in Latin America. There is a joint venture insurance company that's formed, or one might already exist in which the ownership in the venture might be 50/50 or 49/51, depending upon local regulatory environment and who is the controlling party. Often the controlling party is the bank, which ends up with 51%.

We also can have the nonintegrated distribution arrangement where there is a holding company involved, but there's no cross-leveraging of the client base. For example, in Mexico, unless the insurance company and the bank are part of the same financial group, it's against the law to share customer bases between the bank and the insurance company. The bank will sell insurance products on a blind basis to its customer base. This is similar for insurance companies selling assure-bank products. Finally, we have the integrated situation where banks and insurance companies are part of the same financial group. For example, in Mexico, or within the same holding group, such as in Chile, there is the ability to cross leverage customer bases.

In many instances, banks have no concept of what the value of their client base is and often the bank will enter into some form of bancassurance arrangement without having gone through the process of saying what's the value of my customer base in the context of the bancassurance environment. What we've developed over time to help a bank identify this value and maybe subsequently capitalize on this value is a valuation methodology. The methodology simply looks at a segmentation of a customer base, identifying products that might be sold to that customer base, developing what makes the most sense for how those products might be distributed, the degree of market penetration and then ultimately arriving at some sort of financial evaluation of the value of this customer base to the bank in the bancassurance environment. You can do the opposite with the assure-bank focusing in on the insurance company for the sale of banking products. In addition, there are other forms of assure bank opportunities.

The following countries in Latin America allow bancassurance: Columbia, Peru, Chile, Mexico, Venezuela, Brazil, and Argentina. There are some caveats to that. For example, in Chile the bank cannot directly own an insurance company, but the same holding company group that owns the bank can own the insurance company. There are other limitations such as the requirement of an agent or broker to be on record for all insurance sales in Brazil. This is also true in Mexico as well as Chile.

The three countries that have attracted the most attention for reasons of the size of the gross domestic product in those countries as well as its population include Mexico, with a population of 91 million people, Brazil, the granddaddy or the big one of them all with a population of 165 million, and Argentina with a population of 35 million. Chile has attracted some attention recently because of recent regulatory changes that permit bancassurance to take place; however, its population is the smallest (14 million) of the countries that I have mentioned. A number of the U.S. and other multinationals have some sort of bancassurance arrangement. This could include a straight forward distribution arrangement.

Due to time constraints, I'll only cover a couple of these companies. The first is the Banorte/Generali joint venture in Mexico. Banorte, a regional bank out of Monterrey, embarked upon a series of discussions to form a bancassurance joint venture. It ended up including an annuity company in addition to an insurance company. The annuity company specialized in sales associated with the partial privatization of Mexico's social security system. Jackie commented briefly on the evolution of bancassurance as she sees it in Europe. The same evolution applies in Latin America. We are seeing widespread privatization of social security schemes in Latin America. We have three entities that are part of this joint venture arrangement which provided for not only bancassurance sales, but also assure bank sales. In this case Generali was a 49% owner in each of the entities with Banorte maintaining control at 51%.

As for the valuation aspects, the total purchase price paid was around $160 million. Keep in mind that this is just a purchase price for access to the customer base. There was $84 million paid up front to Banorte with deferred payments of $75 million accruing over the following ten years if certain production objectives were met.

I'll quickly cover Aegon and Banamex in Mexico. Aegon, or Banamex I should say, decided that they wanted to enter the insurance market through a bancassurance arrangement. Banamex knew nothing about insurance and realized that they needed to get a partner that knew a lot about insurance. The partner that they ended up structuring their joint venture with, Aegon, has significant insurance operations throughout the world. Again this was a 49%/51% venture with Banamex retaining 51% control. In this instance the purchase price paid was $109 million up front with deferred payments of $58 million over a 10-year period.

In addition, Aegon purchased 10-year convertible debentures amounting to $216 million, which could be converted to Banamex equity over time, which resulted in direct ownership of the bank by Aegon. There are examples of other joint ventures that have been formed in Latin America. There has been a joint venture announced in Chile, one of the first following the regulatory changes there.

In summary, bancassurance is going to be taking hold of the distribution of insurance products as we go forward into the next millennium. I do think that they will also find a way to successfully sell the finance products to the insurance customer base as well as the affiliated customer base.