Article from:

International Section News

June 1998 – Issue No. 16

The Equation for Success—Professionalism and Profitability: Part I

Worldwide Trends in the Insurance Industry

by Thomas H. Kelly

Editor's Note: *This article contains material excerpted from a speech given on June 17, 1997 by Tom Kelly, Senior Vice President and Managing Director of LIMRA International, at a LOMA/ LIMRA Strategic Issues Conference in Singapore. Credit is also due to Randy Makin, who converted the outlines and slides from Mr. Kelly's speech into an article format for the newsletter. This is the first installment of three articles derived from the speech.*

It is an honor and privilege to have the opportunity to be with all of you and participate in this most important LIMRA/LOMA Strategic Issues conference with the theme, "The Equation for Success—Professionalism and Profitability." What I would like to do this morning is reflect upon the life insurance industry around the world and some of the forces driving change and their implications, take a close look at the Asia region, and conclude with six guidelines for the future.

Let me share with you some headlines from the trade press, newspapers, and conversations from my travels over the past 12 months:

- Number of Australian Agents Declined 50% Over Past Four Years as Industry Has Transitioned from Life Insurance to Financial Services—New Zealand to Follow
- Impact of U.K. Regulation Causes Attrition of 50,000 Agents Over Past Three Years
- PIA/Lautro (regulatory body) Fines Exceed £25 Million
- Major U.S. Insurer Fined $100 Million for Unethical Sales Practices. Sales Plummet 30%.
- New Business Written in Asia Has Exceeded 25% Annually Over Past Decade—Career Agent Distribution is System of Choice
- China, India: Markets of the Future (for the insurance industry)
- GATS, WTO Trade Agreements—Boom to Industry
- Growth of Middle Class Will Drive Industry Growth.

The winds of change are blowing across our industry worldwide, and depending on your geographic location and perspective, it could be the best of times or the worst of times. What are some of the market forces for change that are blowing, creating a global marketplace and insurance industry?

First, there have been economic reforms and stabilization, such as:

- Privatization of industry, moving from government-owned to private enterprise
- Stabilization of inflation and interest rates
- Growth of the middle class (which fuels our products and industry)
- Increase in retirement savings, and moving responsibility from government to individuals

Second, there has been an opening of markets, driven by:

- Trade agreements, such as the General Agreement on Trade and Services (GATS) and OECD, creating access to markets
- Entry of foreign players in other markets as their home-country market matures
- Growth of the local industry from the overall economic growth within countries.

All this creates competition, driving competence and the importance for everyone to become better, more effective, and efficient.

Third, companies are focusing on quality, excellence, and a customer focus—becoming market-driven and customer-oriented. Note that:

- Quality can be a competitive advantage and strategy. Companies can differentiate themselves such as Sony Life of Japan with its life planners (average 14 sales per month and an average sale of $1,200), Pru (U.S.) direct line, and Virgin Direct in the U.K.
- The emerging consumer needs of protection for life and property and for estate creation
- There is an increasing consumer awareness of financial security products. Great strides have been made, but there is still a long way to go.
- In the developing markets, certain factors favor agent distribution— low prevalence of checking accounts, little knowledge of products, knowledge of how much and what to own, and less dealing with financial institutions.
- Finally, the customers' desire for quality means that increasingly fewer and fewer of the goods and services you purchase are made in your country. Consumer choice means we are all contributing to globalizing the marketplace on a daily basis.

A fourth factor is technology/the information age:

- Technology and information transfer shrinks time, distance, and structure of work.
- Technology has given us better computerized brains and electronic speed, and thus better tools (e-mail,

continued on page 24, column 1

The Equation for Success
continued from page 23

personal computers, fax, cellular phones, ATMs, VCRs, and so on) all with microprocessor intelligence.

- Population growth provides more brains—88 million brains are being added to the world population base each year.
- When you put the human and electronic brainpower together, it positions the global marketplace for things that would have been considered miracles just a few years ago.
- Today learning has never been easier, and information has never been more accessible. Thus, the biggest challenge today is not only getting an education, but keeping one as well, and with the advances in technology your job and your career become your classroom. Thus there is an importance and priority of professionalism in our chosen career of insurance.
- With every passing day, we get a bigger selection and choice of everything—entertainment, automobiles, medical techniques, athletic shoes, toothpaste—and certainly the choices will soon affect the range of life insurance and financial products that will come online in years to come.

The information age and information technology keep presenting us with more options and expanding our field of choices. Let me give you an example. Today in certain markets, you can walk into a store and buy a computer- designed pair of Levi's custom made to fit your legs, waist, and rear-end—and it's delivered in two days. That's bringing customization to the individual level. And that's exactly what we have the opportunity to do in our industry—sit with a client and design an insurance program that fits his needs.

Finally, regulation has arisen as a driving force for change. Today there now exists an International Association of Insurance Commissioners, an organization made up of insurance commissioners of the various countries around the world who meet to discuss issues such as solvency guidelines, risk selection, ethical sales practices, market conduct, and so on. This forum for information exchange will serve to influence the nature of regulatory practices in each country; thus, the speed with which regulatory decisions will take place will increase dramatically.

These forces—economic reform and stabilization, the opening of the markets, quality, excellence and customer focus, technology and the information age, and regulations—are driving the globalization of the insurance industry and the local development of our great business. Given this background, come with me as we take a quick tour around the world of insurance—to Europe and Latin America, the U.S., and a look in a bit more detail at Asia. We'll take a bird's-eye view into these markets and examine some of the successes and challenges of each.

Europe

The largest markets in Europe are the U.K., France, and Germany, in that order. However, the strongest growth markets are Portugal, Spain, Greece, Poland, Hungary, Italy, and the Czech Republic.

Regulatory changes will continue to play a major role in the evolution of the European life insurance industry—privatization (in France and Italy), deregulation (in Germany), and re-regulation (in the U.K.), driven by market conduct and compliance.

The marketplace in the U.K. is in particular turmoil, given the regulatory environment. The number of agents has declined from 240,000 in 1989 to 90,000 in 1994. Why? Perhaps it is from an overdue assault on the unethical, the uncommitted, and the unproductive agent under consumerist pressure, along with a recession and dramatic cuts in commissions on savings-plan products.

Today, with the presence or entry of banks into the business, experimentation with direct marketing, the continuous growth of brokers, and the attack on career agents, insurance distribution is currently in a state of transition. Every country is experiencing this transition, although the speed of change varies from one country to another. In that regard, it is similar to Asia. Bancassurance in France has already captured 60% of the new business market. In Italy and the U.K., banks have only recently entered the market, yet big gains are being made into what was predominantly the domain of the exclusive agent. An increasing integration of banking, investment, and the insurance industries appears likely to spread across Europe, although, again, the speed with which this takes place will not be uniform. However, this is already happening in Germany and the Netherlands, where the largest insurance company, Nationale-Nederlanden and the largest bank, Post Bank, have joined in a powerful strategic alliance.

Product knowledge and innovation will become important in certain markets as deregulation allows companies to offer a broader product range. For example, there will be an increase in private pensions, particularly in France and Italy, where penetration is particularly low.

Perhaps the most essential component of the sales and market process is distribution. It is, I believe, sufficient to say that those companies with the ability to reach customers efficiently, cost effectively, and with value-added services, will be those who take advantage of Europe's potentially lucrative life insurance and pension markets.

Latin America

Turning to Latin America, significant growth is taking place in Mexico, Chile, Argentina, and Brazil, with Peru and Colombia soon to follow. This growth will be driven by NAFTA in Mexico, and by the opening of the markets and privatization of the Social Security systems in Chile, Argentina, and Peru.

Most insurance companies are part of financial conglomerates with a strategic business unit organization structure—life, health, pensions, and non-life. Again, independent agents and brokers are now the distribution system of choice. The greatest opportunity exists with career agents' distribution of simple, basic individual life products.

Growth of the industry is driven by new entrants into the market from the U.S. and Europe. The hyperinflation of

continued on page 25, column 1

The Equation for Success
continued from page 24

the 1960s, 1970s, and 1980s has given way to single-digit inflation in most countries, opening up the individual life market.

United States

In the U.S., we are witnessing a significant shift in the product mix from risk to living-benefit products, such as annuities, mutual funds, and variable products. This trend is being driven by the graying of America and a significant change in the profile of the family, in which there are more single heads of households, more one-person households, and more unrelated households.

The U.S. industry is moving from a high-margin, low-volume era to a low-margin, high-volume era, and this equals higher productivity and better, more creative expense management.

Perhaps one of the biggest challenges facing the industry in the U.S. is bringing new people into the business. Recruiting was down 9% in 1995 and has been down in seven of the last eight years. Because of this downturn in recruiting, the field force is slowly dwindling. It is down from 241,000 in 1986 to less than 207,000 at the end of 1995. As a result, companies are reassessing and re-engineering their marketing and distribution systems and strategies and deciding what system or systems are appropriate for their company (banks, multiple systems, Internet, and so on). They are looking to technology to improve prospecting and customer identification, at worksite marketing to get agents in front of more prospects more efficiently, and at arrangements with banks for the same reason. The thrust of companies' efforts to be creative in their marketing is to reach more people, but at a cost that is manageable.

Other major issues on companies' agendas are:

- Market conduct and ethical sales practices
- Focusing on core businesses (and the overall effectiveness and productivity)
- Strengthening the financial statement—in this regard, is a merger, acquisition or a strategic alliance an option that should be considered?

So there you have a quick perspective, a thumb-nail sketch of what is going on in our industry around the rest of the world.

Effectiveness in Administrating Individual Life Insurance Policies

by A. Reg Munro

I am an actuary, but over the years I have been involved in many aspects of the life and pensions business undertaken by my employer, Old Mutual, based in Cape Town, South Africa. When I was asked to manage our Information Technology (IT) Division in 1990, among other functions, I was immediately faced with a new measurement challenge. Having come from a business unit where personal selling was a major part of the business, I was accustomed to having very detailed measures of progress, which seemed much more difficult in IT. We could benchmark our IT shop against other IT shops and measure people against the performance contracts negotiated with them. But when it came to measuring the value provided to the various businesses, we didn't even have a conceptual framework for measurement.

The critical breakthrough, for me, came when I realized that no measurement internal to the IT division would provide this. The challenge then became finding a measure of the various businesses within Old Mutual that would demonstrate the strategic impact of their investment in IT. Fortunately, we already had an accepted method of allocating all centrally provided costs to the various businesses and this meant that we were able to develop measures that showed the impact of the increasing investment and expenditure in IT on the businesses. For each business a ratio similar to that proposed below was defined, and progress over time was tracked. Because the businesses are so different, varying from mutual funds to individual life to group employee benefits, comparing the ratios between businesses was clearly without meaning. Comparing the improvement trends, however, proved quite enlightening. One business was improving its measure by 50% every five years, while another was taking 30 years.