Guaranteed Uncertainty

Socioeconomic Influences on Product Development and Distribution in the Life Insurance Industry

008759-0111 (562-41-0-PU4)

Table of Contents

List of Tables

❖ ❖ ❖ ❖ ❖

List of Figures

About the Study

> ***"With prolonged high unemployment predicted, consumer spending is paralyzed by caution... businesspeople are paralyzed by uncertainty..."*[1]**
>
> — George Will

Financial Security Today

The public's frustration with the current economic environment demonstrates the value placed on financial security. Our sense of financial security starts with having a dependable source of income whether it is from a job commensurate with our skills and ambitions or from a retirement plan sufficient to meet the lifestyle to which we are accustomed. The industry challenge is that people have a hard time recognizing what they need in order to achieve financial security beyond a dependable source of income and, furthermore, recognizing how the industry's products and services help fulfill their needs. Consider:

- **Fifty-eight million** U.S. households believe they do not have enough life insurance.[2]
- **Twenty-nine million** Americans controlling $881 billion of retirement savings assets will reach retirement age over the next five years.[3]
- **More than 60 percent of personal bankruptcies** in the United States in 2007 resulted from health care costs associated with a major illness.[4]

These facts and others, to be explored later, will certainly shape the industry in the next three to five years and beyond. They will also inspire creativity in product development and distribution. Recognizing this, LIMRA and the Marketing and Distribution Section of the Society of Actuaries sponsored this research paper. The research objectives are to identify:

- The key socioeconomic trends influencing the need and demand for the industry's products and services, and
- How these trends will influence product development and distribution over the next five years.

[1] Will, George, "No Rational Exuberance," *Newsweek*, January 15, 2010.

[2] *Household Trends in Life Insurance Ownership*, LIMRA, 2010.

[3] *Money in Motion*, LIMRA, 2010.

[4] *Medical Bankruptcy in the United States: Results of a National Study*, American Journal of Medicine, August 2009.

The Four Cs of Marketing

To understand the implications of the trends outlined requires expanding the marketing mix model to better reflect the service economy in which we now operate. Harvard Business School professor Neil H. Borden introduced the concept of the marketing mix in 1953 during a speech he delivered as president of the American Marketing Association. Eleven years later, his article "The Concept of the Marketing Mix," published in the *Journal of Advertising Research*, explored the concept in detail.

In 1960 Michigan State University professor E. Jerome McCarthy refined the marketing mix concept into four key marketing processes — product, price, place, and promotion. McCarthy dubbed these processes the "Four Ps of Marketing" and explored them in detail in his book *Basic Marketing: A Managerial Approach.* To this day, McCarthy's concept is fundamental to establishing a target-market strategy.

University of North Carolina professor Robert F. Lauterborn's notion of the "Four Cs of Marketing" expands the concept to today's service economy.[5] Lauterborn advocates:

- **Customer not product** Remain focused on *customer value* instead of product features by engaging your customer and letting value define the product or service in the marketplace.
- **Cost not price** Consider *cost*, something customers pay instead of price, something you charge by being mindful of the customer's dilemma — limited money and unlimited needs.
- **Convenience not place** Strive for *convenience* not place by going beyond who sells the products and where they are sold. Think about the shopping experience and new ways of connecting with customers.
- **Communication not promotion** Communication means interacting with customers and building relationships, whereas promotion is a relic of mass marketing no longer effective in a diverse marketplace requiring targeted marketing.

[5] Lauterborn, Robert F., *Integrated Marketing Communication: Pulling It Together and Making It Work*, McGraw-Hill, 1993.

Acknowledgements

LIMRA and the Society of Actuaries (SOA) extend their gratitude to the members of the Project Oversight Group (POG) for their input and review throughout this research project.

Representing LIMRA	*Representing the Society of Actuaries*
Richard W. Hekeler, Ph.D.	Charles E. Ritzke, Chair, Project Oversight Group
Lucian Lombardi	PW Calfas
Todd A. Silverhart, Ph.D.	Andy Ferris
Stephen G. Wood	Jeffrey D. Koll
	H. Michael Shumrak
	Ronora Stryker, SOA Research Actuary
	Jan Schuh, SOA Research Administrator

Guaranteed Uncertainty

The villains in our story are the risks associated with uncertainty exacerbated by the "Great Recession." The heroes are the professionals designing and delivering insurance products and services, because insurance is one of society's most powerful answers for managing risk.

Uncertainty — indeed, one need only look to the past three years to see how it pervades our economy. Government, business, and the populace have been forced to react to an economic downturn that few anticipated and which has exerted a broader, more severe impact than most could have imagined. What is certain is that although the recession is technically over, its effects will be felt for several more years.

The recent economic downturn — along with its high levels of unemployment and underemployment — is only one element of our uncertain world. Recent decades have witnessed broad scale changes that continue to influence other aspects of our life in ways not fully understood. Some changes are positive forces, others more ominous.

Positive Forces of Change

- The American family continues to evolve, taking on a variety of different structures with unique needs and abilities to manage those needs.
- Immigration, long part of our nation's history, continues apace, spreading a wave of multiculturalism from large urban areas to rural towns.
- Technology has led to advancements that have improved the quality and length of life, increased efficiency and productivity, and created vast new social networks.

Ominous Forces of Change

- The population of the United States is aging, thus placing a burden on families, health care delivery, and government entitlement programs.
- The social safety net of government and employer-based benefits is less certain, and with it, the financial futures of many are questionable at best.
- Wage stagnation and inflation threaten savings and personal/family financial well-being.

Apart from these socioeconomic trends, a host of other less certain events — both socioeconomic and otherwise — further obscures an already cloudy vision of the future. To meet these challenges of the short term, the industry will have to be nimble in its product development and distribution to stay current with the changing marketplace.

“The Great Recession”

Table 1 — Sample Recessions Since World War II

Recession	Duration in Months	Peak Unemployment	Decline in GDP
Great Recession	18	10.6%	-4.1%
Early 1980s	16	11.4	-2.7
1973–1975	16	9.1	-3.2
1958	8	7.7	-3.1

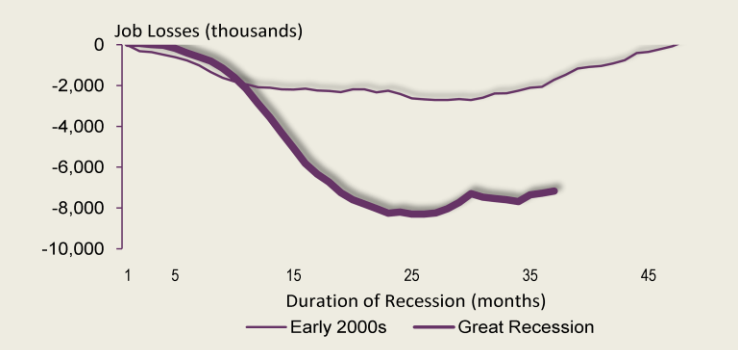
Source: Bureau of Economic Analysis, U.S. Department of Commerce.

The industry’s challenge over the next five years starts with the Great Recession. If it has not hit individuals directly through job or home loss, it has affected their pocketbooks through such things as reduced wages, smaller annual wage increases, and reduced net worth. The factors that contributed to the downturn are complex and the path to better economic times will be arduous.

The Great Recession — a term given by the popular media and economists alike — by many measures is the most severe since the end of World War II. Among the 13 recessions since the end of the war, it is one of the longest, 18 months, along with one of the deepest economic contractions, with a decline in GDP of -4.1 percent (Table 1).

Also quite unique with this recession, particularly in comparison with the prior recession (in 2001), are the size and the rate of job losses: Nearly 8 million jobs were lost within 24 months from the start of the recession (Figure 1).

Figure 1 — Job Losses Since Starts of Recessions



Source: U.S. Department of Labor

Adding those “marginally attached” and those employed part-time for economic reasons yields an underemployment rate of 16.5 percent at the end of the recession.[6] Just these two facts alone are having a major effect on consumer sentiment as well as the industry’s sales. Other unique characteristics of the Great Recession:

- The recession started with already historic low interest rates.
- A crisis in confidence not seen since the 1920s occurred in the fall of 2008.
- The speed at which information is disseminated and at which transactions occur is unprecedented.
- Housing prices declined — a rare occurrence over more than a generation.
- Today’s workers have assumed much greater responsibility for funding their retirement and health care expenditures.

[6] Marginally attached workers are persons not in the labor force who want and are available for work, and who have looked for jobs sometime in the prior 12 months (or since the end of their most recent jobs if they held them within the past 12 months), but who were not counted as unemployed because they had not searched for work in the four weeks preceding the survey. Discouraged workers are a subset of the marginally attached.

The recent recession also has many characteristics of prior recessions:

- Unemployment rates climbing to 10 percent
- Equities posting negative 10-year returns
- Households experiencing a negative wealth effect
- Median household income stagnating

Economic Outlook

The recovery has begun, albeit quite slowly. Real GDP growth is projected to average 2.4 percent annually over the next decade, near its previous 10-year average of 2.5 percent, while productivity growth is expected to slow; the personal savings rate will continue to increase, and slower growth in personal consumption expenditures and rising medical expenses will also characterize the coming years.[7]

The U.S. Bureau of Labor Statistics also expects that the recent decline in home prices, substantial swings in the stock market over the previous decade, and the impact of the recession will all contribute to a slowing of growth in consumer spending. This slowing will result from a deceleration in purchases of goods and not from a slowdown in purchases of services. The Bureau of Labor Statistics expects spending on services to maintain its growth rate from the previous decade. Personal consumption expenditures — which account for more than two thirds of the economy — posted impressive gains over the past two decades. Growth in consumer expenditures in the earlier years of this period mirrored growth in the overall economy, while increases in the latter years were related to the housing market bubble and the steady decline in the savings rate. The slow growth in consumer spending is the major reason for the anticipated slow economic recovery.

The turmoil of the past decade — from 9/11 to the Great Recession — has masked longer-term changes that the U.S. labor force has been undergoing for several decades. Fueled by the Baby Boom generation (persons born between 1946 and 1964), it underwent unusual growth in the 1970s and 1980s. More recently, growth has slowed down and is expected to continue to do so as the Boomers age and leave employment. The Bureau of Labor Statistics expects household employment to increase by about 13.1 million over the next 10 years, less than the increase of 13.9 million over the past decade. Additionally, the economy is not expected to reach full employment until 2018.

Two indicators of how the industry's customers will use their disposable dollars over the coming years are the savings rate and household debt. The savings rate has increased, reversing its decades-long decline as consumers have become more cautious in the recessionary period. This trend in personal savings rates is also influenced by savings for retirement, which continues to be less than adequate, even in the public's estimation. The 2010 Retirement Confidence Survey indicates that 44 percent of workers are "not too" or "not at all" confident of their ability to accumulate needed retirement savings.

In recent years, our economic growth has been fueled by consumer credit. For the past 30 years, consumers spent between 11 percent and 14 percent of their disposable income paying off mortgage and consumer debt (the debt service ratio or DSR). An additional 5 percent is paid to cover other financial obligations such as car lease payments, rental

[7] *The U.S. Economy: From Recession to Recovery*, Monthly Labor Review, November 2009.

properties, property taxes, and homeowner's insurance (the financial obligations ratio or FOR). Since the start of the Great Recession, consumers have trimmed their debt to levels not seen in the past 10 years.[8]

For recent college graduates, debt is particularly troublesome. According to The Project for Student Debt, the average student loan debt level of college graduates was $23,200 in 2008, a figure that grew 6 percent in each of the previous four years.[9] Credit card debt adds to the total. The unemployment rate for this group hovers in the 8 percent range.

Implications

Life and annuity products will remain the major sources of retail sales over the next five years. What is harder to discern is how the mix of products will evolve to meet what customers value. If the trends of the past three decades are a guide, offering a balanced product portfolio will serve as a prudent hedge against this uncertainty.

Variable products and consumers' changing appetite for risk illustrate the point. Variable life captured nearly a third of the $4.6 billion retail life insurance market in 1999; today it has shrunk to 7 percent, or $812 million. Variable annuities have fared better but have not escaped customers' loss of appetite for risk. In 1999 sales were $122 billion, or nearly three fourths of the annuity market; today variable annuities represent nearly 55 percent of the market, or $128 billion (Table 2).

Table 2 —
Mix of Individual Life Insurance and Annuity Sales by Product: 1979–2009

	1979	1984	1989	1994	1999	2004	2009
Life Insurance							
Whole life	84%	55%	53%	48%	29%	24%	28%
Term	16	12	13	14	21	23	27
Universal	0	30	27	22	19	37	38
Variable	0	3	7	16	31	16	7
	100%	**100%**	**100%**	**100%**	**100%**	**100%**	**100%**
Annuities							
Fixed	Not Available		74%	47%	26%	40%	46%
Variable			26	53	74	60	54
			100%	**100%**	**100%**	**100%**	**100%**

Source: LIMRA

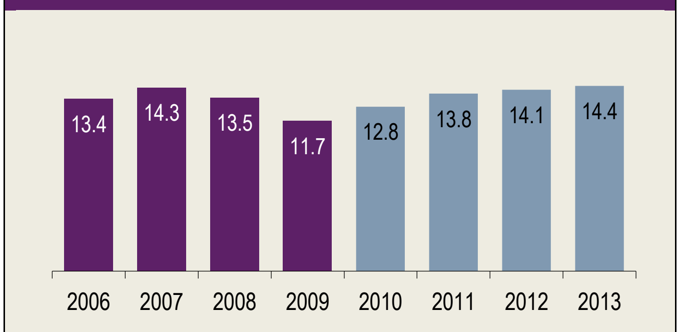
[8] "Household Debt Service and Financial Obligations Ratios," The Federal Reserve Board, June 17, 2010, www.federalreserve.gov/releases/housedebt/default.htm.

[9] *Student Debt and the Class of 2008,* The Project on Student Debt, December 2009.

The key implications as a result of the current economic trends include:

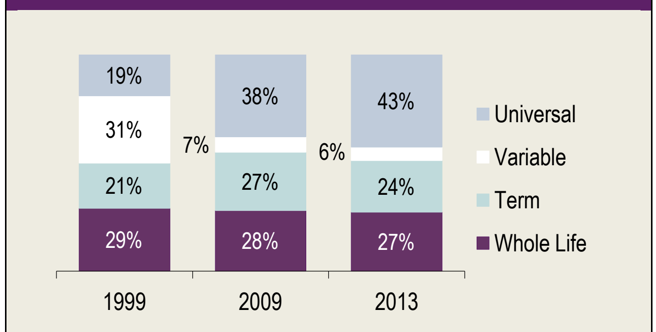
- The growing demand for two other products will significantly alter the competitive landscape. These are health insurance and retirement income products. The effects of health insurance reform will take two or three years to be felt. The effects of retirement income products are already evident and will grow in intensity.
- Individual life sales will not recover to prerecession levels until 2013. Disposable income, consumer confidence, and interest rates have the most impact on total sales. Moody's forecast expects disposable income to recover by early 2011, and then grow at a steady pace. However, interest rates are expected to be somewhat volatile, with corporate bond spreads widening and contracting in varying degrees. The outlook for consumer confidence remains weak (Figure 2).
- Universal life sales will grow the fastest and will take some market share away from other product lines. Whole life sales will grow but not at the pace of the past two years. Growth in term life sales will be positive; however, variable life will remain anemic (Figure 3).
- Indexed products are posting double-digit sales growth; however, it is too early to determine whether the guarantees of index products will appeal to former buyers of variable life products. Variable life products have not recovered since the dot-com bubble burst in 2000. Prior to the bubble and for two years after the bubble, variable life sales tracked closely to the returns in equity markets. However, when the equity market returns turned positive in 2003, variable life sales continued to lose market share.

Figure 2 —
Individual Life Insurance Sales Forecast
Annualized new premium ($billions)



Source: LIMRA

Figure 3 —
Mix of Individual Life Insurance Sales by Product
(Percent of new premium)



Source: LIMRA

The outlook for annuity sales is less positive than the outlook for life sales. Sales are not anticipated to return to 2008 levels in the next five years (Figure 4). The primary reason is the poor outlook for fixed annuities:

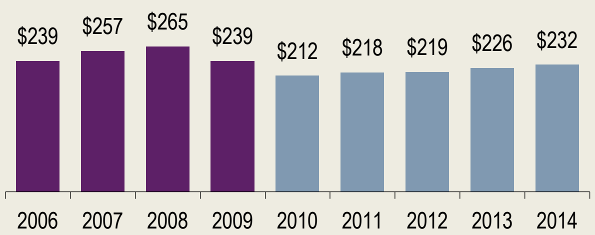
- Fixed annuity sales were exceptionally strong in 2008–2009, setting sales records in both years.
- Sales levels will drop back to more historical trends and remain flat at $72 billion annually.

- The primary reason for the sales slowdown is the low interest rate environment.
- The spread between fixed annuity rates and those for certificates of deposit (CDs) have become much closer, reducing the appeal of fixed annuities.
- Indexed annuity sales, which hit a record in 2009 and captured 31 percent of the fixed annuity market due to the low interest rate environment, are anticipated to capture an even greater share of this market, at least in the short run.

The forecast for variable annuity sales is brighter:

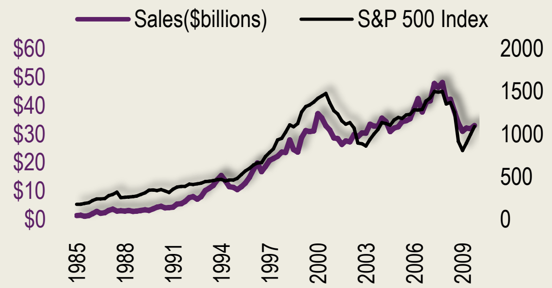
- After the big drop in 2009, sales will grow 5 percent or so over the next five years, reaching $155 billion in 2014.
- Unlike variable life products, variable annuity sales correlate highly with the equity returns (Figure 5).
- Many companies continue to offer guaranteed living benefit (GLB) riders on their variable annuity products.
- Most of the "de-risking" adjustments to variable annuity products and riders appear to have come to an end.
- Consumers continue to show interest in buying variable annuity contracts with GLB riders. The GLB election rate, when available at purchase, remained strong at 87 percent during the fourth quarter of 2009.

Figure 4 —
Annuity Sales Forecast
($Billions)



Source: LIMRA

Figure 5 —
Variable Annuity Sales Versus S&P 500 Index
(Sales left axis; Index right axis)



Source: LIMRA

The Vanishing Social Safety Net

> ***What has changed? In a word, ideology. Over the past two decades, the corporate and government policies that once provided a basic foundation of economic security for American workers and their families have run headlong into a collection of beliefs, institutions, and advocates that I call the 'Personal Responsibility Crusade.' The core assertion embodied in the Personal Responsibility Crusade is that Americans are best off dealing with economic risks on their own, without the overweening interference or expense of wider systems of risk sharing. … It is all about … making people more responsible for the management and finance of the major economic risks they face.***
>
> — Jacob S. Hacker, The Great Risk Shift

In his 2006 book, *The Great Risk Shift*, Jacob S. Hacker described a change in the social fabric of the nation.[10] During the Great Depression, the notion of government and private business providing a social safety net was born with President Roosevelt's New Deal legislation. Political and business leaders put in place institutions that were designed to spread economic risk more broadly over the various socioeconomic groups. This social contract protected many from ill health, disability, and poverty for a half a century. During the Reagan era, however, a different set of principles took hold. By providing subsidies, big government was seen encouraging moral hazard — and at a high cost to the national treasury. This view held that it is best for government to step aside and allow individuals to succeed or fail on their own. The impact of this thinking can be seen in many places, including:

- The switch from defined benefit to defined contribution retirement plans
- Higher premium cost-sharing for medical benefits
- Higher copayments for medical expenditures
- The development of consumer-directed health care plans

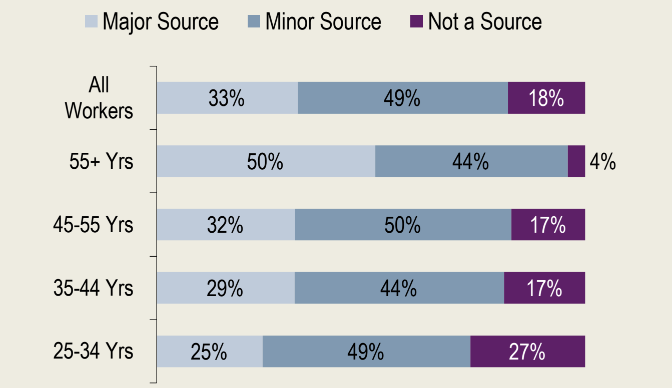
Government Programs

Though never intended as a primary source of retirement income, Social Security and other social insurance programs were an attempt to limit what were seen as dangers in modern American life such as old age, poverty, unemployment, and the burdens of widows and fatherless children. Increasingly, though, Americans came to view Social Security as an important part of their retirement income. However, in recent years, questions about the solvency of the system have caused many workers to question whether they can count on Social Security in their retirements.

[10] Hacker, Jacob S., *The Great Risk Shift*, Oxford University Press, 2006.

Over the years, the Retirement Confidence Survey has documented worker confidence that Social Security will continue to provide benefits in the future of equal value as today. Since 1992, around 2 in 3 workers have said they are "not too" or "not at all" confident. Predictably, younger workers are least apt to expect any contribution to their retirement income from Social Security. Only 1 in 4 of those 25 to 34 years old expects to see income from Social Security when they retire. In contrast, twice as many of those 55 and older do (Figure 6).[11]

Figure 6 —
Workers Expecting Social Security Income in Retirement



Source: *Attitudes About Social Security and Medicare,* Employee Benefits Research Institute and Mathew Greenwald & Associates, Inc., 2009.

When it comes to Medicare, 6 in 10 workers say they are "not too" or "not at all" confident that the program will provide benefits of at least equal value to what retirees receive today. This proportion has held constant since 1992 despite the fact that the program is expected to run out of money in just a few years.[12] What is more, employer-sponsored retiree health benefits have been on a steady decline since 1990 when the Financial Accounting Standards Board approved an accounting change (FAS 106, "Employers' Accounting for Postretirement Benefits Other Than Pensions") that required companies to record retiree health benefit liabilities on their financial statements and therefore affected many companies' reported profits. A study of large employers (500 employees or more) by Mercer indicates that between 1993 and 2009, the percentage of employers offering health insurance to retirees dropped by half from 40 percent to 21 percent.[13]

Employer-Based Programs

For many decades, employers have played an important role protecting the well-being of workers and their families. A key element for many employees was the defined benefit (DB) pension plan that provided a constant income stream in retirement and required little active employee account management. Defined contribution (DC) plans, never intended as primary retirement savings vehicles, were developed in the late 1970s and became especially popular among smaller firms that could not afford to offer the more traditional defined benefit plan. Over time, the costs of maintaining DB plans became burdensome even to large employers. During the 1990s, many of these employers effectively discontinued their DB plans, opting to rely on the DC plans many were already offering their employees. Participation in DB plans dropped by more than half between 1985 and 2005. Additionally, nearly 3.3 million workers have frozen defined benefit plans.[14]

[11] "Attitudes About Social Security and Medicare," Employee Benefits Research Institute and Mathew Greenwald & Associates, Inc., 2009.

[12] Employee Benefits Research Institute and Mathew Greenwald & Associates, Inc. *op. cit.*

[13] *Notes*, Vol. 31, No. 1, Employee Benefits Research Institute, January 2010.

[14] "Defined Benefit Pensions: Plan Freezes Affect Millions of Participants and May Pose Retirement Income Challenges", United States Government Accountability Office, July 2008

DC plans require active employee involvement in terms of both setting contribution levels and managing funds throughout the duration of the employee's participation. This has imperiled many workers' retirement nest eggs. In the first place, most workers are not good savers. In the second place, few have the interest, knowledge, or time to effectively manage their accounts and make sound investment decisions.

In addition to retirement savings, medical insurance has been another area in which employers have played a major role assisting employees with managing personal risk. Starting during World War II as a way to secure workers during the war-induced labor shortage, medical insurance remains a key way in which employers attract and retain talent. Over the past decade, the proportion of U.S. firms offering medical insurance has been between 60 percent and 69 percent, with virtually all firms employing 200 or more employees covering their employees.[15] In all, 56 percent of workers had employer-based coverage in their own names in July 2009, down from 60 percent in January 2007.[16]

In recent years, the cost of providing medical insurance benefits has risen dramatically, more than doubling for both individual employee coverage and family coverage. This has taxed the ability of employers — especially small employers — to afford the costs of coverage. While they have continued to fund a fairly constant proportion of the premium costs over the past decade, they have been forced to make plan changes to control the price spiral. This has typically involved higher out-of-pocket costs for employees. The effect on workers' wallets has been significant. These fees in combination with higher premium contribution (on average $899 annually for individual employees and $3,997 for families in 2010) have taken a significant bite out of any annual pay increases employees received in recent years.

Implications

The implications of the vanishing social safety net portend more of an indirect rather than a direct effect on product development and distribution. These implications include:

- Workers growing increasingly uncertain about when to retire. Though not the only factor, concern about the fate of Social Security is contributing to this uncertainity. Compared with 1991, three times as many workers in 2009 said they will retire at age 66 or older (31 percent); half as many say they will retire before age 60 (9 percent). Likewise, the proportion of workers who anticipate working in retirement has increased by 11 percent between 1999 and 2009.[17]
- Medical insurance costs remain a key challenge. Not surprisingly, 84 percent of employers cite rising medical insurance costs as a key challenge. Although some are beginning to question how important benefits are for recruiting and retaining talent, only a small minority are entertaining thoughts of eliminating their benefits plans. As they look to the next few years, they are more likely to say they will continue to reduce employee benefits to respond to escalating health care costs (Figure 7).[18]

---

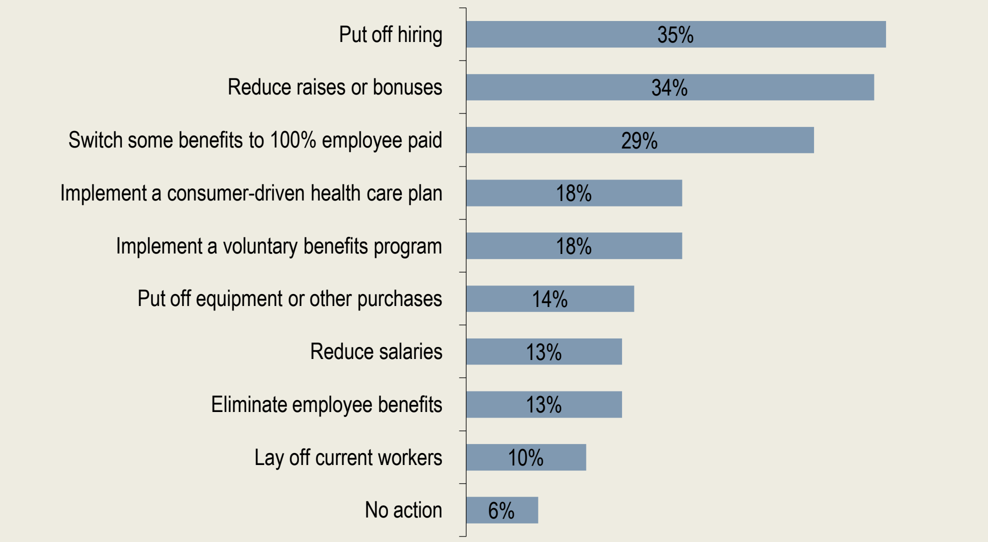
[15] "Employer Health Benefits: 2010 Summary of Findings," No. 8086, The Kaiser Family Foundation and Health Research & Educational Trust

[16] Fronstin, Paul, "The Impact of the Recession on Employment-Based Health Coverage," *Employee Benefits Research Institute Issue Brief*, No. 342, May 2010.

[17] Helman, Ruth, Mathew Greenwald & Associates, Craig Copeland, and Jack VanDerhei, "The 2009 Retirement Confidence Survey: Economy Drives Confidence to Record Lows; Many Looking to Work Longer," *Employee Benefits Research Institute Issue Brief*, No. 328, April 2009.

[18] *Shifting Paradigms? Explaining Employee Benefits in the Midst of Economic Uncertainty*, LIMRA, 2010.

Figure 7 —
Employer Response to Escalating Health Care Costs Over the Next Three to Five Years
(Percent of employers with 10 or more employees)



Source: *Shifting Paradigms? Explaining Employee Benefits in the Midst of Economic Uncertainty,* LIMRA, 2010.

- Worksite marketing may be one of the beneficiaries of escalating health care costs: Nearly 3 in 10 employers say they may switch some benefits to 100 percent employee paid and 18 percent may implement voluntary benefits programs.
- One unsettling trend is the decline in the number of small employers offering group life insurance benefits.[19] This trend is reflected in the percentage of households covered by group life insurance, which has steadily declined over the past decade to 49 percent in 2010 from a peak of 54 percent in 1984.[20]
- In the voluntary benefits market, employer interest in voluntary worksite benefits is reflected in strong sales of critical illness, accident, and AD&D products.

[19] Ibid.

[20] *Household Trends in Life Insurance Ownership*, LIMRA, 2010.

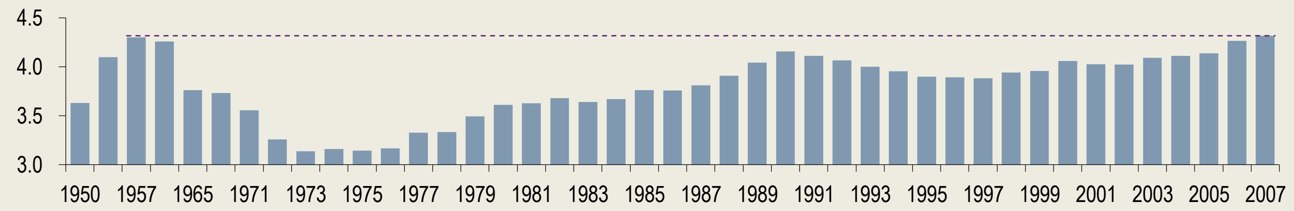
Changing Demographics

When most people think of America's changing demographics, they first cite the aging of the Baby Boom generation and its approaching retirement and then, perhaps, immigration and changes in the family structure, which are also shaping our future in profound ways. But some other profound changes are underway and have been little noticed.

Aging Population — Not So Fast

The nation achieved a little-noted milestone in 2007: The highest level of births in the nation's history was recorded (Figure 8). The prior record was set back in 1957 at the peak of what has become well known as "the Baby Boom." The first baby boom (from 1946 to 1964) had profound effects on social and economic trends, from raising the need for more schools in the 1950s and 1960s to altering consumer products companies' marketing imperatives. More recently it has been used to explain the impending drain in the cash reserves of Social Security and Medicare, not to mention a burden on the health care system. Census estimates put the over-65 population at 40.2 million, accounting for 12 percent of the national population. It is expected to grow by 16 percent by 2015, with double-digit growth continuing at least through 2025 (Table 3).

Figure 8 —
U.S. Births by Year
(Millions)



Source: U.S. Census Bureau

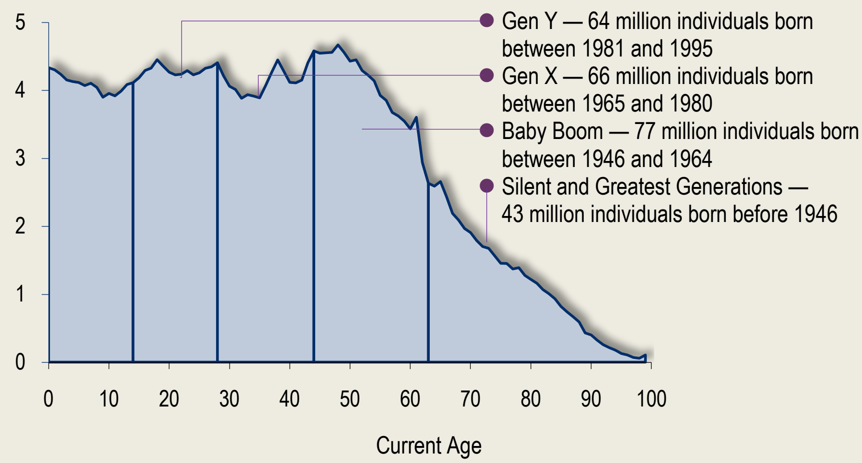
Table 3 —
The Over-65 Population, 2010–2020

	2010	2015	2020
Number over 65	40,229,000	46,837,000	54,804,000
Percent of total population	13%	14%	16%
Percent change from 2010		16%	36%

Source: U.S. Census Bureau

While the size of the older population will increase in absolute numbers, its proportion of the total population will not change dramatically (Figure 9). Gen Y (persons born between 1981 and 1995), which is almost as large as the Baby Boom generation, has kept the dependency burden (the ratio of those under and over working age to those of working age) constant for the past decade. However, as Gen Y enters the family years, the dependency ratio is expected to increase sharply, rising from 67 children and elderly people per 100 adults of working age in 2010 to 74 in 2020.[21] Gen X (persons born between 1965 and 1980), which is also almost as large as the Baby Boom generation, has entered the workforce and is the major reason for the rapid increase in households with young children. Like the Boomers, they will be caught in the middle between providing assistance and support to both young children and aging parents.

Figure 9 —
Generational Cohorts
(Population in millions)



Source: U.S. Census Bureau, LIMRA Analysis

Apart from generational differences in fertility levels, improved medical technologies are prolonging the lives of older Americans. For males, life expectation at age 65 increased between 1950 and 2006 by 4 years, to 17 years. For females it increased 5 years, to 20 years.[22] While longevity has increased, life span has not and diseases of aging will continue to prey on the older population. Among older Americans, chronic conditions — particularly heart disease and cancer — are the predominant causes of death. Our national obsession with food in general, and unhealthy food in particular, has led to high incidences of obesity (7 in 10 adults 20 to 74 years of age are overweight or obese) and high blood pressure (3 in 10 adults 20 and over are hypertensive) both of which will exacerbate the risks of chronic conditions as the population ages.[23]

[21] *The Next Four Decades — The Older Population in the U.S.: 2010–2050*, U.S. Census Bureau, May 2010.

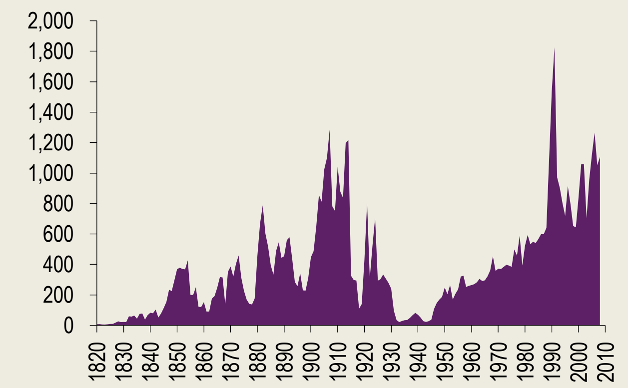
[22] Centers for Disease Control and Prevention, National Center for Health Statistics.

[23] CDC/NCHS, *Health United States*, 2009.

A Diversity of Markets

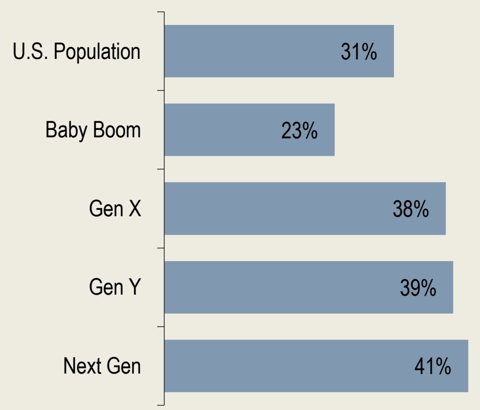
The growing diversity of markets doesn't end with age. The nation's cultural diversity increased significantly in the past two decades. The U.S. Census Bureau forecasts over the next five years that the Hispanic population will grow three times as fast as other ethnic groups. Asian American and African American populations will grow nearly as fast as Caucasian American population. Fostering these demographic changes has been a legal immigration wave larger than European immigration wave in the early 1900s (Figure 10). The magnitude of the recent wave was unanticipated — and the effects by age group are significant. Currently, 1 out of 4 Boomers is Hispanic or nonwhite. Among the nation's youth, more than 2 out of 5 are Hispanic or nonwhite (Figure 11).

Figure 10 —
Legal Immigration[24]
(Millions)



Source: U.S. Homeland Security

Figure 11 —
Hispanic and/or Nonwhite Population by Age Group
(Percent of age cohort)



Source: U.S. Census Bureau

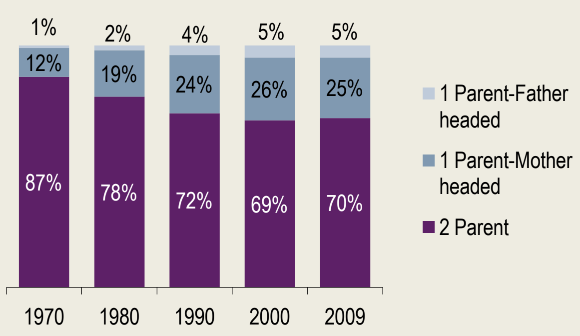
The evolution of immigration in the U.S. has wrought widespread changes in both the appearance and cultural fabric of the country. In the past four decades, white non-Hispanics have dropped from 83 percent of the population to 69 percent. During this period, those identifying themselves as Hispanic tripled. What is more, the mix of immigrants within these broad categories has changed. Traditionally Mexican and Puerto Rican, Hispanic immigration waves have included Cubans in the 1960s and a variety of Central and South American nationalities since then. Asian immigration, once largely Chinese and Japanese, has increasingly included Filipino, Vietnamese, and Indians. Just as in the early days of this country, these groups come with their own languages, attitudes toward family and elder care, and predispositions to save, spend, and protect.

[24] U.S. Homeland Security

Changing Family Paradigm

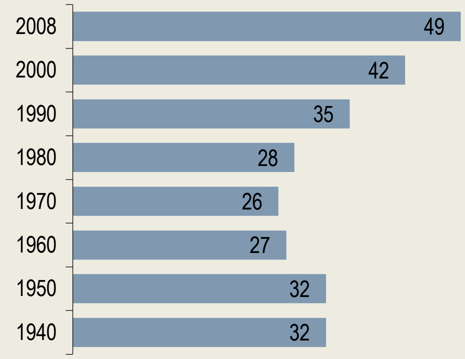
In America, the definition of what makes a family has been evolving. While two-parent households still predominate, one-parent households have more than doubled since 1970, accounting now for 30 percent of total family households (Figure 12). During the same period, nonfamily households have almost doubled and now represent one third of all households.[25]

Figure 12 — Changes in Traditional Family Structure, 1970–2009
(Percent of households)



Source: U.S. Census Bureau

Figure 13 — Multigenerational Family Households, 1940–2008
(Millions)



Source: U.S. Census Bureau

Within the family unit, changes are happening as well:

- The transformation evolution from extended family situations to the nuclear family is coming full circle as older children come "home" to live, contributing to what some have termed "the changing timetable for adulthood" (Figure 13). The comfort, care, and financial support provided by parents in combination with older ages at marriage are delaying the transition to adult obligations.[26]
- At the other end of the spectrum, some older adults, often in poor health or with diminished financial resources, are increasingly coming to live with their children (20 percent of those 65 and older.)[27] In other cases, grand-parents are raising grandchildren for at least part of the day. In fact, about 6 million grandparents live with their grandchildren and 4 in 10 of these have responsibility for them.[28]

In 2008, according to the Pew Research Center, 49 million Americans (16.1 percent of the total U.S. population) lived in households containing adults of multiple generations. This has resulted from multiple factors including delayed marriages and the immigration of Latin Americans and Asians, who are more inclined to live in multigenerational households. The Great Recession has also played a role, with the number living in multigenerational households increasing by 2.6 million between 2007 and 2008.[29]

---

[25] Current Population Survey, Table HH-1 Households by Type: 1940 to Present, March and Annual Social and Economic Supplements, 2009 and earlier, Internet release, U.S. Census Bureau, January 2009.

[26] Henig, Robin Marantz, "What Is It About 20-Somethings?" *New York Times*, August 18, 2010.

[27] Pew Research Center, "The Return of the Multi-Generational Family Household," March 18, 2010.

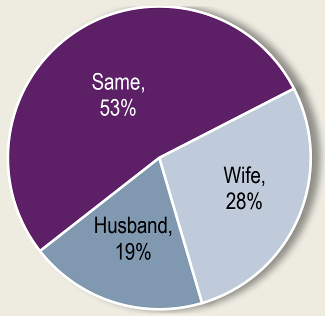
[28] 2006-2008 American Community Survey, U.S. Census Bureau, www.census.gov.

[29] Pew Research Center

There have been other changes as well. Growth in single-parent families has been fueled by high divorce rates. After remarriage, however, many become blended families. Same-sex households with dependent children are becoming more common despite the lack of legal sanction in most jurisdictions.

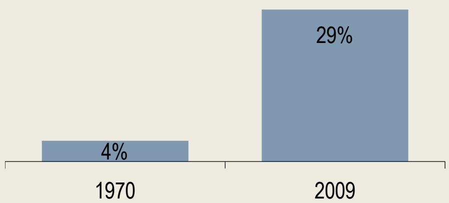
Within the family, another dynamic is at play. Not only have women become a significant part of the labor force in recent decades, in recent years they have outpaced men in education and, in some cases, income (Figure 14). In 2007, 54 percent of college graduates were women, up from 36 percent in 1970. During this same period, the share of husbands whose wives earn more than they do has increased from 4 percent to 29 percent (Figure 15).

Figure 14 —
Spouse With More Formal Education
(Based on married couples)



Source: Pew Research Center

Figure 15 —
Wives Earning More Than Husbands
(Based on married couples)



Source: Pew Research Center

Implications

The three main demographic groups for the industry's products and services are not very different in size based on number of households. This points to a steady stream of new buyers, given that the majority of life insurance is sold to households between ages 30 and 55. Add annuities and health-related products, which appeal to older people, and the outlook is quite positive. In short, the industry has a steady stream of customers in one market and a growing number of customers in another market. Other key implications:

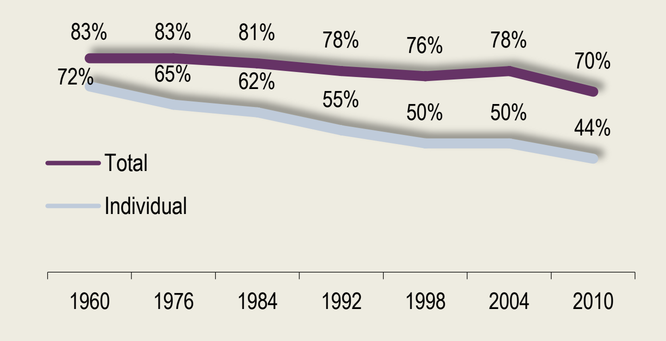
- The demographic trends point to an increasingly diverse customer base, which requires market segmentation in developing product, distribution, and marketing strategies that appeal to targeted customers. Four methods of segmenting customers will prove quite useful (Table 4).

Table 4 —
Customer Segmentation Methods

Basis of Segmentation	Sample Measures for Segmenting Customers
Demographics	Age, income, gender, geography, ethnicity
Economics	Customer revenue, transaction costs, and lifetime value
Attitudes	Brand loyalty, financial orientation, channel preference
Behaviors	Products owned, spending patterns, channel use

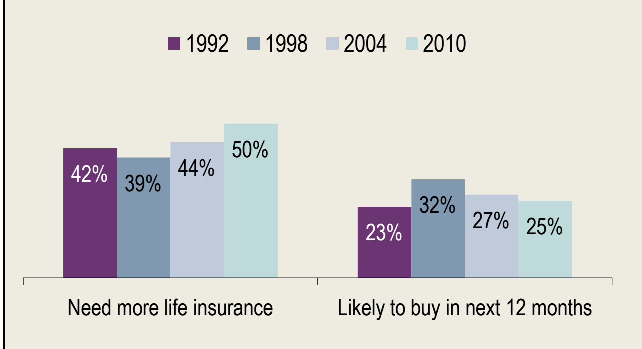
- Life stage and affluence remain the cornerstones in constructing demographic segments, but changes to social norms and recent immigration trends now require incorporating gender, ethnicity, education, and family structure.
- Attitudinal segmentation, although difficult to construct, is needed to address how to engage consumers. Attitude includes basic customer characteristics such as brand loyalty and trust, which have been greatly altered by the recession.
- Attitudinal segmentation should also include the customer's awareness of the need for the industry's various products and services. For example, even though customers have assumed more personal responsibility for planning their retirement and health care spending, many lack the skills or desire to manage these choices on their own. Hence, understanding whether the customer is advisor-driven or self-directed in making purchase decisions helps formulate a distribution strategy.
- Behavior includes tracking channel usage, which is not easy today given the diversity of channels.
- The fact that a 50-year decline in the percentage of households owning individual life insurance coincides with a record number of households saying they need more life insurance illustrates the importance of segmentation. Demographics alone do not explain these phenomena (Figure 16).
- One out of two households recognizes the need for more life insurance and 25 percent say they are likely to buy in the next year. However, similar results were recorded in 2004, yet ownership continues to decline — a trend demonstrating the difficulty the industry has in inspiring consumers to fulfill a recognized need (Figure 17).

Figure 16 —
Life Insurance Ownership
(Percent of households owning group or individual life insurance)



Source: LIMRA

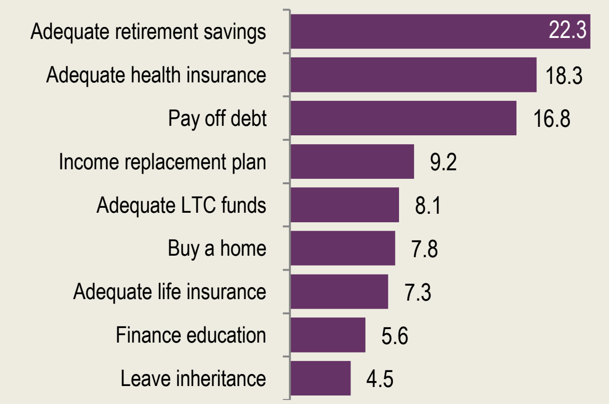
Figure 17 —
Households Recognizing the Need for Life Insurance
(Percent of households)



Source: LIMRA

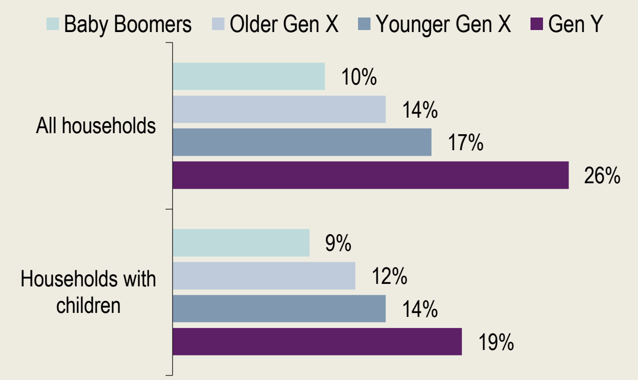
- Marketing strategies should recognize that the industry's customers have many priorities and too few dollars to meet them all. When consumers were recently asked to allocate 100 points across a variety of financial priorities, the three priorities garnering the most points were saving for retirement, having adequate health insurance, and paying off debt (Figure 18).
- The industry also needs to assess its effectiveness at reaching younger generations. Historically, the obvious holds true: The percentage of persons owning life insurance increases with age (Figure 19). What is not certain: Will members of Gen X and Gen Y behave similarly to Boomers or will the percentage of each successive generation owning individual life insurance continue to decline? What *is* certain is that the way we market to Gen X and Gen Y will be very different.

Figure 18 —
Too Many Priorities, Too Few Dollars
(100 Points allocated across household priorities)



Source: LIMRA

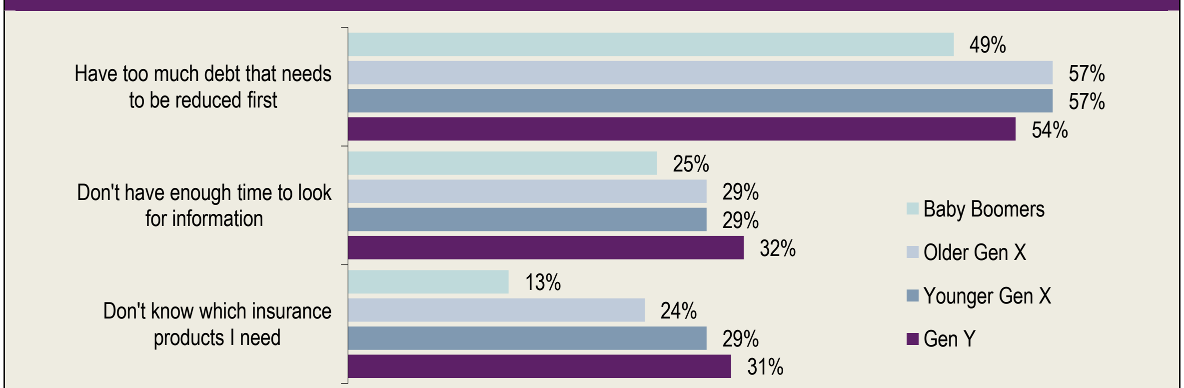
Figure 19 —
Households Without Life Insurance
(Percent of households)



Source: LIMRA

Despite being among the best educated, younger generations highlight the chronic problem the nation faces with financial literacy. Illustrating the point is the much higher percentage of young customers who feel they do not know which insurance products they need to address their financial needs (Figure 20).

Figure 20 —
Generational Cohorts
(Population in millions)

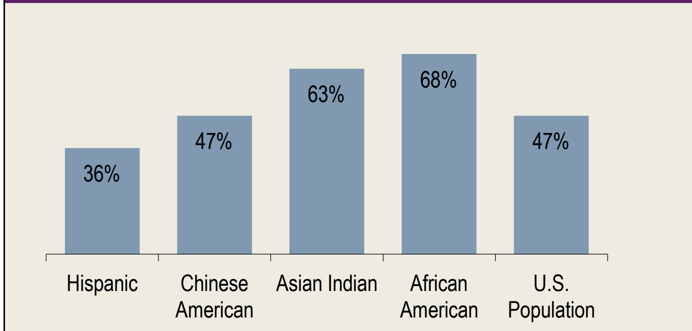


Source: LIMRA

The industry must also be more effective at reaching certain multicultural markets, particularly Hispanic and Chinese American customers (Figure 21). Age explains some of the differences in life insurance ownership, as Hispanic and Chinese American households tend to be younger than those in traditional life insurance markets. But age does not explain all of the differences. Culture also plays a large role: African Americans have lower tolerance for risk than does the general population.

- African Americans express greater interest in the concept of annuities than does the general population.
- Hispanic households often span multiple generations.
- Hispanic households prefer in-language material.
- Chinese Americans are savings oriented.
- Chinese Americans are more concerned than the general population about premature death.
- Chinese Americans prefer in-language material.

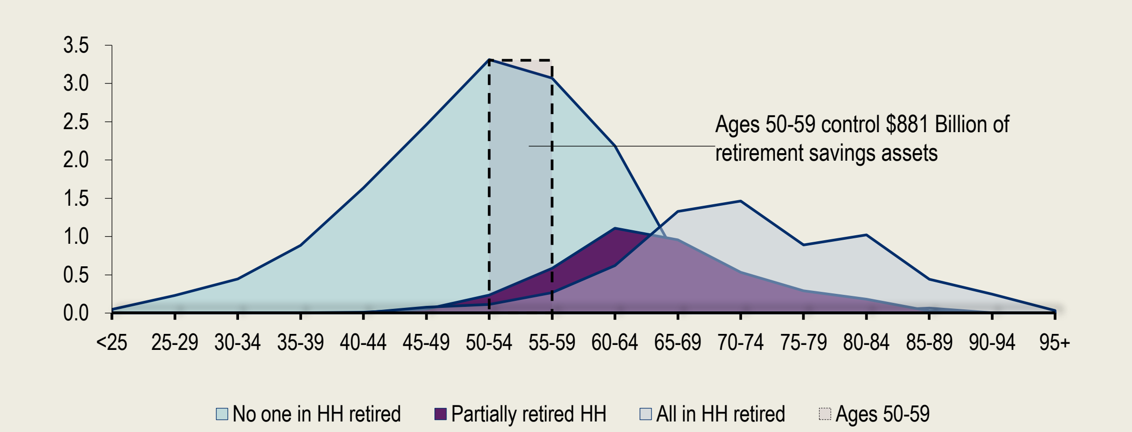
Figure 21 —
Individual Life Insurance Ownership by Ethnicity
(Percent of households with incomes $25,000 and over)



Source: LIMRA

Another major new opportunity for the industry will be clearly defining its role in the large and rapidly growing market for retirement products. Over the next five years, nearly $1 trillion of retirement savings assets will enter the retail market (Figure 22). Capitalizing on this emerging opportunity will require better understanding the needs of both customers approaching retirement and customers already retired.

Figure 22 —
Investable Assets by Age
(Assets in $ trillions)



Source: LIMRA

- Nearly 1 in 2 customers ages 55 to 80 express interest in a guaranteed income product — which represents market potential of nearly $250 billion. A major industry impediment to meeting this demand is the public's limited understanding of how immediate annuities can play a role in retirement income planning.
- Another key to serving the retirement marketplace is ensuring that distributors understand how customers perceive the relative importance of various retirement risks. Currently, the risks retirees are most concerned about in retirement, meaning their priorities, are not aligned with the risks advisors see for them. For example, despite the very low inflation environment, inflation is retirees' number two concern. Advisors rank it last (Table 5).

**Table 5 —
Relative Importance of Various Risks in Retirement**

Priority	How Retirees Rank Risks Faced in Retirement	How Advisors Rank Risks Faced in Retirement
1	Health care	Longevity
2	Inflation	Volatility
3	Volatility	Health care
4	Longevity	Inflation

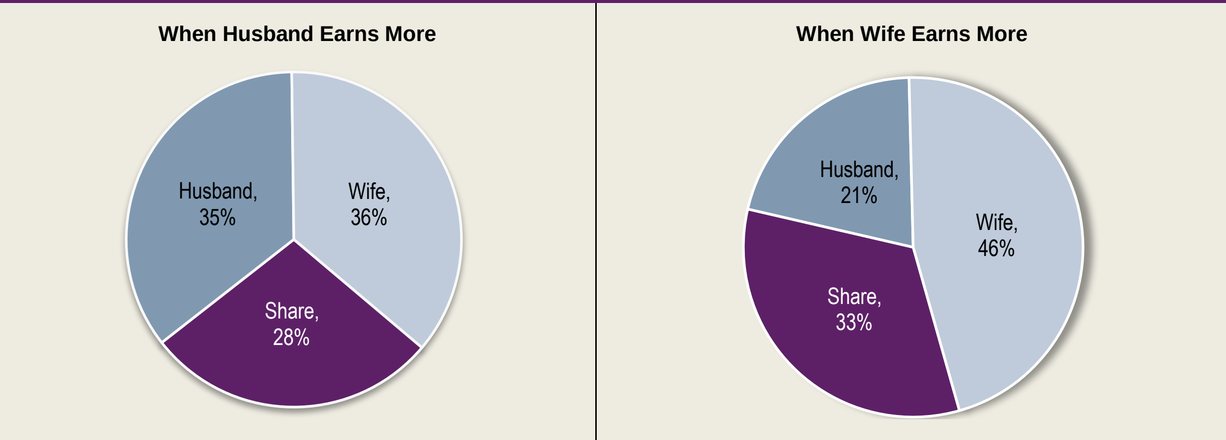
Source: LIMRA

- Products and services should address the issues sales representatives and advisors most often encounter in working with clients in or near retirement. Their clients often:
  - — Do not have a good idea of how much they spend
  - — Struggle with the concept of a sustainable withdrawal rate from retirement savings
  - — Become ultraconservative in how they invest when they retire
  - — Are challenged by low yields on most savings products and taking appropriate action
  - — Need to address personal issues (e.g., parents need to help the kids) that can have a major impact on planning
  - — Struggle to keep up with the ever-changing tax code

Another market, in which the industry's efforts are yielding some positive results, is the women's market. Today, 43 percent of life insurance policies are sold to women.[30] These marketing efforts remain important and future product development and sales materials must continue to reflect the perspectives of the two genders. However, do not simply segment clients by gender — also factor into this segmentation other important trends (Figure 23)[31]:

- In over half of households where the husband earns more, the wife makes the financial decisions or shares that responsibility with her husband.
- In households where the wife earns more, three fourths of the time the wife makes the financial decisions or shares that responsibility with her husband.

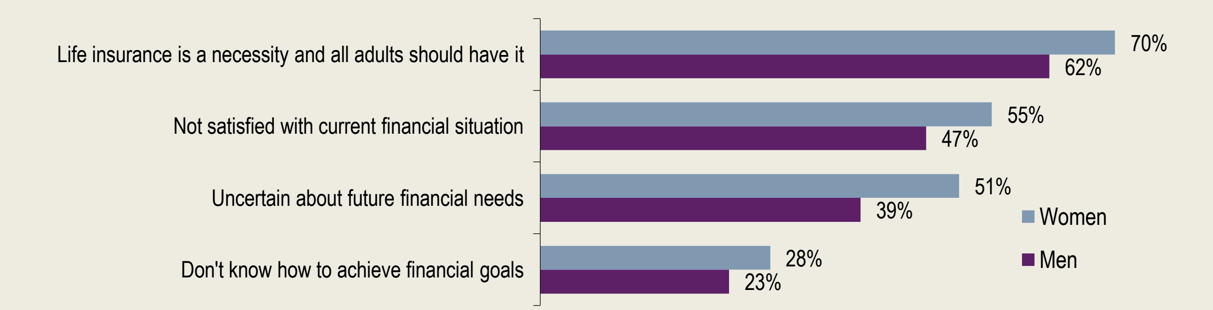
Figure 23 —
How Household Financial Decisions Are Made
(Percent of married couples)



Source: Pew Research

In many areas of achieving financial security, women are generally more receptive to the industry's products and services than are men. Of particular note: 70 percent of women consider life insurance a necessity compared with 62 percent of men (Figure 24).

Figure 24 —
Financial Perspectives by Gender



Source: LIMRA

[30] Life Insurance Buyer Study, LIMRA, 2010.

[31] *Women Call the Shots at Home; Public Mixed on Gender Roles in Jobs*, Pew Research, 2008.

Technological Innovation

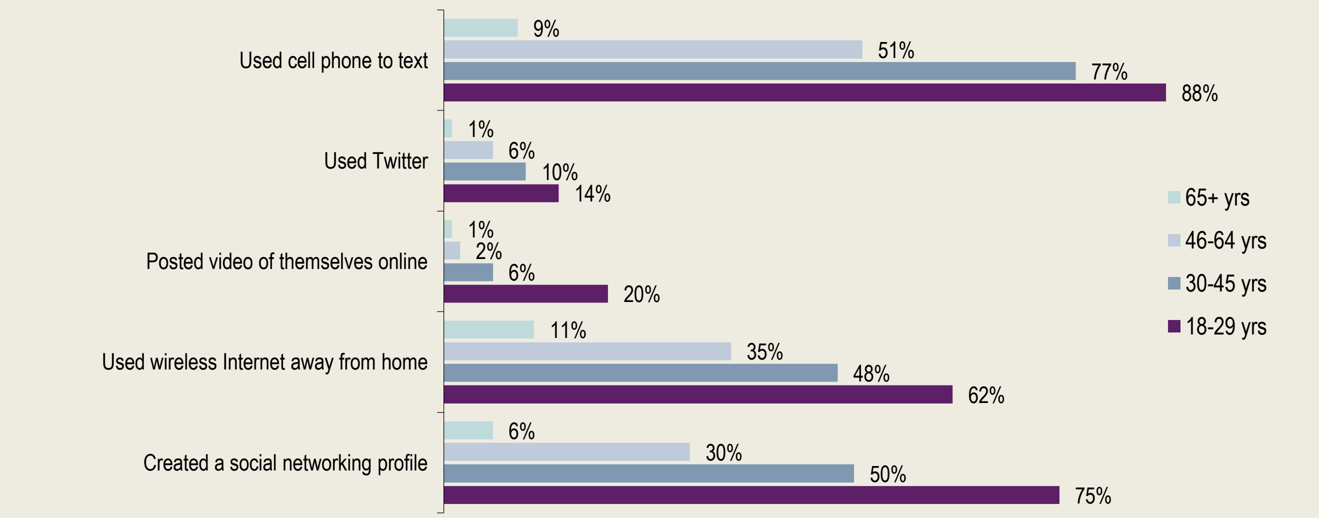
Technology begets technology and the process seems to go at an ever-quicker pace. One need only think back to 1997 when only 18 percent of U.S. households had Internet access and the idea of online shopping, banking, and bill paying was not on the radar screen for most Americans.[32] Today, a great number of people "trust" e-commerce, and online transactions have grown dramatically from essentially zero in 1995 to over $130 billion in 2009.[33]

Wired Society and the Self-Service Model

With each passing year, the Internet is increasingly becoming all-encompassing — a trusted and necessary part of daily life. In fact, we are nearing a time in which our customers will no longer perform the action of going online but rather, they will always be online. According to the Pew Internet and American Life Project, 6 in 10 American adults are now wireless Internet users through either a laptop or a cell phone (Figure 25). Laptop computers are owned by 55 percent of American adults, just shy of the 62 percent who own desktop machines. Cell phones are owned by 82 percent of adults.[34] More and more cell phones have wireless Internet capability.

Regardless of how they use the new technology, Americans feel that the digital revolution has made life easier (64 percent), brought people closer together (50 percent), and allowed them to use their time more efficiently (52 percent). For many, it has become the second major content provider for news.[35]

Figure 25 —
Public's Use of Various Technologies by Generation
(Percent of generation cohort)



Source: Pew Research

[32] *Current Population Survey*, U.S. Census Bureau, February 2010.

[33] *The 2010 Statistical Abstract*, U.S. Census Bureau, Table 1021.

[34] "Mobile Access 2010," Pew Research Center, July 7, 2010.

[35] "Millennials, A Portrait of Generation Next," Pew Research Center, February 2010.

We might consider social networking a new center of influence. Its use is one of the most noticeable differences between older and younger generations. The vast majority of Gen Yers use some form of online social networking. In contrast, Boomers lag behind their younger counterparts in using the new technology for staying in touch. The industry's challenge is defining what social networking is and how to leverage it as a communications channel (Figure 25).

The abundance of different online social networking activities has led Forrester Research to classify people into seven different categories based on how they use social media technologies (Table 6).[36] The research uses 20 different online activities to classify individuals into a hierarchy of social networking. The research illustrates the complexity in defining and understanding these new media. It also highlights the challenges of incorporating the media into marketing strategies. Yet their influence in capturing people's attention cannot be ignored.

Table 6 —
Forrester Research Social Technographics Ladder
(Percent of individuals online)

Classification	Person Performs at Least One of These Activities Monthly
Creators (24%)	Publish a blog Publish own Web page Create and upload video Create and upload audio/music Write and post article or story
Conversationalists (33%)	Update status on a social networking site Post update on Twitter
Critics (37%)	Post rating/review of product or service Comment on someone else's blog Contribute to online forum Contribute to/edit article in a wiki
Collectors (20%)	Use RSS feed "Vote" for Web site online Add "tag" to Web page or photo
Joiners (59%)	Maintain profile on a social networking site Visit social networking site
Spectators (70%)	Read blog Listen to podcast Watch video from another user Read online forum Read customer rating/review
Inactives (19%)	None of the above

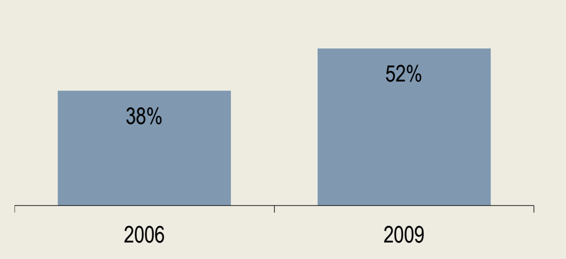
[36] *Groundswell: Winning in a World Transformed by Social Technologies*, Forrester Research, 2008.

Furthermore, our customers are increasingly using the Internet to manage their finances. In a 2009 LIMRA study, 3 in 4 middle market adults said they use the Internet to view bank statements. Smaller percentages said they use it to read financial advice, obtain information about financial investments, and obtain information about automobile and homeowners' insurance.[37] Other LIMRA research indicates a growing interest among online consumers in researching individual insurance and annuities.[38]

The 2009 LIMRA study showed that while only 12 percent of consumers used the Internet to obtain information about life insurance in the past 12 months, this percentage rises dramatically when the consumers surveyed are actually in the market to buy life insurance. According to the same study on consumer Internet use, about half of middle-market consumers had used the Internet for information when shopping for life insurance in the past 24 months.[39]

Other LIMRA research also shows recent growth in the marketplace. For example, 52 percent of consumers in 2009 who sought information on individual insurance or annuities looked online, in comparison with only 38 percent in 2006 (Figure 26).[40] This type of growth in online search mirrors that of what other burgeoning online industries saw before those models became successful. The most common online sources are insurance companies' Web sites.

Figure 26 —
Consumer Use of Internet for Insurance Information



Source: LIMRA

Other statistics from the same study include:

- Consumers who sought information in 2009 are significantly less likely, relative to 2006, to consider insurance professionals their *most valuable* information source. Instead, they assign greater confidence to employers, people they know, and insurance company Internet sites.
- The Internet is considered both a good source of information (86 percent) and advice (73 percent); both perceived values have increased significantly since 2006.
- The number of consumers who have purchased individual insurance or annuity products online has doubled since 2006 to about 1 in 7 online consumers.

Generational differences in attitudes toward the online world and using self-service models are no surprise. As one would expect, each successive age bracket shows less concern about agent-client trust and privacy issues. Older generations view the traditional life insurance salesman knocking on doors as the classic model. Boomers are aware of the practice, but are far more familiar with visiting their representatives at their offices. Generations X and Y, however, are becoming increasingly comfortable with completing entire transactions — from educating themselves about the products, to comparison shopping, to seeking peer-review ratings and comments, to finalizing purchases — all online.

---

[37] *Is There Magic in the Middle Market? Distribution Preferences and Internet Use,* LIMRA, 2009.

[38] *Trends in Consumer Internet Use for Insurance,* LIMRA, 2009.

[39] Ibid.

[40] Ibid.

These changes are pervasive online. Leads and word-of-mouth are now spread over the entire world via the Internet. While that may not help sales representatives and financial advisors who rely on face-to-face meetings, the younger generations of representatives, advisors, and consumers will be positively affected by this change. In the past, one trusted recommendation from a friend or family member could generate one sale. Online, one may trust 10 or 15 recommendations from unknown sources to generate a sale, but instead of a one-to-one ratio, the model may be more like 15 positive online reviews to 20 sales.

Privacy

The amount of personal and confidential information that is being used and shared in various electronic applications is staggering — as is the ease with which it can fall into the wrong hands. The need for privacy has spawned its own industry and captured the attention of business and political leaders alike with concerns running the gamut from simple nosiness to disclosure of sensitive information to identity theft. The Privacy Rights Clearinghouse has estimated that 500 million sensitive records have been breached since 2005.[41]

Once a consumer researches the different types of insurance available and perhaps surfs through various financial Web pages, the next step is to compare policies and prices. Many insurance companies provide baseline prices online today, but consumers cannot know their specific rates without completing a health diagnosis (and more specifically, blood work).

Again, we see marked generational differences in how people perceive privacy issues online (Table 7). A 2009 Pew Research survey shows that teens and Generation Yers are far more likely than older groups to use social networking sites (which often involve posting personal information) and create blogs.

Table 7 — Generational Differences in Online Activities[42]

	Gen Y (18–32)	Gen X (33–44)	Baby Boom (45–63)	Silent Gen (64–72)	Greatest Gen (73+)
Go online	87%	82%	75%	56%	31%
Use social networking sites	67	36	14	5	4
Create a blog	20	10	6	6	6
Get health information	69	82	77	70	67
Buy something online	71	80	70	56	47
Research products	84	84	81	73	60

Source: Pew Research

Consumers are now expressing greater interest in control over personal information; for example, 59 percent of adults have refused to provide information to a business or company because they thought it was not really necessary or was too personal. Yet, many people are still uploading their work histories to LinkedIn, or their photos to Flickr, or

[41] "500 Million Sensitive Records Breached Since 2005," Privacy Rights Clearinghouse, August 26, 2010.

[42] "Generational Differences in Online Activity," Pew Research Center, January 2009.

their personal musings to Facebook, choosing to connect their online identities with these key pieces of personal information.[43]

Implications

The growing interest in online insurance product research is expected to increase over time, perhaps at a very fast rate. We do not have comprehensive data for the financial and insurance industries dating very far back, but LIMRA has conducted some relevant research on consumers' online behavior. Two major hurdles to overcome for online life insurance sales are the potential lack of trust/impersonal nature of the Internet and a deficit in consumer product knowledge. As a result, the self-service model is gaining traction faster in the online insurance marketplace than online sales.

This trend highlights the importance of understanding what triggers a consumer to recognize a need for insurance and then to search online for product information. Not surprisingly, the triggers are significantly different by age (Table 8). However, one trigger most generations have in common is "Information through my employer" — once again illustrating the important role the workplace can have in reaching customers.

Table 8 —
What Prompts Consumers to Search Online[44]
(Percent of responses by age)

Triggers	All	Gen Y	Young Gen X	Older Gen X	Baby Boom	Silent Generation
Life event (e.g., marriage, birth, death of someone you know)	24%	30%	34%	26%	18%	17%
Advice from friends, relatives, or coworkers	23	30	31	24	18	18
Advice from an insurance professional	23	17	20	25	22	32
Information through my employer	22	24	24	22	24	9
Something in the mail	16	8	8	10	21	24
Got a job or a new job	11	27	15	10	7	2
Information online	8	5	6	9	9	5
Ad or print source (not online)	6	5	4	4	7	8
Email	6	4	6	6	7	8
Became unemployed/retired	5	4	3	4	6	8

Note: Columns add to more than 100 percent because multiple responses were allowed.

Source: LIMRA

[43] "Privacy Implications of Fast, Mobile Internet Access," Pew Research Center, February 2008.

[44] *Trends in Consumer Internet Use for Insurance,* LIMRA, 2009.

Accessible, professional, and easily navigated Web sites as well as social media (Twitter, Facebook, etc.) usage may drive more sales in the next three to five years. Although online sales models are promising, life insurance products do not readily or easily lend themselves to online sales, simply because they are too complicated. Also, trust is still an essential component of life insurance sales, and consumers may not be ready to trust an online sales model yet.

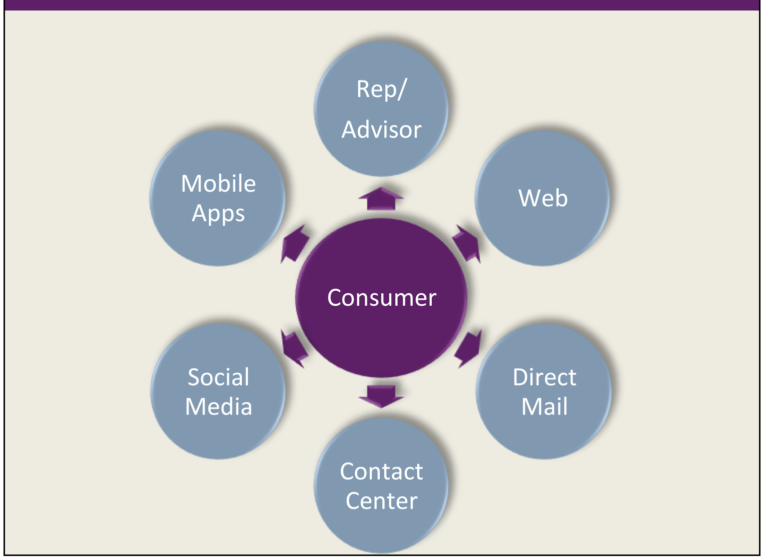
Along those lines, consumers would be more interested in buying online if they understood the product and someone were available to talk with them on the phone.[45]

- 40 percent of those surveyed would prefer a toll-free number to call with questions
- 17 percent (a doubling of the 2006 number) would be apt to use online chat

The industry will need to adapt as technology improves and each successive generation becomes more comfortable with an impersonal sales process. The customer experience is already being redefined by how we recognize and address this fundamental issue: When customers shop online for insurance and questions arise, their preferred contact method is calling the contact center. This customer expectation leads to very important implications:

- A well-trained contact center staff is critically important.
- The organization must have an integrated communication strategy across all channels.
- The organization must have an intimate understanding of not only how we communicate with our customers but also how they communicate with us (Figure 27).

Figure 27 —
How the Customer Communicates With Us



[45] *Trends in Consumer Internet Use for Insurance*, LIMRA, 2009.

Marketing and Distribution Trends

The old adage *insurance is sold not bought* has led to vast networks of sales representatives and financial advisors selling the industry's products on a one-on-one basis (Table 9). What's new is that all companies are engaging in multichannel distribution when considered from the vantage point of who and where — 'who' meaning the representatives selling and servicing the company's products and 'where' meaning the places they are sold and serviced. *Where* includes traditional methods such as at a customer's home, in a local office, through the mail, and over the phone. Of much greater importance today compared with the decades following World War II are the customer's workplace, contact centers, and the Internet. *Who* sells the industry's products has exploded in the past two decades and now includes seven different channels:

Table 9 —
Number of Representatives and Advisors by Sales Channel

Sales Channel	Total
Multiple-line exclusive agent	67,000
Career agent	104,000
Independent agent	151,000
National full-service rep	56,000
Regional and independent broker-dealer rep	75,000
Bank financial consultant	15,250
Independent financial advisor#	15,000
Estimated total*	**427,000**

Source: LIMRA, 2009

Estimate includes only advisors serving retail markets

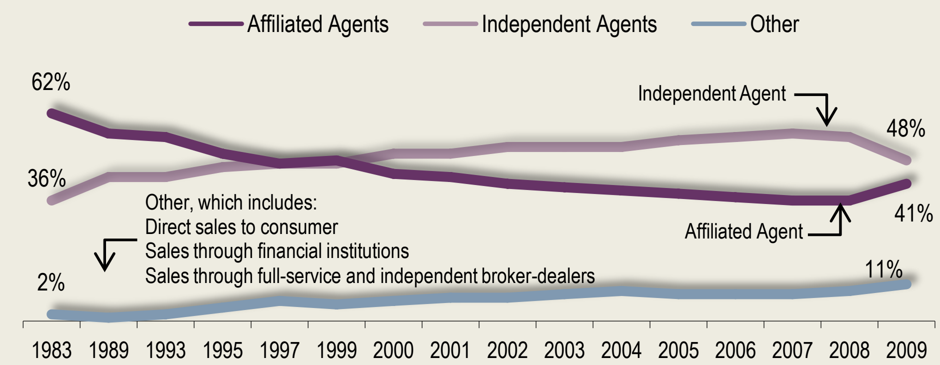
*Adjusted for: 1. Independent agents registered with independent broker dealers or independent registered investment advisors, and 2. Individuals dually registered as registered representatives and registered investment advisors.

- Multiple-line exclusive agents exclusively sell the products of one insurance company, with the preponderance of sales coming from property-casualty products.
- Career agents, with the preponderance of sales coming from life insurance and related products, are primarily affiliated with one insurance company but may also sell other companies' products.
- Independent agents are not affiliated with any one insurance company and sell the products of several companies.
- Full-service broker-dealer representatives are registered representatives employed by a national or regional full-service broker-dealer.
- Independent broker-dealer representatives are registered representatives working as independent contractors for broker-dealers.
- Banking representatives are registered representatives and insurance or annuity specialists employed by banks, credit unions, or savings and loans.
- Independent financial advisors are registered investment advisors (RIAs) or their investment advisor representatives.

Major Sales Channels

These seven sales forces are the primary sales channels for the industry's products and services. Individual life and annuity sales through the direct response and worksite marketing channels are increasing but still represent a small percentage of total sales (Figure 28 and Table 10). Individual health products are also primarily sold through agent channels or workplace channels, although direct response is becoming a significant channel for certain supplemental health insurance products.

Figure 28 —
Individual Life Insurance Sales by Distribution Channel
(Percent of annualized new premium)



Source: LIMRA

Table 10 —
Annuity Sales by Distribution Channel
(Percent of new deposits)

	1995	2000	2005	2009
Multiple-line exclusive and career agents	30%	22%	20%	21%
Independent agents	25	20	21	17
Full-service and independent broker-dealers	20	31	29	32
Banks and other savings institutions	14	16	18	19
Direct response	8	6	7	8
Other	4	5	4	4
Total	**100%**	**100%**	**100%**	**100%**

Source: LIMRA

Direct Response

Although direct response and affinity marketing represent less than 10 percent of new individual life and annuity premiums, they represent a much higher percentage of the policies sold. These sales channels are quite effective at reaching middle-income markets and include marketing through mass media and affinity groups.

Direct response to consumers represents 23 percent of new life insurance policies sold, 13 percent of new face amount, and 5 percent of new premium. Sales would be higher if not for the very high not-taken rate. Consumers searching for coverage through direct channels appear seriously interested in obtaining coverage, taking the time to schedule and even complete paramedical exams to determine their eligibility. But along the way something goes wrong, causing most of these consumers to abort the buying process. Many factors contribute to why some interested prospects do not complete the insurance buying process. But more often than not, the cost of coverage contributes in some way to this decision, as does the time it takes to issue a policy. Consumers, using online sales channels, are price sensitive and often initially select the lowest cost provider. They are also deterred by the length of time that it takes insurers to issue new policy. Consumers clearly expect quick turnaround once they have committed to buying. Close to half believe that no more than two weeks should elapse between the time they request coverage and when they have their policies in hand (Table 11). However, they also expect prompt and professional service, and will promptly consider alternative sources if they encounter inferior treatment. The message is simple to understand but difficult to execute: *Consumers want the best of both worlds*. Price is the primary attraction, but shopping experience will often make or break the deal.[46]

Table 11 —
Time Elapsed From Application to Policy Issue
(Percent of customers who purchased policies from other sources)

	Expected		Actual	
Less than 1 week	10%		12%	
1–2 weeks	35		16	
3–4 weeks	41		35	
5–6 weeks	11		17	
7–8 weeks	2	14%	6	37%
More than 8 weeks	1		14	

Source: LIMRA

Worksite Marketing

Access to voluntary worksite insurance products is quite good, with 81.7 million employees working for employers who offer at least one such product. Nearly all large employers (those with 1,000 or more employees) offer one or more worksite voluntary insurance product. However, only 1 in 2 smaller employers does so, and the pace at which these employers are adding worksite voluntary benefits has slowed considerably in recent years. The industry has long

[46] *The Case of the Disappearing Customers*, LIMRA and the Life Insurance Direct Marketing Association, 2009.

struggled with reaching the small employer segment, and now must overcome distractions from health care reform and the slow economy when trying to persuade these employers to consider voluntary benefits.

Cancer insurance and life insurance are the most commonly available worksite voluntary benefits offered, with nearly 3 in 10 of all U.S. firms with 10 or more workers sponsoring these plans on an employee-pays-all basis (Table 12). Several voluntary benefits offerings have seen a dramatic upswing in popularity over the past 10 years. These products include accident, accidental death and dismemberment, and critical illness.

Table 12 — Voluntary Worksite Benefit Offerings
(Percent of employers with 10 or more workers offering benefit)

Benefit	2002	2006	2010
Cancer	22%	29%	29%
Dental	16	17	19
Accident	18	24	20
Accidental death and dismemberment	12	17	16
Life	28	23	29
Critical illness	11	17	18
Supplemental medical	18	20	16
Vision	8	9	12
Long-term disability	17	20	20
Prescription drug	7	5	6
Short-term disability	16	20	19
"Mini" medical	Not available	3	3

Source: LIMRA

Contact Centers

Consumers have come to expect companies to offer multiple-service options. These expectations may have been kindled by other industries, but the imperative is clear — our consumers want to be able to choose their methods of receiving service. Thanks to advances in technology, consumers now have numerous choices for receiving customer service. They can take their pick of:

- Speaking to a customer service representative
- Calling an automated phone system
- Logging on to a Web site
- Sending an email
- Using a combination of any or all of these methods.

For the insurance industry, these self-service options supplement rather than supplant traditional service options. Customers will always want to have the option of calling their representatives for service, and most sales representatives prefer that their clients call them first. But there are times when self-service options benefit everyone. Allowing customers to conduct simple service tasks through an automated channel or the contact center can free up representatives for handling more complicated service issues.

Although an increasing number of contact centers are adding sales and lead generation to their responsibilities, the vast majority of contact centers' sole responsibility remains service. They service a wide variety of products and do not specialize in any particular product line. Nearly all centers offer service via a toll-free phone number, almost three quarters perform customer service via email, and close to two thirds of these companies provide service through their Web sites. Fewer companies offer interactive voice response (IVR) systems.

There is a great deal of difference in the costs of various service options (Table 13). A call to a customer service representative is, on average, over 12 times as expensive as an Internet transaction and eight times as expensive as a call to an IVR system. Emails from customers still require a response from staff, but cost about one third as much as an interaction on the telephone.

Table 13 —
Contact Methods and Costs[47]

Service Method	Percent of Companies Offering	Transaction
Toll free	95%	$6.41
Email	72	2.03
Internet	66	0.51
IVR	43	0.77

Source: LIMRA

Even though Purdue University's Center for Customer-Driven Quality, a leading research center on contact centers, expects a significant movement from phone communication to online communication for service transactions, such a changeover in the insurance and financial services industry has not yet occurred. From 2001 to 2010, the call volume to contact centers as a percentage of total communication decreased only slightly.[48]

Point-of-Sale Technology

If some is good then more is better. The list of marketing technology sales representatives (and financial advisors) use or plan to use is quite long (Table 14).[49] About 1 in 3 representatives currently use e-newsletters and videos with their clients and prospects, and another 1 in 4 plan to add these to their sales and service tools in the future. Webcasts, used by 22 percent of representatives now, will be used by an additional 20 percent in the near future. Relatively few representatives currently use other electronic media, such as instant messaging, blogs, forums, and social networking. Even though relatively few representatives use this new electronic media, usage will increase. In fact, while only 13 percent now use social networking with clients and prospects, an additional 13 percent of representatives plan to use it in the near future, doubling the number of representatives engaging clients and prospects in this way.

[47] *Policyowner Self-Service: Company Practices*, LIMRA, 2005.

[48] *Staffing Practices in Financial Services Contact Centers*, LIMRA, 2010.

[49] *Technology's Impact on Sales and Service: Individual Producer Technology Review*, LIMRA, 2010.

Table 14 —
Sales Representatives' Use of Electronic Media With Prospects and Clients
(Percent of sales representatives)

Media	Currently use	Do not use now, but plan to	Would use, but carrier prohibits	No interest
Email	87%	3%	3%	7%
Electronic newsletters	38	25	6	31
Educational videos	31	25	7	37
Webcasts	22	20	8	50
Text messages	22	10	11	57
Social networking sites (e.g., LinkedIn)	13	13	10	64
Instant messages	12	12	12	64
Discussion forums for clients/prospects	9	13	12	66
Podcasts	8	17	9	66
RSS feeds	3	14	7	76
Personal blogs	3	10	12	75
Microblogs (e.g., Twitter)	2	8	12	78

Source: LIMRA

Offer online functions and they will be used.[50] Of nine possible online functions, most sales representatives either currently have the function and use it or want to have it available (Table 15). At least 7 in 10 have and use pending business status, client account information, marketing materials, commission statements, downloadable new business applications, and reflexive forms. They are less likely to have available electronic signatures, prepopulated forms, and electronic submission of new business applications, but those who have them usually use them and those who do not have them now would like to have them in the future. The fastest growing technology application is electronic signature. The most important function to sales representatives is the ability to track pending business status.

[50] *Technology's Impact on Sales and Service: Individual Producer Technology Review,* LIMRA, 2010.

Table 15 —
Sales Representatives' Use of Various Sales and Servicing Technologies
(Percent of sales representatives)

Function	Have it now and use	Have it now and do not use	Do not have it, but want it	Do not have it; do not want it
Pending business status	89%	5%	5%	1%
Client account information	89	3	5	3
Marketing materials	85	9	4	2
Commission statements	82	6	7	5
New business applications: downloadable	80	6	8	6
Reflexive forms (i.e., can complete online)	73	10	12	5
New business applications: submit online	46	16	28	10
Prepopulated forms	43	12	31	14
Electronic signatures at the point of sale	27	17	43	13

Source: LIMRA

Implications

The implications of these marketing and distribution trends range from concerns over increasing sales capacity to leveraging the rapidly changing point-of-sale technology. The implications fall into four major areas:

- Sales capacity increased significantly in the 1990s but has recently stalled. To achieve growth, sales capacity, sales productivity, or both must increase.
- Financial diversification is no longer an aspiration but a reality for most organizations; this new reality will require a new sales office model.
- Point-of-sale technology is expensive but it can also be a competitive advantage. What confronts organizations is the innovator's dilemma: when to introduce new technologies.
- A major catalyst for fundamental change in how the industry's products are sold will be automated underwriting developments.

Increasing Sales Capacity

Since 1985, the number of insurance companies recruiting inexperienced sales representatives has declined from 220 companies to 73 in 2009. In an effort to lower distribution costs, many of these companies stopped recruiting inexperienced talent and moved their incumbent representatives to an independent affiliation model. This trend, which fueled the rapid growth in independent agent distribution during the 1990s, has ended. And, the cost advantages of independent distribution over affiliated distribution have diminished. Also contributing to the parity in effort between competing for inexperienced sales talent and competing for shelf space are two other trends:

- New agent recruiting has been fairly constant over the past two decades, averaging between 35,000 and 40,000 new recruits annually. This recruiting level is not sufficient to offset the number of agents leaving the industry.
- The affiliated agent channel is an important source of talent for the independent agent channel. A decline in the affiliated agent channel most likely will lead to a decline in the independent agent channel.
- The average number of active companies with which independent agents place business has dropped to 10, down from 13.[51]

Another contributor to increased competition for talent are the demographics of our current field force, which point to a decline in the number of sales representatives and financial advisors resulting from a growing number retiring. The median age of the U.S. worker is 37. Fifty percent of affiliated agents are over age 48 and 50 percent of independent agents and financial advisors are over age 52. The other channels are similar in age. The only exception is the bank sales channel, where the median age is 40. Factoring in the 1 in 4 representatives age 55 or older planning to retire or sell their practices within five years shows the industry facing a daunting task to build sales capacity.[52]

The decline in sales representative turnover offers some assistance with the task of increasing sales capacity — as does the high unemployment rate, which has made recruiting easier.[53] Even though sales representative turnover among insurance-oriented sales channels is improving, it remains at historically high levels. The turmoil in the investment and banking industries is not helping with retaining investment-oriented sales representatives; their turnover remains nearly double the rate for insurance-oriented channels.

[51] *Forces of Changes: Issues Facing Distribution Leaders*, LIMRA and McKinsey & Company, 2009.

[52] *New Games, New Rules: New Reality*, LIMRA & Moss Adams, 2008.

[53] *Affiliated Agent Recruiting for 2009*, LIMRA, 2010.

New Sales Office Model

Emerging among these seven major sales channels are two kinds of sales representatives and financial advisors: a traditionalist and a contemporary (Figures 29 and 30).[54] In the insurance-oriented channels, the traditionalist sells primarily insurance, which includes annuities and property/casualty products. The contemporary sells significantly more investment products. In the investment-oriented channels, the traditionalist's income is mainly from transacting commission-based sales. Insurance (primarily annuity products) does represent a significant portion of their sales. In contrast, the investment-oriented contemporary derives a higher portion of income from fee-based advisory services.

Figure 29 —
Sources of Revenue for Insurance-Oriented Sales Representatives and Advisors
(Percent of revenue)

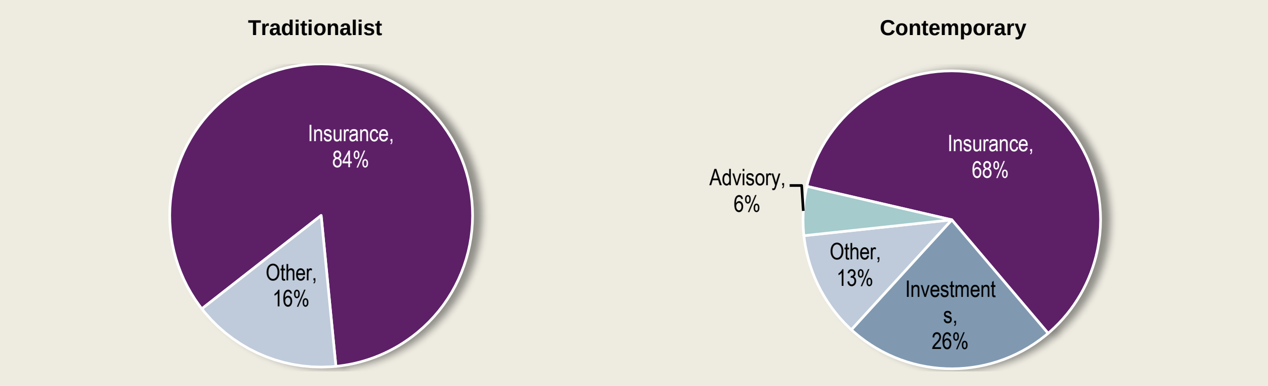
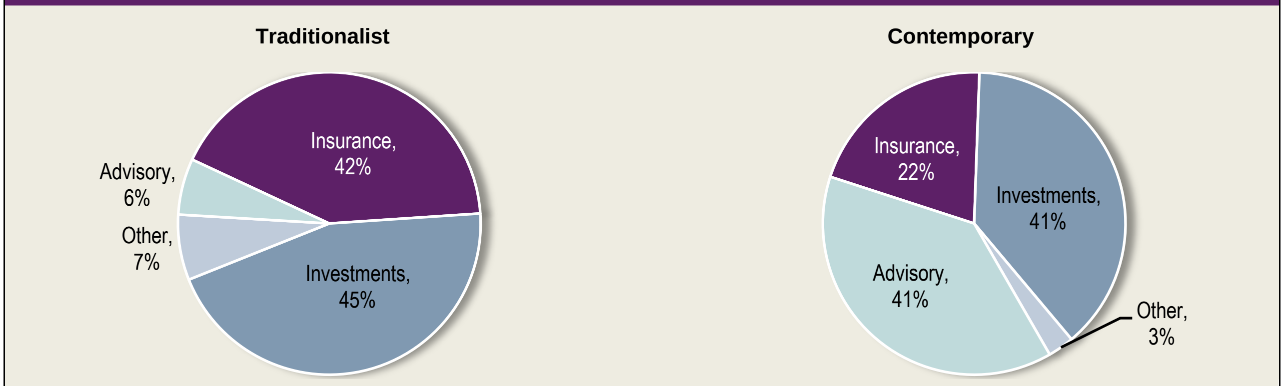


Figure 30 —
Sources of Revenue for Investment-Oriented Sales Representatives and Advisors
(Percent of revenue)

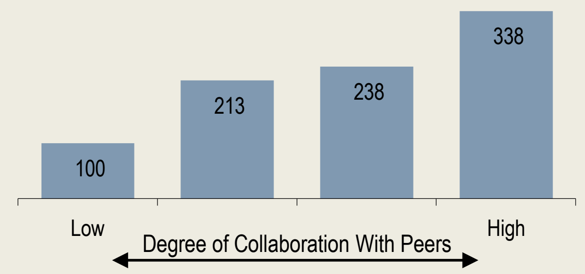


Source: LIMRA

[54] *Forces of Change: Issues Facing Distribution Leaders*, LIMRA and McKinsey & Company, 2009.

Adapting to the increasingly diverse and complex products they sell and markets they serve, sales representatives and financial advisors are building their practices around more collaboration with peers.[55] Many no longer practice solo but instead partner with their peers. Fairly uncommon 10 years ago, today nearly 1 in 8 are members of a permanent team, collaborating on finding new business, serving existing clients, and leveraging resources. These collaborative business models take on several forms. They may be organized by product, market, geography, skills, or mentorship arrangements. Skills-based and product-based teams are most prevalent. However, team focus often overlaps. For example, a product-based team will also incorporate elements of a market- or skills-based approach. Other characteristics of collaboration include:

Figure 31 —
Likelihood of Being a Top Performer by Degree of Collaboration With Peers and Other Professionals*



* Ratio of the percentage of representatives in the top income quartile to the percentage of representatives practicing as sole proprietors and in the top income quartile

Source: LIMRA

- Lower unit costs and increased likelihood of success — a representative who regularly collaborates with peers is three times as likely to be a top performer than a representative working solo (Figure 31).[56]
- Five or six people is the ideal number in a group; when the number is larger, the productivity per person starts declining.[57]

[55] *Forces of Change: Issues Facing Distribution Leaders*, LIMRA and McKinsey & Company, 2009.

[56] Being a top performer is defined as being in the top net income quartile.

[57] Klein, Katherine J., and Beng-Chong Lim, *Team Mental Models and Team Performance,* Journal of Organizational Behavior, January 2006.

The Innovator's Dilemma: Introducing New Technologies

Despite their similar ages, these two agents illustrate how much sales representatives' attitudes toward technology vary.[58] The majority is slow to adopt new technologies and would rather wait until they are well established — not surprising given the aging of the field force. However, the recent surge in recruiting younger talent has put companies in the position of meeting the demands of some who clamor for more technology tools while addressing the reservations of others who resist any change to their traditional sales and service methods. Despite the varying attitudes toward technology, all recognize its importance — in fact, 2 out of 3 sales representatives use some form of technology at the point of sale and 97 percent are interested in more technology training (Table 16).

I am a yellow pad agent.

— Agent, male, age 65

[The carrier's] Web site is huge; it is extremely easy to navigate. It makes it easy to do business with the carrier.

— Agent, male, age 65

Table 16 —
Sales Representatives' Self-Description on Technology Adoption

Representative's View Toward Adopting New Technologies	Percent of Representatives
Innovator: Intrigued by new technologies; aggressively pursue	10%
Early majority: Buy into new technology early in the life cycle	22
Moderate: Require well-established references before implementing technology	35
Late majority: Wait until the technology becomes well established	27
Laggard: Skeptical and resistant to the use of technology	6

Source: LIMRA

Advances in Underwriting

Advances in medical and information technologies are bringing fundamental change to the underwriting process.[59] The use of automated underwriting is still relatively low, but interest is high. A recent Society of Actuaries report defines an automated underwriting system as using technology to perform all or some of the screening functions traditionally completed by underwriters, and thus seeks to reduce the labor, time, and/or data necessary to underwrite an insurance application. It means more than replacing paper forms with electronic forms and managing workflow. It incorporates algorithms and heuristics to enable underwriting decisions.[60]

[58] *Technology's Impact on Sales and Service: Individual Producer Technology Review,* LIMRA, 2010.

[59] *Memories of the Future: Four Scenarios of the Life Insurance in the Year 2016*, LIMRA, 2007.

[60] *Automated Life Underwriting: Phase 2*, Society of Actuaries, 2010.

The Society of Actuaries report describes three categories of uses for automated underwriting:

- Alerting underwriters to risk factors by flagging items in the underwriting process that an underwriter must review more carefully. For example, a blood chemistry profile of an applicant will be submitted to the insurer, data will be loaded into the system, and user-defined logic will determine that the cholesterol level is out of range. This information, and any other items in the underwriting process exceeding the acceptable boundaries, will be included in a report to an underwriter. The underwriter then uses his or her judgment and knowledge of the underwriting guidelines to make an underwriting decision.
- Automating simplified or nonmedical underwriting for smaller face amounts (often up to $100,000 or $250,000). The systems capture a limited set of underwriting requirements, interpret the information received, and make underwriting decisions for most cases in a short period of time. The set of requirements processed varies slightly, but usually includes some combination of an application (either short-form, traditional, or reflexive questions), and data from the Medical Information Bureau (MIB), motor vehicle records (MVR), prescription drug (Rx) databases.
- Automating paramedical and medical underwriting translate underwriting manuals into rules-based automated system. After the applicant completes a full application with reflexive questions, the rules-based system assesses the information against the company's standard requirements and assigns an underwriting class. Companies are using automation to process the application and to retrieve information from MIB, MVR, and Rx databases, and lab results. If an attending physician statement (APS) or further requirements are necessary, the case will kick out of the automated system for a review by an underwriter.

Automated underwriting has implications not only for product design, but also for product distribution. If it is able to shorten the time frame from application to underwriting decision from weeks to minutes, automated underwriting will fundamentally change the sales process and the customer's shopping experience. The potential benefits include:

- Higher close ratios, which in turn mean higher sales productivity
- Better alignment of the life and health insurance sales process with the sales processes for other, more transaction-oriented financial services, thereby fostering better cross-selling opportunities
- Increase sales in nontraditional sales channels resistant to current underwriting procedures.

If the risks associated with automation are sufficiently mitigated, automated underwriting offers significant promise for the company and the customer.