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Editorial

A Time for Planning

by Linda B. Emory

Spring and summer are the times insurance companies participate in the management process that reaffirms or revises their strategic plan. It is a time to break away from day-to-day crisis management and to reset one's long-term aim — before the fall exercise in detailing the 1988 plan.

In this process, we look to what's happening in the external environment that will affect our business. We need to hear from people outside our industry like Carolyn Corbin (see her article beginning on page 1), and from people inside our industry like Lynn Merritt, President of L.O.M.A., who spoke at the Pacific Insurance Conference on "Strategies for Managing the Unforeseeable," and Dr. Kenneth Black, Jr., Regents Professor of Insurance, Georgia State University, who spoke in Tokyo, Japan, at The Research Institute of Life Insurance Welfare, on "The Future of the U.S. Life Insurance Industry."

Many keynote speakers on the future of our industry are our own members — Harold Ingraham spoke at the A.C.L.I. Investment Management Seminar on "The Life Insurance Industry in 1992"; Peter Walker presented "Leadership and Renewal — the Challenges Facing Life Insurance CEO's" at the A.C.L.I. Executive Round Table; and James C.H. Anderson gave "How We Got Where We Are Today... Where Do We Go From Here" at the LIMRA Annual Meeting last fall 1986. (Quotations in this editorial are taken from the preceding references.)

In their writings and presentations, these authors and speakers agree the insurance industry has experienced unprecedented change and that we must plan for continued turbulence in the foreseeable future. "These are the opportunity years, but not for the faint hearted," says Jim Anderson. He believes that to survive and succeed, "Most companies require new strategic initiative."

Ken Black notes the increasing globalization of financial services: from deregulation in the United Kingdom in 1986 — and the ability of one insurer licensed in the European Community (EC) to do business in another EC country — to the increased deregulation in Canada, to the partial opening of Japanese and other Asian markets. He remains confident in the prospects for continuing growth in the relatively "mature" U.S. life industry primarily due to increases in the number of U.S. households. Black noted the profound recent changes in U.S. products and pricing concepts. The new interest-sensitive products are complex; require sophisticated systems which create the need for additional capital investment and skill in managing technology; and have set the tone for a more competitive environment, replacements, and a squeeze on product profits. He notes that many companies are too small to have the managerial or financial resources "to meet the demands of the more competitive environment." The high distribution costs are a point of vulnerability for our industry. Black states, "Many companies have tried to meet the need for greater sales force productivity by market segmentation.... Competition for sales at the upper end of the income spectrum...seems to have reached a point of diminishing returns."

Lynn Merritt comments, "The insurance industry faces changes brought on by competition from other financial institutions, in demands for new products, in growing complexity of automated systems, and in the regulatory environment." He believes management of the planning process, technology, and people are the keys to coping with the unforeseeable. "Planning is critical in three areas: responding to the external environment, maintaining a competitive edge, and maintaining financial stability," he says.

Harold Ingraham believes there are six significant forces of change which will impact the competitive equilibrium in the next several years: 1) possible financial services deregulation; 2) demographic trends as America ages and the number of Asian and Hispanic immigrants grows; 3) AIDS; 4) modification in the distribution system to more leveled commissions, rebating, and producer-owned reinsurance companies; 5) possible regulatory changes to tax the inside build-up and single premium life and possible repeal of McCarran-Ferguson; and 6) surplus adequacy and solvency concerns stemming from the challenge to control the C-3 risk through both traditional and new investment vehicles and to optimize results to support the aggressive product pricing. Ingraham sees tomorrow's winners as those maintaining competitive advantage through 1) superior cost fundamentals; 2) preferred access to markets or distributors; 3) product/service differentiation which increases the chance of profit realization; 4) sharp focus — leading to cost efficiencies or differentiations; 5) superior implementation; and 6) merger or strategic acquisitions which result in economies of scale.

Jim Anderson dramatically states that companies have "four groups of strategic options...according to their intended or likely outcome." These are: 1) continued independence for those who can establish sustainable competitive viability based on superior cost fundamentals or on price and commission competitive avoidance; 2) merger of equals either to improve financial results or to change for the better the nature or scope of the business; 3) dressing up for sale or acquisition by another party; or 4) doing nothing and slowly and painfully declining with the eventual outcome of sale or acquisition on unfavorable terms.

On the implementation front, Peter Walker sees the challenge for the CEO to 1) understand product profit economics; 2) rationalize distribution channels; 3) attack costs; 4) address the changing investment requirements; 5) broaden competitive horizons; and 6) balance strategy and execution in the group health line.

We hope our companies have done a good job of developing a strategic initiative which will respond to how the environment may be expected to impact them. We can be sure there will also be the unexpected. These are the best of times; these are the worst of times. Change is challenging, exhilarating, and nervewracking.