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Life Insurers Seek to Capitalize on Middle-Market Opportunities

by Mark L. Trencher

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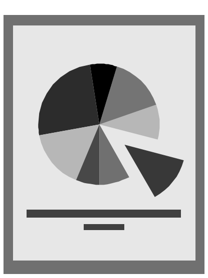
Most life insurance companies and agents continue to focus on the upscale market for good reason; it is profitable. The middle market has adopted a "buy term and save the difference" philosophy, but term life does not generate much profit for insurers or agents. To sell more profitable products to the more desirable upscale market, carriers provide a high level of face-to-face interaction with customers. Distribution channels providing such interaction have not been cost-effective in the middle market. Thus, over the past two decades, this segment has suffered from a growing "benign neglect" on the part of the insurance industry.

Although the upscale market still has growth opportunities, it is becoming increasingly saturated. At the same time, the number of middle-market households that are either uninsured or underinsured for life coverage is growing. In this environment, some carriers are rethinking their abstention from the middle market and are grappling with finding distribution channels to cost-effectively reach that market.

Conning surveyed life insurers in November 1998 to assess where they are focusing their distribution efforts. Many insurers expect this focus on the upscale market to persist over the next five years but are experimenting with new markets and new channels.

Channels With Middle-Market Potential



The gap in middle market individual life insurance will not be closed through heavy reliance on agents. So the problem remains: how can term life be "pushed" to the middle-income consumer—together with enough interactivity and financial planning support—in a cost-effective manner?

The levels of interactivity and financial planning support provided to buyers by the various distribution channels correlate with financial position (e.g., income and net worth) and financial needs. The middle market and lower markets will not have access again to the level of face-to-face interactivity they had 20 or 30 years ago and that is common in the upscale market today.

But a new set of distribution channels is emerging that may present a viable compromise by delivering a less labor-intensive form of interactivity to meet consumers' basic needs. Several of these (direct marketing, Internet, quote services, worksite marketing and bank distribution) have a significant middle-market orientation.

A growing number of carriers have adopted or are testing these channels. We expect insurers' middle-market individual life premiums generated by these channels to grow 19% annually, from $4.5 billion in 1998 to $10.8 billion by 2003.

Direct Marketing

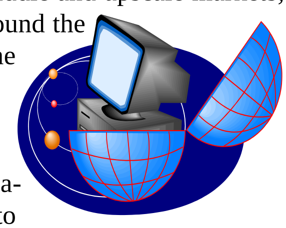
Direct marketing is one of a group of channels that we have collectively dubbed *Direc/Tech*—which also includes the Internet and quote lines—because they are more or less direct approaches that rely on technology to identify and interact with prospects. Also known as direct response, direct sales and direct mail, direct marketing has grown enormously in recent years, with $153 billion spent in the U.S. in 1997.

Many insurance companies are using direct marketing—most often direct mail—to sell certain products or generate leads for agents. While this sounds like an easy approach to adopt, success in this business is very much based on technology (the ability to segment and develop quality databases) and efficiencies of scale (which drives down the cost). The challenge for insurers lies in both areas. In particular, insurers will need to be better at using databases and data-mining tools to target their markets, as opposed to the current, often-used scattershot approach.

We forecast that direct marketing individual life sales in the middle market will reach $4.9 billion by 2003, representing 12.4% of the market, compared to 8.8% in 1998.

Internet and Quote lines

The Internet and toll-free quote lines straddle the middle and upscale markets; households around the $75,000 income level have higher-than-average computer sophistication, are used to buying products over the phone and typically are more interested in the type of products such as term life that these channels offer.



In most cases, the Internet is being used today for lead generation and to provide company and product information. Lead generation will continue to be more of a factor than Internet sales over the 1998-2003 period, although we see a gradual shift toward sales. Typically, quote services are run by what are essentially insurance agencies/brokerages. They use technology (e.g., quote-generating programs, linkages to carrier databases and back-office systems) to offer consumers a broader array of choices and greater assurance that they will find a good value.

Carriers have ambivalent attitudes toward the Internet. On one hand, they know that there is growing consumer activity on the Web. On the other hand, there is fear and uncertainty about where this new technology will take them. Fear of alienating current distributors is a major factor behind many companies' slow adoption of the Internet. (Insurers tend to think they are unique in this regard, but the fact is that every industry that relies on distribution staff is wrestling with this issue.) While the Internet can make agents more productive by lessening prospecting and administrative loads, it also can lead to the commoditization of products. Thus, one concern for insurers is how to add value so they are not seen as simply selling a commodity.

We forecast that individual life combined sales and leads generated via the Internet in the middle market will reach $1.5 billion by 2003, representing 3.8% of the market, compared to 0.2% in 1998. We expect quote services to grow to $0.6 billion by 2003, representing 1.5% of the market, compared to 0.3% in 1998.

Worksite Marketing

Worksite marketing is predominantly a middle-market channel; three-fourths of current sales through this channel are in this market. The issue for insurers is how to get this channel to work better than it has in the past. Distribution involves two steps and requires expertise at both the wholesale (obtaining an employer’s permission to offer voluntary insurance with a payroll deduction option) and retail levels (enrolling individual employees). As a result, worksite marketing of life insurance is different from the traditional life sale, because the agent is not used to going through an intermediary.

While its potential has not been realized, a number of carriers are rethinking their approaches and the resources they will need to succeed in worksite marketing. The field still is wide open for this distribution channel; the number of companies selling via worksite marketing is growing, and a vast majority of carriers that offer products in the workplace are small players.

We forecast that this channel will continue to grow, although at a slower rate than the Direc/Tech approaches. We expect worksite-marketed individual life sales in the middle market to reach $2.1 billion by 2003, representing 5.3% of the market, compared to 3.6% in 1998.

Banks and Financial Service Providers

Financial intermediaries are selling life insurance today. As agents have moved upscale, their clients have required such services as financial planning, investment advice and execution, retirement planning and wealth transfer. Thus, agents in the upper market and even at the upper end of the middle market face growing competition from financial advisors, stockbrokers and mutual fund firms, which already provide these services and see life insurance sales as another service to integrate in their total customer package.

A growing number of agents are becoming integrated providers by moving upscale themselves—e.g., getting licensed to sell securities—with the result that insurance-selling sometimes becomes a smaller part of their business. For example, John Hancock Mutual Life Insurance Co. announced in February that all of its 850 agents will become full-service independent financial advisors, joining the 2,150 independent contractors that are affiliated with the company already. This change will broaden the portfolio of products that the agents can sell, including those of other insurance companies.

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On the other hand, banks have less opportunity to sell insurance in the upscale market, but have greater potential to sell in the middle market. Coming off their success in selling annuities and their search to increase revenues, more and more banks are trying to sell life insurance to the middle market. This represents an opportunity for carriers and agencies that can partner with banks.

Several challenges remain, however. One is the fact that banks have a history of—and are very good at—selling credit life, which is a more profitable product for them; some view term life as a competing product. Another challenge is to reach customers better. While banks have good databases of customer information and have been using these in direct marketing of insurance, they also are trying to “kick” customers out of their branches—preferring that they use ATMs. This obviates the sale of products in their ubiquitous branch offices—one of the strong inherent advantages of the banking industry.

But expected federal regulatory changes could change this environment drastically and open up new avenues of opportunity for cooperative bank/ insurance ventures. We forecast that bank and financial service providers’ individual life sales in the middle market will reach $3.5 billion by 2003, representing 9.0% of the market, compared to 7.4% in 1998.

Will The Gap Be Closed?

While the middle-market life under/ uninsurance problem is not as widely publicized as the problems in health care availability, it is a problem that the insurance industry needs to address from both public policy and market opportunity perspectives. The array of distribution channels discussed in this article provides new—albeit not fully tested—potential to meet those needs. Over the next few years, we will learn which of

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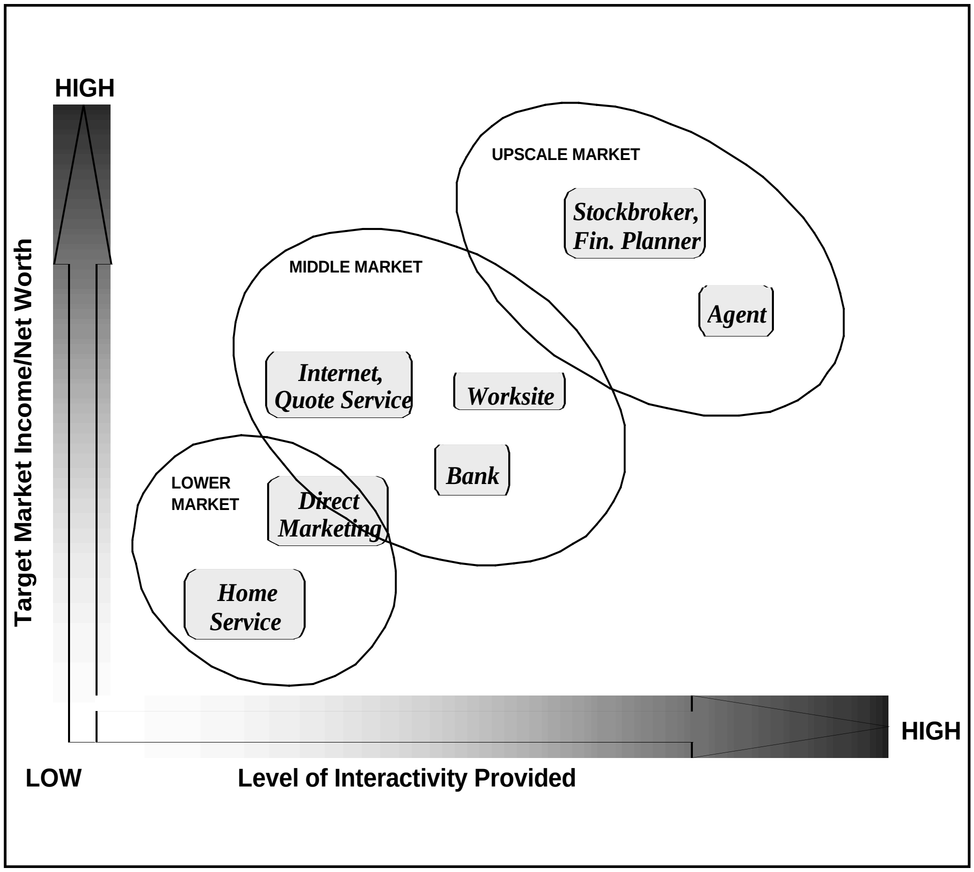
these channels are successful, and which carriers—the ones that adopt the right channels—will be the middle-market life distribution winners.

Conning's recent study, "Life Insurers' Distribution Strategies—Testing the Waters," discusses these challenges and provides more details from our survey.

More information on research by Conning & Co. can be obtained from Kevin Gough at (888) 707-1177. Mark L. Trencher is assistant vice president of Insurance Industry Research, Conning & Company in Hartford, Connecticut.

Life Distribution Channels Interactivity vs. Target Markets



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