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SOCIETY OF ACTUARIES Marketing and Distribution Section

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LETTER FROM THE EDITOR

By Juliet Sandrowicz

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By Brian Grigg

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By Maria Thomson

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GUARANTEED UNCERTAINTY: SOCIOECONOMIC

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Feature articles in this issue are:

- Brian Grigg, vice president Annuity Distribution of Old Mutual Financial Network, tells us "it's relatively easy to figure out what the middle market needs" and "distribution plays a key role in designing products that will help the middle market take a step in a positive direction" in his article on "Challenges of Product Development within Middle Markets."
- Maria Thomson, founder of RAD Insurance Holdings, summarizes two examples of pioneering firms that have tried RAD (Rapid Assessment & Delivery) and have been successful in "Reflections on SOA Annual Meeting Panel on e-Commerce–RAD Pioneers Making Mid-Market Inroads."
- LIMRA and the Marketing and Distribution Section of the Society of Actuaries recognize that both socioeconomic and other trends will shape the industry over the next five years in "Guaranteed Uncertainty–Socioeconomic Influences on Product Development and Distribution in the Life Insurance Industry," by Richard Hekeler, Ph.D., director of Custom Research LIMRA.

As part of our initiative in expanding partnerships with non-actuarial organizations, we will make available upcoming meeting and event announcements. At this time, the JCG Group Ltd. would like to announce: Mory Katz, former chairman and CEO of private-equity owned Direct Response Corporation will present the keynote address at the 2011 Insurance Direct

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Marketing Forum. The 2011 Insurance Direct Marketing Forum (www.jcg-conferences.com) will be held March 7 & 8 in Annapolis, Md.

I encourage each member to contact the council or me with your ideas, your articles, or any comments that you have to make NewsDirect more useful to you. Enjoy this issue of News Direct!

Juliet Sandrowicz is corporate vice president and actuary at New York Life, Tampa Fla. Juliet may be reached at Juliet_sandrowicz@nylaarp.newyorklife.com.

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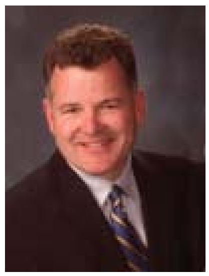

I was invited to write an article on the challenges of product development within middle markets (64 million people strong). I currently deal with annuity product marketing and distribution, so you'll have to forgive me for extending my opinions in to other product realms, but I think they apply (and I do have a number of years of work under my belt in life marketing and product development).

I find the concept of "challenges" in the middle market to be an interesting angle. It implies that there are product design or pricing challenges, that it's difficult to determine what needs are unmet, and that we need to focus on that and solve "real" problems. Quite the contrary, it's relatively easy to figure out what middle market needs.

The middle market needs life insurance protection. It knows it; it admits it. Sixty-six percent of the middle market tells us that all adults should have life insurance. Seventy-three percent tell us that life insurance is "... a necessity, not an extra." Yet, the middle market is incredibly underinsured. It's also confused.

Despite the proclamation that life insurance is necessary, protection goals are not a top priority. Where 53 percent believe that having enough money to start a family and 50 percent believe having enough money for comfortable retirement are top priorities, only 7 percent believe having adequate life insurance is a top priority. Not quite the necessity they say it is.

Could this be due to debt burden? Twenty-nine percent of the middle market says it is struggling to pay off debt. Another 5 percent is still growing dept. Forty-seven percent have some debt but are "comfortable" with it. C'mon, who's "comfortable" with debt?

The middle market needs to save more and more appropriately to their own situation (stop chasing returns and focus on what's appropriate for their individual situation). Our culture promotes getting the most, the biggest, the best, etc., only to fall short on explaining the cost of getting there. I once heard a so called "expert" in investing, an "esteemed" professor from some top eastern school tell a whole conference of retirement specialists that the solution for retirees is to take on more risk. They need more return. This was prior to the 4th quarter of 2008 and boy did he get it wrong, but it's not the timing that was so wrong. What so many experts don't even understand is that it's not about the market. It's about the individual and what is appropriate for him/her. What's appropriate?

Let's say you spent your whole life living beyond your means, saved little, and your employer bailed on a defined benefit pension plan long ago. "Ah," say the experts. "You need more money so the important thing is to take on more risk." Bunk. Sure, you need more money, but chasing good or better returns risks being even poorer than you were before. Going "all in" for equities or some other high-risk vehicle doesn't make sense for someone at or near retirement . Unfortunately, you didn't have a good professional nagging you to save more earlier, when you had enough time to withstand a prolonged depression in stocks or, for that matter, were in a good time for buying equities. Now, what is likely appropriate is to reduce lifestyle to make sure there are some resources to live a minimally acceptable financial future. Of course, you could gamble a good chunk of what you need to live in the near future and get lucky. Our culture, of course, says that if you do this and win, you're a winner. I don't agree. You just got lucky and the cost is more than most can afford.

The real challenge is getting the middle market to respond, to do more, earlier. It's key for insurance companies to understand that motivations can't be taken for granted. They must be influenced. In other words, influencing them do the things that they identify as important and necessary is the key to understanding how to grow middle market share. This is not easy.

Distribution plays a key role in designing products that will help the middle market take a step in a positive direction. Earning enough to survive and thrive is the question every fee- or commission-based person deals with constantly. Even the really big hitters are challenged with the cost of getting in front of qualified individuals. Contrary to some ideas that people line up outside the planners office for service and product (they don't), it's tough finding good clients. And, it's expensive. Good planners tell me that they are spending at least 30 percent of their revenue on marketing to find new clients. This with additional overhead of staff, compliance, tools, etc. An average producer could very well spend more than 50 percent of their revenue on expenses.

Distribution is concerned about sales flow and compensation. They know how difficult it is to establish good flow. If sales flow was high, compensation might be less. However, reality is that it's difficult to find new clients and challenging to get commitments. This puts pressure on all financial products, perhaps more so in middle markets, to pay a reasonable commission. Also, despite many front-end commission products being a low burden on product cost, many, including regulators, see commissions as negative. Ironically, fee-based products, many with higher overall costs (they're just measured in a different way), are seen as client friendly.

Of course, "optimal," perhaps a code word for "without commissions," could produce a better solution. Good producers, however, will employ themselves in another field and no one will be served. Insurance companies know that the "best" product, the one with the least compensation and the lowest expenses, will sell zero to the middle market because good sales people aren't out there influencing motivations.

Sales flow is also influenced by product that works in the sales world, i.e., motivates clients to take action. I've had many conversations about whether a premium bonus on an annuity is a good thing or a bad thing. It's neither. Of course, nothing is free; bonuses are paid for by spread, reducing the declared rate; or, in the case of fixed indexed annuities, spread that is used to buy options, reducing the cap. A bonus in an FIA is a bird in the hand, two in the bush argument. If you take the bonus, you have it, but reduce the potential return over time. If the crediting method doesn't perform well over time due to the underlying index performance, a bonus approach could very well produce a higher return.

Let me end by expressing my appreciation for agents–annuity, life, LTC, Medicare Supplement, final expense, etc. The best of you are truly magical. You know how to motivate people to take steps in the right direction, to do something about the challenges we all face. You use your behavioral knowledge of people for their own benefit.

Brian Grigg is vice president Annuity Distribution Old Mutual Financial Network, Baltimore, Md. Brian may be reached at brian.grigg@omfn.com.

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Now the industry has two examples of pioneering firms that have tried it and have been successful. Farmers New World Life was the first, with their introduction of "Rapid Issue Term" about five years ago. This product is sold by their P&C parent's sales force, and it utilizes simplified issue automated underwriting, with the policy being issued at point-of-sale. In spite of high premiums typical of simplified issue programs, sales have been strong, and they have been happy with their profitability.

Thanks to the Society of Actuaries' e-Commerce panel discussion, which I moderated at the last Annual Meeting, I now know of another pioneer that has embraced a similar model–HSBC (a bank). John Lucas, SVP of Product and Michael Palace, VP of Product were kind enough to share the details of their "unway" program with us. This program utilizes automated non-med underwriting for face amounts up to $500,000! This is the first example I have encountered of a carrier exceeding $250,000 for an automated underwriting offering. They instantly issue all their policies via e-mail–the issue process only takes about 15 minutes! Their distribution includes bank agents, brokers and self-service on the Web. Interestingly, they reported that about 25 percent of their business is from the latter category.

They feel their rates are competitive with traditional fully underwriting business–they do offer preferred rates. This program was introduced three years ago, and

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they have experienced strong growth and satisfactory lapse and mortality results. I would speculate that they are also experiencing dramatically reduced policy issue costs.

One of the virtues of automated underwriting according to the Marketing and Distribution Section sponsored SOA study, is the detailed data it provides–which is very helpful for fine-tuning rules and the sales process. As a nice companion to the HSBC presentation, David Moore of Deloitte (which performed the research) presented the results of this study–which showed that companies that utilized the software for simplified issue or non-med underwriting are very pleased with the results. Those that are using it to sell through P&C agents have been particularly pleased.

Those who are unhappiest with their results are firms that are attempting to duplicate full medical underwriting results. For these companies, setting up the rules and modifying them has proven to be very difficult, and so much of the business is ultimately referred to the underwriters, that there doesn't seem to be strong efficiency gains.

Another caution comes from those that distribute through independent agents. Such agents tend to resist learning new processing approaches, and tend not to embrace the technology.

In summary, RAD is the simple sales solution required for capitalizing on CSR and internet distribution channels, while producing mortality in line with appropriate nonmed underwriting expectations. Since most of the populace has a bank or P&C agency relationship, CSR agency channels can provide unlimited market access.

Maria Thomson, FSA, MAAA, is the founder of RAD Insurance Holdings. Maria can be contacted at maria.thomson@radinsuranceholdings.com.

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GUARANTEED UNCERTAINTY SOCIOECONOMIC INFLUENCES ON PRODUCT DEVELOPMENT AND DISTRIBUTION IN THE LIFE INSURANCE INDUSTRY

By Richard Hekeler, Ph.D.

Uncertainty–indeed, one need only look to the last three years to know this is the case. Government, business, and the populace were forced to react to an economic downturn that few anticipated would be so severe. However, what is certain is that the effects of the recession, although technically over, 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 of change while others are 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 a part of our nation's history, continues apace spreading a wave of multiculturalism from the large urban areas to the 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 as such, the financial future of many is questionable.

- 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, the industry will have to be nimble in its product development and distribution to stay current with the changing marketplace.

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 life style for which we are accustom. The challenge for the industry is the public has a hard time recognizing what they need to achieve financial security beyond a dependable source of income and, furthermore, recognizing how the industry's products and services help fulfill their needs. To illustrate the industry's challenge, consider these three facts:

- Fifty-eight million U.S. households (44 percent) believe they do not have enough life insurance.[1]
- Twenty-nine million Americans controlling $881 billion of investable assets reach retirement age over the next five years; yet the public has only a limited understanding in how immediate annuities can play a role in retirement income planning.[2]
- More than 60 percent of personal bankruptcies in the United States in 2007 were caused by health care costs associated with a major illness.[3]

LIMRA and the Marketing and Distribution Section of the Society of Actuaries recognize these facts and others will shape the industry over the next five years (and beyond) and will also inspire creativity in product development and distribution. The two organizations also recognize the importance of conducting a joint study exploring how socioeconomic trends will influence the need and demand for the industry's products and services over the next five years. The research is now available and addresses these objectives:

- What are the key socioeconomic trends influencing the need and demand for the industry's retail products and services?
- How will these trends influence product development and distribution given the potential changes to the economy, population, and societal

expectations anticipated over the next five years?

The report will be posted to the Society's website in January 2011. If you would like more information on the research please contact Lucian Lombardi (llombardi@limra.com) or Ronora Stryker (rstryker@soa.org).

Richard W. Hekeler, Ph.D., assistant vice president, director of Custom Research, LIMRA, Windsor, CT is lead researcher on this project.

For more information on this research you may contact Lucian Lombardi, vice president LIMRA Research, Windsor CT, at llombardi@limra.com.

[1] Trends in Life Insurance Ownership, LIMRA, 2010.

[2] Money in Motion, LIMRA, 2010.

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