NewsDirect

May 2017
Issue 74

Defining Direct—What Does D2C Mean for Financial Services?

By Patrick T. Leary and Eric T. Sondergeld

Increasingly, organizations across all industries are leveraging direct-to-consumer (D2C) strategies. This article provides a backdrop for companies seeking to develop a new or expand an existing D2C distribution program.

WHY NOW?

While the financial services industry has always had a "stake in the ground" with D2C distribution, interest in developing expanded D2C capabilities has increased considerably. Several trends contribute to this renewed attention:

- Other industries have raised the bar and created appealing D2C experiences—particularly online. Consumers will increasingly expect (and even demand) the same digital capabilities from financial services organizations.
- Financial services organizations are seeking new outlets for profitable growth.
- Some market segments (e.g., the middle market) have expressed a need and desire for the industry's products and services, but existing distribution methods have not successfully met that need in a cost-effective way.

WHAT IS DIRECT (TO CONSUMER)?

Before exploring D2C in detail, it is important to understand go-to-market strategies that manufacturers—regardless of product or industry—have at their disposal to reach target markets. As financial services organizations take a more consumer-centric perspective of marketing and distribution, the industry must view distribution strategies in a way that is consistent with the distribution framework other consumer-focused industries use to connect with markets.

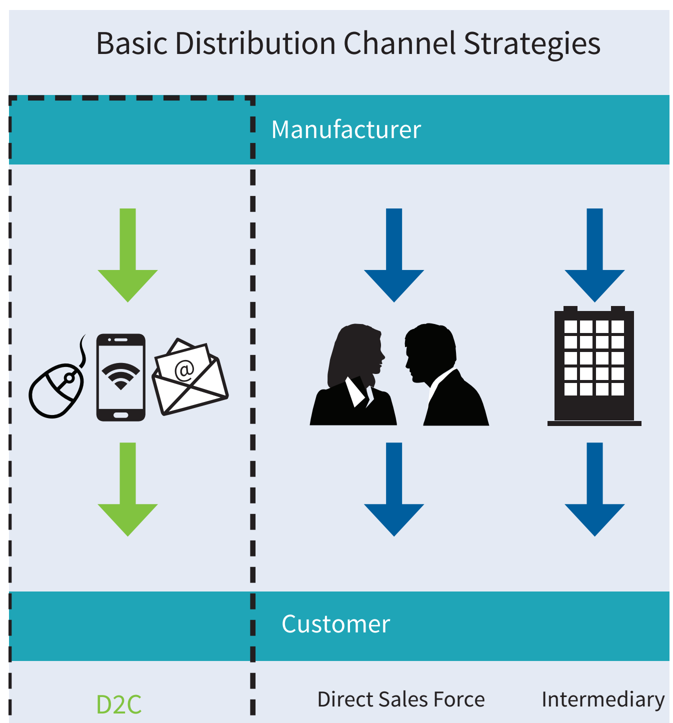
At a fundamental level, distribution is the process of connecting a manufacturer with the market of potential customers. There are essentially two basic strategies (Figure 1). A manufacturer can connect with customers:

- **Directly** through its own distribution channels, including its own stores, outlets, salespeople, and D2C approaches (e.g., online and mail), or
- **Indirectly** through intermediaries, third parties, and other partners that provide access to markets the manufacturer seeks to reach.

Direct distribution channels are those where manufacturers interact directly with the consumers who might purchase their product; they have direct access to them and control of the channel. Thus, direct channels include not only what is traditionally considered direct response, but also direct sales forces. If the manufacturer doesn't direct or control the channel and sells through someone else, then it distributes indirectly using intermediaries (third parties).[1]

As an example, Apple Inc. can distribute its products directly through its offline and online channels (e.g., Apple stores and its website). It also can distribute them indirectly through retail outlets (e.g., Target and Best Buy) and wireless service providers.

Feature 1



Source: LIMRA (2016)

In our industry, investment firms such as Fidelity Investments and Vanguard distribute directly when selling their own mutual funds—yet they also serve as intermediaries for countless other manufacturers. A life insurance manufacturer could sell its products directly through its own sales force or website or indirectly through banks or brokerage general agencies.

> D2C can be defined as any non-face-to-face distribution program directed by the manufacturer such that no third party has a financial incentive for the program's success.

THREE PRINCIPLES

As marketing and distribution strategy has evolved, so have the fundamentals that define D2C channel distribution. Three key principles provide clarity and a contemporary perspective:

1. D2C is more than direct "response."

What was once called direct response typically had some type of stimulus that consumers **responded** to. For example, these included a television or other advertisement with a toll-free number to call, "bangtail" billing envelopes (with a perforated coupon attached to return), or another mailing with a call to action. But with the advent of the internet as a potential sales channel, self-motivated consumers may be responding to their own initiative when seeking information and potential outlets for purchasing financial services products online.

As such, the term "direct response" represents an incomplete picture of the channel. The term "direct to consumer" provides a more contemporary reflection of how organizations engage with consumers on a direct basis with non-face-to-face methods.

2. D2C is non-face-to-face—but not all non-face-to-face is D2C.

If a manufacturer's offer is made through a distribution partner's website, is that D2C or distribution through an intermediary? Does it matter that the manufacturer is making an offer via a third party? The customer experience is similar.

For example, many would consider Amazon.com to be a D2C channel. From a manufacturer's perspective, however, it is selling through an intermediary (i.e., indirectly). In this case, it is through an online retailer versus its own D2C website, where it has direct access to the customer. Here, the distribution channel is indirect: an online retailer. The method is non-face-to-face: online. The fact that it is online does not alone define it as D2C.

3. Marketing and fulfillment do not necessarily determine whether something is D2C.

A third consideration is understanding the distinction between direct marketing and the fulfillment of the product purchase. Working with their chosen distribution channels, manufacturers can encourage the purchase of their products in two ways (Figure 2):

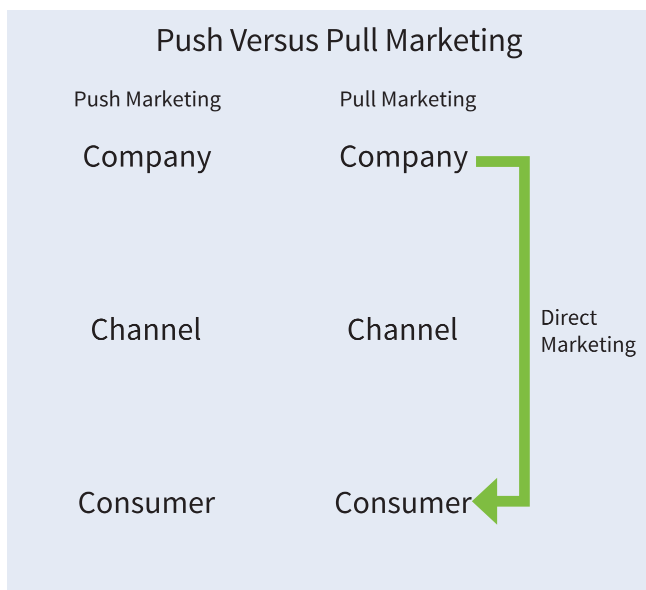
- Using **push marketing,** they push messages through intermediary channels, encouraging them to sell more of their product.
- Using **pull marketing,** they market directly to consumers by encouraging them to seek out the company's product, thereby pulling the customer up through a channel to purchase. The channel could be an intermediary, a direct sales force, or D2C. So, while all pull marketing is direct marketing, it does not follow that all direct marketing is D2C.

DISTRIBUTION CHANNEL VERSUS DISTRIBUTION METHOD

A distribution channel describes the entire network or path from manufacturer to consumer. The concept of channel is primarily of interest to the manufacturer. A distribution method refers to how the manufacturer, distributor or financial professional engages clients and potential clients. Regardless of channel, multiple distribution methods may be used, such as face-to-face, mail, phone and online.

Historically, direct response methods were limited to mail and phone via contact centers; the customer was purchasing directly from the company without using a local advisor or agent. D2C now includes digital methods such as online, email, social media and online advertising. At the same time, some financial professionals and distribution organizations employ non-face-to-face methods to facilitate sales, rather than simply to generate leads.

Feature 2



Source: Innovating in a "Sold Not Bought" Category, Maria Ferrante-Schepis and G. Michael Maddock (2013)

> A D2C strategy can also be integral to an omnichannel strategy for companies that want to offer a variety of access points and seemlessly integrate them.

An important distinction is that financial services product purchases are typically fulfilled by the manufacturer. Unlike most consumer goods, financial services products cannot be purchased by distributors, marked up and then resold. With insurance products, the insurer needs to be involved for order fulfillment, since it must underwrite the risk, issue the policy, and set up an administrative record for the policy. Because of this, it sometimes can be confusing to determine whether something is D2C. This is why the definition of D2C is not tied to the fulfillment process.

Connecting with consumers as part of a D2C strategy requires a direct marketing campaign to advertise and promote the manufacturer's offer through mail, billboards, television, magazines, websites or other media outlets. Often the promotion is calling for an action on behalf of the interested consumers—such as making a phone call, clicking through to the manufacturer's website, or returning a postcard. There is an advertising cost to the manufacturer, but the media outlet has no vested interest in how successful the campaign is; they receive the advertising revenue regardless.

When distributing a product through an intermediary's non-face-to-face methods (such as their online website or membership publication), a similar call to action is often employed. What distinguishes it from a D2C channel is that the intermediary receives more than just advertising revenue. It may receive a contractual sponsorship or branding payment and/or compensation for the success of the program. It gets a "piece of the action" for any leads and/or sales the campaign generates. Unlike with paid advertising, here the intermediary has a vested interest in the result of the campaign.

CHALLENGES AND CONSIDERATIONS

Building a D2C program from the ground up requires marketing muscles that may have atrophied or never existed. To do so, companies will need to develop go-to-market strategies that:

- Identify a market need;
- Define the specific markets that have the need;
- Find the most effective way to reach and engage those markets; and
- Determine what their competitive advantage will be, including the actual product or service offering.

The order of these steps could vary by company, but it is critical that—before deciding on D2C as a path to market—it is the most (or one of the most) effective means of reaching the desired market. If there is a better way to reach a particular market, then companies should seek that out instead. Once it is decided that D2C is the way to go, companies need to develop a true marketing mindset to understand the needs and attitudes of their target markets and how they want to engage.

A D2C strategy can also be integral to an omnichannel strategy for companies that want to offer a variety of access points and seamlessly integrate them. At the same time, they need to be careful not to inadvertently create conflict between a D2C program and their direct sales force. Conceivably, they could even create friction with other distribution partners, though this is less likely. Another potential risk is spreading marketing mindshare too thin across a growing number of distribution channels/methods.

Finally, one of the biggest challenges many companies face in building a D2C strategy is determining the actual product or service offering. In many cases, existing products just may not work. They may be too complex, not adequately priced for D2C, or otherwise a poor fit for the chosen D2C market(s).

Companies must remember that—unlike most products sold face-to-face—the D2C offering includes not only the product, but also the price, process and experience. And this is where we come full circle to the importance of revisiting and reinventing the customer journey in financial services. ■

Patrick T. Leary, M.B.A., LLIF, is corporate vice president, Distribution Research, for LIMRA. Leary can be reached at 860-285-7840 or *pleary@limra.com.*

Eric T. Sondergeld, ASA, CFA, is corporate vice president and director at LIMRA, leading the Technology Research and Developmental and Strategic Research teams. He can be reached at 860-298-3957 or *esondergeld@limra.com.*

ENDNOTE

1 *Retail Distribution Perspectives,* LIMRA, 2014.