# Bancassurance and life assurance

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## 1. Introduction

One of the most remarkable developments on the "Spanish insurance" scene in recent years, especially as regards life assurance, is the emergence and development of bancassurance.

The term refers to the sale of insurance products through the branch networks of financial institutions and its impact has been notable in both quantitive and qualitative terms.

From the quantitive aspect it has helped decisively to increase the specific importance of insurance in the economy.

As regards quality, bancassurance has accelerated the transformation of life assurance by introducing in its savings schemes mechanisms that are capable of competing with other financial products in yield, transparency and adaptation to the needs and preferences of clients.

Below we look at the reasons that led to the appearance of bancassurance in Spain, at the motives that drove its development, as well as its current importance. We will also consider the evolution of bancassurance types and the challenges and matters still to be resolved that are facing this distribution channel. All this with regard to life assurance.

**Comparative Image Survey of Banks, Savings Banks and Insurance Companies (end 80s)**

| | Savings Banks | Banks | Insurance companies |
|---|---|---|---|
| Safer | 54% | 27% | 8% |
| Invest your money better | 44% | 28% | 4% |
| Quicker | 45% | 31% | 7% |
| More informative | 37% | 25% | 10% |
| Treat clients better | 40% | 23% | 9% |

*Source: Survey by Insurance Research Organization (ICEA))*

## 2. Emergence and Development of Bancassurance

### 2.1. Initial Situation

Until the second half of the 1980s, we were independently located between the distribution networks of the banks and the marketing channels of the insurance companies; the fact that most of the large insurance companies belonged to banking groups or savings banks did not lead to the systematic joint creation of marketing channels.

Nevertheless, this basic separation did not hinder the maintenance of certain relationships between the marketing activities of insurance companies and banks, such as:

**1.** The existence of certain insurance products linked to typical financial operations (life assurance to pay off personal and mortgage loans, compulsory fire insurance required to obtain such loans), whose marketing normally did not require the involvement of an insurance specialist.

**2.** The participation, in various ways, of certain persons responsible for bank branches in the marketing activity of some insurance companies, which took advantage of the resulting client relationship.

The image of banks and savings banks amongst savers at the end of the 80s was clearly superior to that of insurance companies. This meant that their clients had greater confidence in these institutions, which began to be attractive to insurers who needed an effective marketing vehicle. The above table illustrates this point.

## 2.2 Reasons the Strengthening of Relations between Banks and Insurers

As a result of the aforementioned situation, in the late 80s and also in the 90s there was an increasing move by the insurance companies to use bank marketing channels. This development, which was encouraged by all parties, not only involved institutions within the same group but also organizations independent of each other.

We can list the following as the main reasons for this trend from the viewpoint of the financial institutions:

**1.** Availability of extensive bank and savings bank networks with an ample supply of human and material resources. The existence of this infrastructure as a result of the particular development of the financial sector, forced Spain to adopt measures to make it profitable. Amongst these the inclusion of new financial products and quasi-financial products such as investment funds, property operations, and importantly, insurance, stand out. By this means cost distribution was spread over a wider business base.

**2.** The reduction in intermediary margins due to the rise in deposit costs as a result of greater competition or across-the-board rate cuts. The need to offset the reduction of operating profit by increasing commission income generated by different kinds of services was considered.

**3.** In a fairly mature financial product market with a high level of competition, the banks and savings banks did not neglect the need to strengthen client relationships and offered the most extensive product range possible.

**4.** Finally, in spite of the large number of bank and savings bank branches, there were certain areas, particularly outside the traditionally established field of each financial institution, where they did not reach; by strengthening ties to the insurance sector they would also later be able to avail themselves of the network of insurance company agents as a marketing channel for banking products.

The following are the insurance sector's reasons for using bancassurance:

**1.** The need for marketing outlets to give their business a greater rate of growth so as to meet the heavy potential insurance demand arising from the economic expansion as a result of Spain's entry into the EEC.

**2.** The advisability of applying advanced technology to insurance distribution to reduce costs and improve service. Spanish insurance companies have frequently not had the necessary technical means to tackle growing market competition because of inadequate technology.

The bancassurance model, which looks towards banking when setting efficiency ratio targets, has been salutary for the insurance sector by driving the companies towards greater modernization and renewal of their operating models. Even so, there still remains a balance in favour of banking in respect of resources dedicated to technological development.

## 2.3 The tax factor

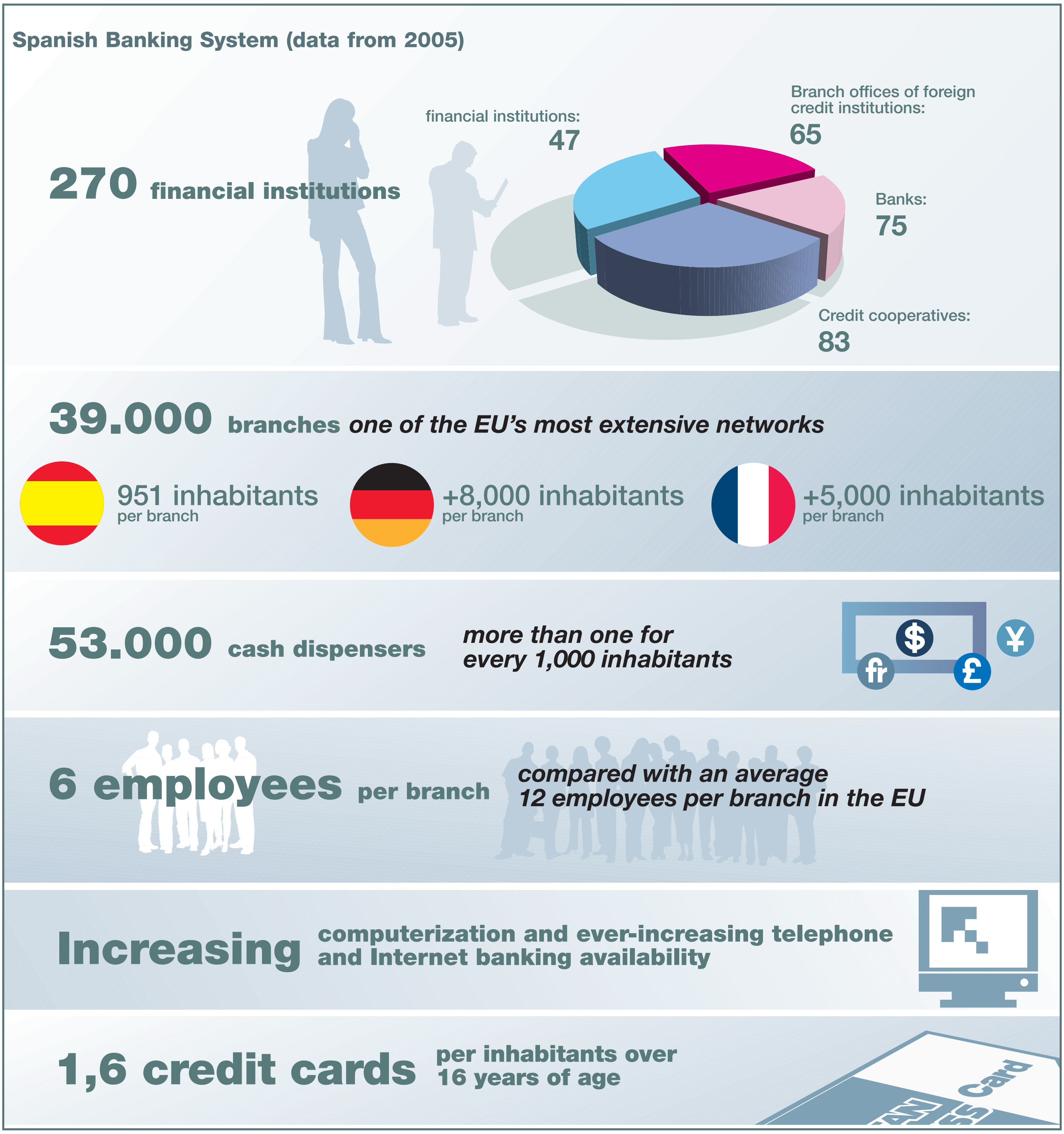
The interest of banks and savings banks to include insurance products amongst their portfolio was influenced to an important degree by their desire to pass on to their clients the advantages that the income tax regulations have traditionally conferred on long-term savings in general, and on life assurance endowment schemes in particular.

From the mid-1980s financial institutions concentrated on designing products that favoured the concept of financial/tax returns, as these had been a factor in driving the growth of life assurance endowment schemes in Spain in recent years. The process was not without its problems, because as a sub-product of this activity operations emerged known as “single premiums”, which, because of problems regarding client transparency and differing interpretations by the financial marketing entities and the tax authorities, produced a serious and lasting dispute, which had a negative effect on the sector's reputation.

The tax incentive has continued to be the driving force behind life assurance, in spite of the appearance in 1987 of pension plans and funds, which are specifically regulated final savings instruments with more important tax advantages from the outset than any other financial or insurance product.

## 2.4. Pre-eminence of the Spanish Banking System

In short, the Spanish banking system presented itself as an opportunity to speed up the development of the insurance industry, especially in life business. This continues to be the case and its strength is reflected in the following data from 2005:




*Source: Banco de España*

## 2.5 Current Importance of Bancassurance

Finally, the level of consolidation achieved by bancassurance in the Spanish life assurance sector is reflected in the information in the table of this page.

## 3. Types of Bancassurance

The reasons given for the strengthening relationship between banks and insurance companies help to explain the appearance and development of Bancassurance as a concept. The truth is, however, that initially this distribution channel was mainly brought about by the specific creation of wholly-owned insurance companies by banks and savings banks, which was clearly instrumental. This fact was evidenced by:

- Full integration of the insurance company into the bank or savings bank structure, i.e. into the respective group's functional organigram.
- Intensive use of insurance products by the systems and branch networks open for normal business.
- Use of services provided by corporate units of the bank or savings bank group.
- Maximum reduction of technical and human resources in the company itself.

Later this original type of bancassurance developed at the same time as the volume of insurance business grew along with the results and value added by this model and the complexity of its management. Today there are beginning to be a significant number of financial groups that are opting to become involved in the project with highly respectable independent groups, who are well equipped with management skills and brand images.

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In this connection it is worth mentioning as typical market examples Caixa-Fortis, MAPFRE-Caja Madrid, Aviva in conjunction with several savings banks and also Zürich-Deustche Bank.

### Percentage Distribution of Life Assurance by Channel. 2004

| | Premiums | | Number of Policies | |
|---|---|---|---|---|
| | Portfolio | New Business | Portfolio | New Business |
| Agents | 14.6 % | 15 % | 23.6 % | 19.8 % |
| Brokers | 7.7 % | 4,3 % | 5 % | 4 % |
| Banks & Savings Banks | 60 % | 71.1 % | 61.3 % | 71 % |
| Direct Offices | 15 % | 8.3 % | 6.4 % | 2.9 % |
| Others | 2.7 % | 1.3 % | 3.7 % | 2.3 % |
| | 100 % | 100 % | 100 % | 100 % |

Each of these cases represents its own type of joint venture, but they all share the following common characteristics:

- Business management is wholly undertaken by the insurance group, which for this purpose sometimes uses its own existing resources, and in others, employs resources obtained from previous bancassurance activities; the aim is to seek to take maximum advantage of the economies of scale brought about by integrating management within its traditional business, i.e. as seen from a multifaceted perspective.
- For its part, the bank or savings bank acts as intermediary which may be evidenced by signing an agency contract with the insurance company, in which, where applicable, the marketing commissions to be paid on each product marketed through the network are stipulated. Such products are fully integrated into the bank's or savings bank's portfolio, so that the marketing image adopted is that established for their entire portfolio. On the other hand, client relationships are always channelled for all marketing purposes through the banking network, except for administrative communications, which the insurance contract specifies should be undertaken by the insurance group.
- Product marketing integration is also accompanied by maximum integration of computerized tools in the bank or savings bank branches or other outlets, in order to achieve the optimum level of operational automation, so that this comes as close as possible to the system used for contracting the respective entity's other non-insurance products.
- The foregoing is compatible with maintaining a company that is jointly owned by banking and insurance groups; such

a company legally assumes the insured risks and reflects the maximum involvement of both parties in the development and overall outcome of the business. Furthermore, the jointly-owned company usually serves as a vehicle for considering future insurance and banking plans and taking decisions on various matters including:

– General business strategy,

– the product portfolio to be marketed,

– design and marketing characteristics,

– development priorities,

– targets to be achieved by each one in any given financial year,

– the planning of publicity campaigns and marketing backing,

– systems, contents and publishing frequency of management information, and

– training plans.

## 4. Current Bancassurance Challenges

The contribution made by Bancassurance to the growth of the sector in recent years has been important. The rate of development achieved cannot however easily be extrapolated for the short-term future.

- Firstly, for the simple reason that this channel is nearing its maturity; the involvement of financial institutions in marketing life assurance came about at an opportune moment, but also at a time when there was the capacity to absorb rapid growth in business. It can be said that, contrary to initial fears, "banking networks were market makers", and brought life assurance to places not reached by the traditional networks without reducing, in absolute terms, the size of the business they controlled.

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In turn, the distribution of premium volumes between the different channels will also tend to stabilize, with special reference to agency networks, which are adopting a more general profile. Indeed, in the wake of bancassurance we are currently witnessing an expansion in the sale of strictly financial products relating to loans and deposits through insurance agents.

Nor should the distance marketing channels be overlooked, particularly the internet, which although growing at a slower rate than anticipated, is being converted by society into a leading strategic marketing medium; this will also be the case for life assurance companies.

- And secondly, because the first signs of bancassurance exhaustion may soon be seen, based exclusively on exploiting the tax advantages in life assurance endowment schemes and in cross-selling with other bank and savings bank financial products in other types of life assurance.

Indeed, the view that the different savings products should receive the same tax treatment is beginning to gather strength in the industry and amongst legislators, a principle that implies the same taxation for products that are similar in character and purpose. There is, however, no reason to deny governments the faculty to discriminate positively in favour of those instruments that are especially well suited to achieving political, economic and social objectives. Here we make mention of the need to provide incentives for final savings, especially those directed towards retirement, when they are channelled through products that facilitate long-term realization, in a systematic manner and with maximum guarantees. In this field, life assurance, where legal solvency requirements are much more pronounced in favour of savers than those set for other savings instruments, has a fundamental role to play.

The fact that different savings vehicles may easily be substituted one for another is more pronounced in the absence of tax advantages and this may, in the context of bancassurance, be to the detriment of life assurance if the companies fail to undertake consistent training initiatives that allow the distinguishing features of life assurance to be exploited, at the same time as service to clients is improved. The most important of these features are:

- Cover for biometric risks, which allow for probable survival and the possibility of combining savings and risk protection guarantees, by using a mechanism better adapted to the needs of clients and their families in the different situations that may have a contingent bearing on their lives.

- In line with the foregoing, greater capacity to integrate with and complement the public schemes for covering risks and pensions.

- Guarantee of returns at medium, long and very long term, backed by a proven ability to manage investments, to control and neutralize financial risk in those areas, in which final savings schemes are usually developed.

- Finally, the use of protection and savings insurance should be furthered through training, without overlooking the essential mechanism of incentive, as a method of attracting new clients for financial institutions. In summary, the aim is to develop Bancassurance as an instrument for establishing new business relationships arising from insurance products, and not merely as a way of increasing the relationship ratios of existing clients.

Insurance-linked lending has in recent years been an indisputable source of growth for risk insurance. The future of bancassurance, however, cannot be sustained by this alone, but rather it must develop further its ability to sell policies independently of other business. Only in this way can we speak of bancassurance as a true distribution channel. ■