

Bancassurance: The Revolution That Hasn't Come

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A year after the enactment of Gramm/Leach/Bliley, bancassurance in the United States has made very little progress. With the conspicuous exception of Citigroup, whose formation of course predated the Act, no significant mergers have yet taken place between banks and insurance companies. Moreover, even though hundreds of financial holding companies have been approved by the Federal Reserve, no US insurance companies other than Citigroup have obtained such status.

An Unpromising Outlook

To this point at least, the US banking industry's response to bancassurance was probably best stated by Dick Kovacevich, chairman of Wells Fargo: "We don't have to own the factory to sell the product." Even in terms of marketing, the bank channel appears to be best suited to selling simple, commodity-like insurance products to customers with correspondingly simple needs, such as the savings bank life insurance long offered in New York and other states. It is far less effective for products and customers that require the specialized expertise of a trained and experienced agent.

Unfortunately, those simple, easily-commoditized products also tend to be the ones with the lowest profit margins and the most vulnerable to online competition, so the marketing window for bancassurance products would seem to be customers with simple needs who have not yet figured out how to find what they want online. Not the most promising of outlooks.

European Experience

Bancassurance, of course, is a French word. In France, where bancassurance has long been popular, this situation is primarily tax-driven: some tax-advantaged insurance products are *only* available through banks.

In the United Kingdom, there is no such tax advantage, but bancassurance there has a longer history than in the US, dating back at least to the implementation of the European Union's Second Banking Directive in 1986. Two cases there are worth looking at: Direct Line and Lloyds TSB.

Direct Line, owned by The Royal Bank of Scotland, has been a great success selling personal auto – sort of a British version of GEICO - and now, homeowners and life policies over the phone and, more recently, online. However, there is very little overlap between Direct Line customers and those of the bank, for which Direct Line has been little more than a highly successful venture capital investment. As bancassurance, it proves nothing.

Lloyds TSB, too, (no relation to Lloyd's of London), provides no strong evidence of the advantages of bancassurance. TSB, the old Trustee Savings Bank, before merging with Lloyds Bank in 1996, was primarily a thrift institution that served a relatively downmarket, blue-collar clientele. It, too, was successful in selling simple personal lines, in relatively small amounts, to customers with simple needs who were generally overlooked by the larger clearing banks and mainstream insurance companies, which tended to go after the more affluent middle class.

On the other hand, Lloyds Bank had a relatively upscale customer base. During the 1980s Lloyds bought a controlling interest in Abbey Life, a specialist in annuity policies that was at one time owned by ITT. Along with most of the UK life insurance industry, Lloyds Abbey Life and its sister company, Black Horse Life (which marketed annuities through the Lloyds Bank branch network) were caught up in a large, ongoing controversy over government accusations of policy mis-selling that has so far cost the bank more than GBP 800 million in loss provisions. Lloyds TSB has since acted to wind down these operations and recently acquired Scottish Widows, a large, well-known life insurance company with a very strong brand, for which it has had to pay a correspondingly high price.

Property/Casualty Underwriting

US bankers have three good reasons for not being very interested in underwriting property and casualty insurance. The risk-adjusted return on capital, or RAROC, is not especially attractive when averaged over the cycle, the property/casualty cycle itself tends to be highly volatile, and the risks involved are not those which bankers are experienced at managing.

While banks and insurance companies have some areas of expertise in common, such as investment management and capital markets, the core competence of banking is credit, not insurance underwriting. While it is certainly true that the convergence of derivatives with insurance products is continuing to grow, and that some of the larger banking companies are quite expert in derivatives, there are still substantial differences between the risks covered by derivative instruments available in the market and those faced by specific insureds. Covering those risks through underwriting is the core competence of insurance companies, and again with the principal exception of Citigroup, few if any US banking companies would claim expertise in this area.

Corporate Customers Like Independent Insurance Companies

From the US corporate customer's point of view, bancassurance is perceived as adding little value. A recent survey of senior-level financial executives at 444 US companies, conducted by the Association for Financial Professionals, revealed that 70% of respondents reported a preference for an insurance company that has *not* combined with a bank or securities firm, while only 14% said that they would use a bank that has merged with an insurance company for the purchase of insurance products. In contrast,

more than 50% of the survey's respondents said they would opt for a bank that has joined with a securities firm for capital markets, mergers and acquisitions, investment management, and derivatives/hedging services. The survey's responses were equally divided among small, mid-sized and large companies.

So far at least, the future of the independent US insurance company seems well assured.