Bancassurance – Business and Operational Models

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Bancassurance

- Mechanisms for provision of insurance services through banks
- Usually assumes that insurance company and bank are separate legal entities (even if part of same owner group)
- For the purpose of this presentation I am excluding captive business from the scope of bancassurance
  - Captive business means business passed on by an entity to a related insurance company, but without any detailed involvement by the bank
- Implemented using various models/structures, which vary with respect to
  - Product structure
  - Financial arrangements between bank and insurance company
  - Administrative responsibility
Potential Benefits

- **Bank**
  - Fee Income
  - Strengthen long term client relationship
  - Competitive pressures

- **Insurance Company**
  - Leverage on bank customer relationship
  - Higher “hit rate” and therefore lower acquisition cost
  - Low cost collection mechanism

- **Customer**
  - Better Value Products
  - “One Stop Shop”
Business Models / Product Structures
Business Arrangements

- Business arrangements revolve around:
  - The nature of the products and especially the extent of relative involvement of the insurer and the bank in the business.
  - The nature of the relationship and relative long term rights
    - Especially relevant in the case of long term business (life insurance)
  - Key success factors
Business Models

Level of Involvement of Bank

Level of Involvement of Insurance Company

Referral by Bank to Insurance Company
Referrals

• Very low level of involvement by Bank
  – Bank basically provides insurer access to its customers
  – Suitable for products which are complex and need to be sold by full time insurance sales personnel

• Mechanisms
  – Mail shots designed by insurer sent out to bank customers and responses forwarded to insurance company
  – Insurance sales personnel given space at bank branches
  – Bank personnel receive initial queries and pass on to insurance company for follow up

• Bank usually compensated in the form of low level of commission

• Variable costs usually borne by Insurance company
Business Models

Level of Involvement of Bank

Level of Involvement of Insurance Company

Distribution of Insurance Products by Bank

Referral by Bank to Insurance Company
Distribution Arrangements

- Bank responsible for sales of third party insurance products in return for commission
- Products tend to be either
  - simple products sold by bank personnel selling other consumer finance products; or
  - more complex products sold by dedicated insurance sales persons hired by bank
Business Models

- **Integrated Product**
- **Distribution of Insurance Products by Bank**
- **Referral by Bank to Insurance Company**

Level of Involvement of Bank

Level of Involvement of Insurance Company
Integrated Product

- From a customer perspective an integrated product, although in practice (due to regulatory constraints) could essentially be either
  - two products packaged together; or
  - a single product with a certain aspect being outsourced to the other party
- Common in the Middle East for life insurance savings products where the savings element is managed by the bank and the insurance element by the insurance company
- Products tend to be invest linked unbundled products
- Bank fee income partially from commission and partially from asset management charges
Business Models

- Bank Product with element of Insurance
- Integrated Product
- Distribution of Insurance Products by Bank
- Referral by Bank to Insurance Company
Bank Products with Element of Insurance

• Very common with consumer credit products where life (and sometimes other) cover provided for the balance outstanding
• Sometimes independent insurance coverage provided (unrelated to any debt) to provide an additional benefit to customer on occurrence of a contingency
  – Accidental coverage quite common
• Role of insurance company usually limited to provision of cover on payment of premium
• Cost of cover sometimes borne by bank (out of interest rate margins) and sometimes charged across to customers
  – If the latter usually common for regulators to require customer consent prior to this being done
Business Models

Level of Involvement of Bank

Bank Product with element of Insurance

Integrated Product

Distribution of Insurance Products by Bank

Referral by Bank to Insurance Company

Limited By

Regulation
Technological Infrastructure

Level of Involvement of Insurance Company
# Bancassurance in Pakistan (Life Insurance Only)

<table>
<thead>
<tr>
<th>Company</th>
<th>Group Credit Life</th>
<th>Individual Life</th>
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<tbody>
<tr>
<td>State Life</td>
<td>Yes</td>
<td>No</td>
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<tr>
<td>EFU Life</td>
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<td>New Jubilee Life</td>
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<td>Yes</td>
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<tr>
<td>ALICO</td>
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Relative Rights

• Any arrangement needs to protect the two parties over the long term.

• Main risk for bank – long term legal contract usually with insurer. Hence danger that insurer will eventually cannibalize bancassurance business by selling other policies to bank customers
  – Protected by containing customer ownership clauses in agreement (with suitable caveats)

• Main risk for insurer – when volumes are sufficiently large bank can enter into another relationship or even float its own insurance company
  – Protected by clauses which require existing insurance policies to continue to their full term (especially for life insurance) and by preventing bank from such ventures for a defined period.

• Mechanism usually legal agreement between the insurance company and the bank
Key Success Factors

• Commitment by top bank management
  – Cannot be driven by insurance company without this

• Well coordinated operations between bank and insurance company and between various functions in each entity

• Product design responsive to customer needs
  – Good value always helps

• Assigning proper incentives to key personnel in the bancassurance cycle
Operational Models
Operating Models

• Operational Models are closely related with the underlying business models

• For referrals on the one extreme and bank products with an insurance element on the other there is limited coordination required

• For all other models close coordination and a clear understanding of the responsibilities of each entity (and teams within each entity) is vital for success

• Various operating models are followed, varying with the extent of integration between the processes of the two entities
Business Cycles (Life Insurance)

- Sales and Policy Issue
- Renewals (premium collection)
- Alterations
- Surrenders
- Claims
- Investment Returns
Two possible approaches
- Sales cycle on a stand alone basis with underwriting and policy issuance as a follow up back office activity
- Sales cycle followed up with immediate underwriting and Policy Issue. Cases requiring underwriting referred to insurer – although even here immediate underwriting possible if supported by systems.

Latter approach yields much higher success rates
- Also much cheaper and hence allows offering better value

Approach also drives product design
- Automated underwriting means smaller Sums Assured and therefore a higher
Sales and Policy Issue
Non-Integrated
Sales and Policy Issue Integrated

Bank Customers

Bank Staff

Completes

Generates Illustration
Prints Proposal

Front End System

Further U/W Required

Basic Underwriting

Yes

Back End System at Insurer

No

Bank Coordinator

Application Evaluation Process

Policy Issued

* UW Required

Requirements Procedure

After Underwriting Decision Entered

Bank Staff

Signs

Handed to

Bank Customers
Premium Collection

• Insurance premiums are most conveniently paid monthly
  – Coincides with monthly earnings cycle for most customers

• Not possible in Pakistan and other regional countries without automated central clearing systems and therefore no ability to collect through direct debits

• Bancassurance enables banks to collect premiums using automated processes by simply accessing client accounts with bank
  – Needs a mandate from the customer as part of application process
  – Probably the most attractive feature of bancassurance for life insurers where collection of renewal premiums is a major issue
Automated Premium Collection

Bank Database

Passes Data to Banking System for Debiting Accounts

Receives Results and Passes on to Ins Co

Extracts Due Premiums from Administration Database

Updates Insurance Administration Database

Ins Co Database

Automated Premium Collection
Claims

- Claims rarely tend to be automated – unless volumes large
- Death and disability claims usually require verification by a specialist capable of forming a view based on medical reports
- Hence cycle usually manual with Bank playing a coordinating role
Claims

- Claim occurs: Death, Disability, Medical Expense

- Client/Nominee

- Intimates

- Insured Company

- Bank Branch

- Claim requirements fulfilled

- Claim paid

- Claim Form

- Sent directly to the Client

- Sent to the Client
Other Issues

• Whereas there are pluses there are also some areas of potential concern
  – Mis-selling – insurance products often deliver less value than traditional bank savings products. Hence bank has to ensure that sales process robust.
  – Lack of specific regulation in Pakistan (apart from recent State Bank circular)
Conclusion

• Area of enormous potential
  – Needs to be focussed on by both banks and insurers.

• Possibly the key to increasing insurance penetration in Pakistan.