Bancassurance

A Valuable Tool for Developing Insurance in Emerging Markets

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Abstract

Bancassurance is the process of using a bank's customer relationships to sell life and non-life insurance products. In some developed countries it has had a dramatic impact on developing sales volumes, attaining market shares in excess of 50 percent in life and more than 10 percent in non-life. By contrast, in other developed countries it has had much lower impact.

Its strategic benefits to developing countries are wide ranging. This paper discusses the potential of Bancassurance to contribute to the growth and the stability that both life and non-life insurance products can bring to developing countries. The details of

how some approaches work better than others, and how regulation and consumer protection issues can impact such development, are reviewed here, together with a discussion of regulatory policy issues and recommendations for best practice.

The paper provides a detailed study of the operation of Bancassurance in a major developed market (France). This is contrasted with a further study in a developing market (Mexico).

A short summary draws together the key implications for developing countries.

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Key words ; Bancassurance, distribution channel, emerging markets, insurance,
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Introduction

It is hard to underestimate the importance for developing countries of making insurance products accessible to the community. Undoubtedly important value is found in the ability to use insurance to mitigate the effects of the unexpected disaster, whether a fire in a property or injury in a motor accident, or even—to the extent that affordable insurance can be structured—against natural catastrophes.

It is therefore a core issue for the best path forward of many developing countries that the correct emphasis should be placed upon insurance. In particular, it is essential that the best environment—regulatory, legal, social, and political—should be created to foster the effective growth of good insurance products.

The distribution of insurance is not a simple matter. Training sales people takes time and needs to be economically effective if it is to thrive. Consumers often need to be taught how the products work to feel comfortable to buy them. Claims specialists need to be taught how to respond fairly and professionally to events giving rise to possible claims. Other obstacles are impeding progress toward pluralizing insurance, one of them often being the level of awareness of what insurance is and what it can do. In some places we also find an attitude to events that insurance is designed to mitigate that says “What will be, will be,” which also makes insurance as a concept hard to communicate. So the path to addressing all these aspects takes time and skill—and costs money.

Pitfalls also lie along the way. The sale of the wrong kind of insurance can lead to the waste of valuable resources that could otherwise be directed to better matters. The unfair handling of claims can lead to customer dissatisfaction and disillusionment with the product. Many communities see compulsory Motor insurance as a kind of motor tax. These types of attitude problems impede all concerned from progress.

As a consequence of these issues, it is important that every country, developing or otherwise, gives careful consideration to the great value of Bancassurance as a means to grow the presence and use of insurance within a community. Bancassurance is relatively recent in comparison with other forms of insurance distribution —Early Marine insurance market was transacted more than 300 years ago in the eighteenth century, and both Life and non-Life insurance beginning in the form of mutual distribution have been with us for more than 150 years. Bancassurance has really only been an effective distribution channel, even in France, where it was first effectively implemented, for about 30 years.

But for all its youth, Bancassurance is emerging as a natural pathway for the effective development of insurance. Banking has been dynamic in the community for far longer than insurance, with some banks even today having histories dating back to as early as

1472. Banking is generally much better understood than insurance as a result. Banking also penetrates further into rural communities than insurance often does or can. There can be no doubt of the importance of the potential for Bancassurance to open the path toward cost-efficient access to insurance products, both Life and non-Life.

This paper therefore sets out a range of key aspects of Bancassurance.

Chapter 1 outlines the strategic aspects of Bancassurance as a development tool. It discusses the essential dynamics of how it works. It describes and debates the many positive value opportunities inherent in facilitating Bancassurance. It also looks at the scope for Bancassurance to go too far and cause problems through mis-selling. The chapter offers an assessment of the advantages, and the challenges, of the distribution aspects. Finally it proposes a preliminary discussion of a selection of regulatory issues for both banks and insurers, a subject addressed in greater detail in the next chapter.

Chapter 2 then goes beyond theory and strategy to consider the dynamics of Bancassurance in practice. It looks at the penetration levels of both Life and non-Life insurance in a wide range of countries and draws conclusions about the general conditions that are needed for penetration to develop. It looks in more detail at how the presence of private credit is a particular powerful indicator of an environment in which insurance can flourish. There follows a detailed review of selected representative emerging markets. This considers which countries have found obstacles and which have shown best practice in creating an effective development path. A final and valuable section then addresses the policy issues that emerging markets are facing. These include disclosure, tied selling, packaging or bundling, wealth management products, licensing and training of point-of-sale staff, and data protection concerns.

We then turn in *chapter 3* to a particularly detailed study of a leading developed market with strong Bancassurance successes. The natural market to choose here was France. An illuminating study is provided, of the origins of Bancassurance, of the factors that have supported the development of Bancassurance, of the reasons non-Life has proved less well supported by Bancassurance than Life has been, and of the new challenges that face Bancassurance in France today.

The natural balance to a study of a developed country would be one of a developing market. Accordingly *chapter 4* reviews the current status of Bancassurance in Mexico. This gives a taste of the key banks and insurers involved, looks at the legal framework, and assesses in detail which types of insurance have prospered and how it is mainly the banks that own insurers (the “integrated” Bancassurance model) that have developed most effectively.

Finally the *conclusion* summarizes the study with brief closing remarks.

Chapter One

Overview and Analysis of the Strategic Benefits of Bancassurance as a Development Tool

Introduction—Bancassurance as a Natural Development Tool

The different ways to approach risk-Exclusion, Management, Self-insurance and Risk Transfer-all play key roles in encouraging effective development. Insurance in particular plays a remarkable role as a development tool in many contexts of personal, commercial, and industrial activity. The different business classes of insurance—Life, Health, Property, Motor, Casualty, Marine, and Aviation—cover the widest ranges of human activities.

One very natural way to encourage the use of insurance is to introduce its use as part of a wider transaction. The consumer who is keen to purchase a house or apartment might not be well disposed toward buying insurance against damage property, but a bank that is lending money to facilitate the purchase would be well placed to explain the importance of having insurance to stabilize the risk. From the bank's perspective, both the life and the health of the borrower are key to the ability to service the loan, and the Property insurance would be key to preserve the security that supports the loan.

On the other hand, the bank that is lending money can quickly be in a position of inappropriate power over the borrower. The linking of a continuing insurance purchase to the continued availability of a loan can lead to an imbalanced situation in which the consumer is not in a position to understand whether the insurance offered through the bank is an attractive purchase.

It is therefore crucial that Bancassurance is used as a development tool in a context in which there is careful regulation of the activities of the lender. This paper explores the strategic aspects of the positive value opportunities, while at the same time examining methods to avoid the pitfalls, of using Bancassurance as a development tool.

Bancassurance—How It Works and Its Potential

Bancassurance—How It Works

The typical Bancassurance sales model is not complex (figure 1.1). A customer finds he or she is going to a bank for a solution to a problem, commonly the need for finance to help with a purchase or a development. The bank's customer adviser is face to face with the consumer. The customer's request is for a loan or other form of financial review. It is an obvious and convenient thing for the bank's customer adviser to be able to offer a range of insurance products to assist with the loan transaction or otherwise enhance the consumer's financial position.

Figure 1.1 Bancassurance Sales Model

The distinctive advantage here is that the customer in many cases does not know or realize how much an insurance product is going to improve his or her situation. In the typical non-Bancassurance sales model, the stimulus to look at an insurance product as a solution comes from a mixed range of drivers—the need to have a motor certificate to drive a car, the encouragement to buy travel insurance from a travel agent or an airline, the at-point-of-sale transaction in a shop to buy Warranty and Breakdown insurance with a physical product such as a car or electronic goods. Most consumers have only a very limited grasp of what insurance can do, and they often feel it as a kind of taxation, especially with Motor insurance. The situation in which the consumer is talking with the bank's customer adviser about a financial need is a powerful moment of sales opportunity. From the bank's viewpoint, the insurance sale is only one of four main lines of sales possibilities (figure 1.1), so the client meeting has multiple possibilities for sales. This undoubtedly makes the Bancassurance attractive because the marginal costs of making the insurance sale are far lower than would be the case for the pure insurance adviser.

Thus we can define Bancassurance as the process of using a bank's branches, sales network, and customer relationships to develop sales of insurance products.

It should be noted that Bancassurance is not simply a sales technique. It is a development channel.

It is also worth noting that Bancassurance is this development channel, whether or not the insurance company is a wholly owned bank subsidiary. Almost always the bank and the insurer will be different legal entities. Sometimes the bank will own the insurer (and, rarely, the insurer may own a bank). Often the bank will not own the insurer—and often the virtues of diversifying the risk will mean that some banks prefer not to own the insurer. So there is nothing intrinsic within the term Bancassurance that implies linkage in ownership terms between bank and insurer.

Bancassurance—The Potential

Bancassurance has had important success in some economies and really quite limited success in other economies. It will be worth reviewing where it has worked well, and contrasting that with countries where it has not worked well, to give some answer to the question –“What is the potential of Bancassurance?”

Where Bancassurance Has Shown Important Growth

Table 1.1 sets out those countries where the market share of insurance placed through Bancassurance has shown important growth and exceeds either 40 percent (for Life business) or 10 percent (for non-Life business). Data are the most recently available as of 2007; sources are insurance regulators, insurance associations, Axco, Limra, and Swiss Re estimates.

Table 1.1 Countries Where the Bancassurance Market Share Has Shown Important Growth and Exceeds 40 Percent (Life) or 10 Percent (Non-Life)
percent

Country	Bancassurers' Life Share	Bancassurers' Non-Life Share
Australia	43	Very small
Belgium	48	6
Brazil	55	13
Chile	13	19
France	64	9
Italy	59	2
Malaysia	45	10
Portugal	88	10
Spain	72	7

Source: Authors

The penetration into Life insurance sales in many of these countries has been spectacular. Chile is quite unusual in that there has been greater success in non-Life than in Life with Bancassurance penetration. But in Brazil, France, Italy, Portugal, and Spain, the use of Bancassurance sales techniques has literally transformed the

marketplace. The Australian numbers may be distorted because of the acquisition of Life insurers by banking groups; this creates an apparent link, but to a significant degree the source of the market share in some Australian cases did not originate in the Bancassurance sales process.

Where Bancassurance Has Shown Limited Growth

Table 1.2 sets out those countries where the market share of insurance placed through Bancassurance has shown limited growth and less than either 40 percent (for Life business) or 10 percent (for non-Life business). Data are the most recently available as at 2007; sources are insurance regulators, insurance associations, Axco, Limra, and Swiss Re estimates.

Table 1.2 Countries Where Bancassurance Market Share Has Shown Limited Growth and Exceeds 40 Percent (Life) or 10 Percent (Non-Life) percent

Country	Bancassurers' Life Share	Bancassurers' Non-Life Share
Canada	1	Negligible
China	16	Very small
Germany	25	12
Japan	Very small	Very small
Mexico	10	10
Poland	14	Very small
Korea, Rep.	9	4
Taiwan, China	33	Very small
Turkey	23	10
United Kingdom	20	Less than 10
United States	2	Very small

The penetration into Life insurance sales in many of these countries has been material but not nearly as impressive as the first group. This prompts the question asked in the next section's heading.

Why Do Some Countries Show Strong Growth and Others Limited Growth?

Numerous factors influence the differences shown by the above two tables.

At the heart of the U.S. and Canadian market's low response to the Bancassurance concept is the regulatory situation there. Only in 1999 did the Gramm-Leach-Bliley Act remove obstacles to banks selling insurance, which had been in place since the 1933 Glass-Steagall Act. This, allied with the reality that the U.S. Life market was

already deeply mature, made it harder for a brand new sales approach to make a worthwhile return on investment.

Similarly in Korea, regulatory constraints before 2003 made it hard for Bancassurance to gather any momentum. Even in 2003, only pure savings products and loan protection insurances were authorized for sale by banks, with greater flexibility being allowed beginning in 2005.

Thus one basic reason for differences between countries is the extent of regulatory constraints.

Other reasons may be cited as well. In Germany the presence in many villages and towns of insurance agents that have handled insurance matters for people from one generation to the next has meant that culturally there has been resistance to the idea of buying insurance through banks. In the United Kingdom strong movement has been seen toward buying insurance over the telephone and online. The cost savings of these distributional arrangements have curtailed the scope for growth in Bancassurance, especially in non-Life lines. On the Life side, the substantial market for arranging Group Life insurance coverage through employers has also made it harder for Bancassurance to make progress because many U.K. employees have Life coverage through their employment contracts.

Other Motivations and Implications in Bancassurance

We should mention further nuances here, including the following:

- Delivery of post-sales service—this is both an opportunity and a risk for the bank
- Gaining of efficiencies in the administration—the bank may be able to use existing staff to deliver the insurance servicing in addition to their existing tasks
- Increasing customer loyalty and lifetime value—again this is a risk as well as an opportunity for the bank because a poorly executed insurance product can damage the brand, while a well-delivered insurance experience can enhance it
- Capital advantages through diversification of risk—this needs careful analysis and generally is beyond the scope of this paper and
- Arbitrage opportunities, which may enable a bank to hold an advantage over its competitors.

What Is the Potential for Less Developed Markets?

The answer must be that the potential for growth in all insurance lines is very great, so the issue should not so much be how great is the Bancassurance potential, but how

great is the overall insurance growth potential. The understanding in many less developed markets of the value of insurance, whether for Life or non-Life products, is often at a modest level. This means that the scope for using Bancassurance to boost development is very significant indeed.

However, the enthusiasm for strengthening an economy through the use of increased penetration of insurance products must always be tempered by the need to ensure that insurance is bought for reasons that are functionally effective in the economy. Some types of insurance add very little value to the wider economic system; one thinks of many brown- and white-goods warranty insurance plans,¹ some types of unemployment insurance, and some types of Life insurance where sufficient coverage already exists. This leads us naturally into the next part of our discussion, where we review the development opportunities from the perspective of whether they present positive or negative value propositions.

Positive Value Opportunities

Life

Both the bank and the dependents of the borrower are at risk in the event of the death of the borrower.

From the bank's point of view, Life insurance can be used to diminish the hazards of both secured and unsecured lending. The risk of default on a loan once the borrower had died is understandably high. The situation tends to be different depending upon whether the loan is secured or not.

If the loan is properly secured, such as is likely to be the case with a Property loan, the bank may not be much in need of Life insurance to support the loan. The security itself would usually be expected to be sufficient to guarantee the repayment of the loan principal. In this situation, it is likely to be more a concern for the dependents of the borrower, who may find that not only have they lost the person who may well be the principal earner in the family, but at the same time they are facing finding a new home because of the requirements of the bank to repossess and sell the property to recover the loan for which the property was providing security.

By contrast if the loan is not secured—a common example would be the position on a credit card facility—the dependents would normally not have the liability to repay the loan, nor would they be concerned if the bank were to suffer loss on the loan. So it would seem that the bank would have greater interest in insurance coverage being in force for the Life risk on their unsecured loan portfolio.

In either situation, the demand for insurance coverage should be strong. It is clearly an attractive proposition to a property borrower for the lender to be able to say, “And if you were unfortunately to die before your being able completely to repay your mortgage, then the Life insurance component of this package will completely repay your debt. In that situation, your family will be free of the debt and the property will pass to them without the bank needing any payment to close down the loan.” Equally it is probably sensible practice for the bank to price (into the cost of providing unsecured debt such as that in credit card issuance) the consequences of the risk of the borrower dying, because in most cases this scenario ends with the bank absorbing a loan write-off. Some banks may prefer to handle this risk implicitly, without purchasing the Life insurance externally. This saves on administration and is probably risk efficient because the Life exposure is actually rather a stable risk. Other banks may prefer to outsource the Life insurance risk and seek to minimize the risks absorbed on their own balance sheet.

Property

The bank involved in a Property loan portfolio faces a number of economic hazards affecting each property. These derive either from concerns about continuing loan repayments or from the risk of impairment of the collateral. They include the following:

- The building burns down
- The building is heavily damaged due to natural peril disaster
- The borrower loses employment, thus disturbing the borrower’s capacity to repay the loan
- The housing market collapses, giving the borrower a heavy disincentive to worry about repaying the loan, because the value of the loan might exceed the value of the property by a large margin.

All of these carry hazards from the bank’s perspective. It is valuable to discuss each in turn.

Generally the risk of the individual building burning down is a specific location issue and does not represent a systemic threat to the bank. However, a serious fire at a property that is not insured would cause severe disruption to the borrower, and the likely consequence of noninsurance would carry a high risk of impairing the security for the loan. It makes sense for both the bank and the borrower to be certain that insurance is in place.

The second hazard mentioned, that of a natural peril disaster such as a very large windstorm, flood, or earthquake, can be devastating for numerous borrowers simultaneously. This scenario would cause severe disruption for both borrowers and bank if it were not properly insured. Indeed, the risk of such natural disasters causes

the insurer significant discomfort, and this is why most insurers carry extensive property catastrophe reinsurance programs.

The risk of the individual borrower defaulting due to loss of employment carries the potential to be significantly problematic for the borrower. Without the income to meet the loan repayment schedule, the borrower may well be forced to sell the property. In most situations in which the borrower's loss of employment is an isolated case, the bank is not seriously at risk because the Property loan is secured by the title to the property, and thus (barring the resale occurring at a time of serious house price collapse) the bank has a fair expectation of recovering the substance of the value of the loan. However, at times of significant national economic recession, risk of collective unemployment may be high. Collective unemployment may act as a collective trigger for a heavy reduction in property pricing, because if large numbers of borrowers are forced to sell their properties at the same time, the laws of supply and demand will enforce a drop in prices. The bank's risk quickly multiplies upwards in this scenario, as we will see in the next, fourth hazard.

The fourth exposure mentioned, that of a general collapse in property pricing, can have significantly problematic consequences for the bank, as well as heavily damaging consequences for the borrower. For the borrower, the loss of value in the property asset on which the loan was based can be a manageable risk. On the one hand, if the borrower continues to be employed and can thus continue to meet the repayment schedule, the variation in value (which may only be temporary) might seem unimportant in the longer term. On the other hand, if the borrower loses employment, there may well be temptation to "hand in the keys" to the lender and leave the bank with the problem of reselling the property and absorbing the loss that ensues when the resale proceeds turn out to be lower than the loan.

However, from the bank's point of view, the systemic consequences of a major collapse of house prices will be the risk that many borrowers default and material proportions of the loan portfolio may turn sour. Many historic examples can be identified of serious troubles for the banking sector arising as a consequence of housing market price collapses. However we would like to point out that this is a risk that bank has to undertake. Genuine credit risk that is caused by house price collapse should not be advised to pass on from bank to insurer.

The clear consequence of all the foregoing is that both the borrower and the lender will be in a much stronger position to meet the economic hazards of the future if the property-based loan is supported by a properly designed Property insurance product. Insurance cannot cover all the development perils; it is clear from the above example that insurance cannot address the systemic risk of property price collapse, for example, and other perils are found as well, such as war and nuclear (the latter most disturbingly illustrated by the March 11, 2011, tsunami disaster at Fukushima Daiichi), which are generally beyond the capacity of the insurance industry to cover.

For catastrophe insurance to be optimally effective, the insurer ideally should not be a subsidiary of the bank. The catastrophe risk may be subject to external reinsurance, but the catastrophe peril is very hard to eliminate entirely because the retention before reinsurance, the creditworthiness of the reinsurers, and the potential risk that a catastrophe loss might be so severe that the limits purchased are insufficient would all leave a bank-owned insurer retaining a catastrophe risk that would impact the gross corporate balance sheet.

A further virtue of linking the sale of Property insurance to the sale of a Property loan is to be found in distributional efficiency. However, because this matter applies quite closely to all types of Bancassurance sales, it is discussed at the end of this section.

Motor

The Motor situation is a more complex picture than the Property one. Many individuals feel strong peer pressure to own a new vehicle. It is often seen as a key status symbol, but its value depreciates quickly, and its location is not fixed. These two aspects give banks a different proposition; it is harder physically to repossess a mobile asset than a fixed one, and the extent to which one can extend a loan supported by a diminishing-value asset is restricted.

Hence Motor-based loan portfolios often are restricted to a three-year term (occasionally up to five years), and the up-front cash requirement from the customer is usually higher. Typical Motor loans can require 30 percent up-front cash, whereas Property loans can be as low as 10 percent or occasionally lower still. Further, the typical face value of the loan is much smaller in financial terms than a Property-based loan: Motor loans typically are for values ranging from perhaps 20 percent of a Property loan value down to as little as 5 percent of a Property loan value.

So the term is much shorter, the cash commitment much higher, and the scale of the Motor loan is much lower, than is the case with a typical Property loan.

A fourth and critical complication in using Bancassurance for development purposes is the fact that the Motor insurance risk is varying in many complex ways depending upon the vehicle and the driver of the vehicle. Property insurers are only slowly moving to bring focus upon the fact that the age of the occupant of a property is a determinant in the risk. Occupants aged between 60 and 80, for example, tend to be better theft risks, simply because there is a far higher proportion of time when such properties are occupied. Younger couples are often both out at work and thus represent higher theft risks. So customer-based nuances are found in Property insurance pricing. But these are nothing compared with the rich range of variables that affect Motor insurance.

Many banks have tried their hand at linking the sale of Motor insurance to the sale of a car-linked loan. The motor dealers likewise have tried to generate commissions by selling Motor insurance as part of their car sale proposition. However, these efforts have not always met with unqualified success. Much depends upon the pricing structure of the Motor insurance market.

In the case that the Motor insurance market is structured around a unique fixed price per vehicle, scope should be left for the bank to sell the Motor insurance alongside the car-related loan. Questions of economies of scale may be seen—it is quite possible that the compulsory Motor insurance premium is too small for it to be practical to sell the insurance efficiently. But with a Motor price structure that is not much related to the underlying driver risk, and that is also large enough for the commission available to an agent to be worthwhile, scope is found for Bancassurance to be an effective development tool.

More commonly the Motor insurance will be structured around a price that is significantly linked to the specific driver risk. In this situation, if the bank that is proposing the car-related loan tries to offer insurance at a fixed price, the typical response of the mature driver with a clean accident record is to prefer the cheaper price available by using the maturity and clean record information to buy separate insurance in the open market. Conversely, the young driver with a serious accident record is likely to find any fixed price proposition attractive. So when a fixed-price Motor insurance is offered at the same time as a bank loan to buy a car, the attempt tends to work poorly.

The alternative here is to offer a variable-priced insurance product. This tends to involve a sequence of questions, sometimes touching upon issues that the customer prefers not to have raised (for example, past accident record discussions can lead to tensions). Most motor sales people prefer not to get involved in such discussions because they can disrupt the final points leading to the firm sale of the car. Hence generally it is not easy (in a risk-linked market pricing structure) to sell Motor insurance in conjunction with offering the loan that might assist in completing the car sale.

This does not mean that Bancassurance in the Motor arena is predestined to fail. One quite popular product is the insurance that is sold as a single-premium coverage that reimburses the entire original cost of the car in the event that the vehicle suffers a “total loss” write-off within the first three years of its existence. This is less contentious than the more general Motor third-party insurance, and it has a natural appeal to the customer as a means of paying off any loan taken out to purchase the car in full if the car is written off.

So some scope is found to use Bancassurance to develop in conjunction with Motor-based loans. But this is a much weaker area than Property and Life.

Other—Health/Medical, Travel, Commercial

In a situation in which a bank is talking to a customer about any kind of loan, scope can be found to develop a sale of insurance, whether of Property, Life, or Motor, as discussed above, or of other lines such as Health and Travel. Scope also exists to expand a commercial loan discussion into commercial insurance lines.

We can discuss these three in reverse order. This paper is focussed closely upon Bancassurance in a personal lines context, so the commercial lines potential will not be expanded in any detail here, but it nevertheless represents a business development opportunity for banks.

Similarly although Travel insurance is a very useful product for those traveling abroad—especially to the United States, where the medical system is materially different from most non-American systems—the reality is that Travel insurance is best sold alongside the travel decisions (for example, the long-distance journey tickets). Some banks have sold insurance alongside the foreign currency sales, but generally this is not likely to be a strong growth line for developing countries.

Health, however, may be an important sale to assist in securing a loan of any kind. Here much will turn upon the domestic situation in the country concerned. If a strong health support network already exists that cannot be easily accessed without finance from an insurance policy, then there may be good scope to improve the stability of the loan risk by encouraging the borrower to purchase Health insurance. On the other hand, if the health support network is not strong, this potential may be limited.

Negative Value Opportunities

Unemployment Insurance

The example of Unemployment insurance is worth reviewing in some detail because it illustrates the extent to which the consumer public can be convinced to purchase financial products that may well be unsuitable for them.

Unemployment insurance (known as Payment Protection Insurance or PPI in the United Kingdom) has been sold in the United Kingdom for more than 30 years. From the point of view of the bank loaning money secured by property, the two critical risks are (1) that the borrower loses the income that is required to service and eventually repay the loan and (2) that the value of the property drops below the value of the loan. Clearly the bank is unlikely to suffer materially if only one of these risks comes to occur—if the property value drops heavily but the borrower maintains payments, the bank does not suffer; and if the borrower ceases payments but the value remains above the level of the loan, the property can be sold and the loan recovered.

We have already seen how banks can reasonably require that borrowers maintain Property insurance, to protect the gross value of the property asset. Unemployment insurance has been sold to alleviate the stress upon both the bank and the borrower in the event of the borrower ceasing to be employed. The difficulty here in the United Kingdom was that the insurers were understandably very concerned that the process of selling this insurance could cause severe problems of anti-selection. Clearly any individual applying for a new loan while being well aware that there was a high risk of his or her employment being terminated would be a keen buyer of Unemployment insurance. Conversely, those individuals who believed they had safe jobs would be reluctant to purchase this coverage.

As a consequence of this pressure from insurers (and perhaps also because the additional insurance sales would drive additional commission revenue), the banks adopted pressure-selling tactics to convince people taking out loans also to take out Unemployment insurance. Effectively, those workers in secure jobs were being asked to subsidize the unemployment risk of those in weak jobs. A minority of strong-minded consumers resisted buying the insurance, but once the remaining consumers became aware that they had purchased a product that was not really suited to their needs, a public controversy ensued, and in April 2011 the U.K. banks were forced into an admission that these policies had been improperly sold. It is estimated that refunds to policyholders may cost the U.K. banking sector anywhere from £4 billion to £7 billion.

There is no absolute “right” or “wrong” here. Some observers would argue that it is a healthy thing for those people in secure jobs to make a contribution to the position of those in insecure jobs.

But wider economic issues are at stake. The existence of these insurances encouraged some people to buy property who were not really in a sensible position to undertake the commitment of a long-term home loan. This in turn fueled an increase in property prices. The more the property market has been inflated, the more it deflates when the economy turns into recession. So the existence of these insurances did not actually serve the wider development of the economy well.

In addition, the insurers carrying the risks of those policies were not at all well placed to manage the exposure. Unemployment insurance is subject to severe systemic risks. The insurers could not build reserves sensibly to allow for the much higher frequency of claims that would be likely to happen in a severe recession. So the process by which the insurers accepted the exposure was in turn creating an instability within the insurance sector that was likely to cause insurer insolvency risk at exactly the low point of recession when the wider economy would least want insurer insolvencies to be disturbing the development of the economy. At such times the community needs insurers to be at their strongest, not at their weakest.

Distribution Advantages and Challenges

Distribution Advantages

Bancassurance carries important distributional advantages over traditional insurance agency networks. However, in an age in which insurance is frequently sold via the Internet or via the telephone, the earlier distributional efficiencies that helped Bancassurance develop in some countries are not so clear.

One critical advantage held by the Bancassurance model is that the insurance is often a *minor add-in cost* when viewed as part of a much larger economic transaction. So the decision to take it (or not) is a relatively simple one. If the customer is taking out a loan that will run for perhaps 25 years, the insurance that helps make the transaction work may be only a small fraction of the interest payments.

Often the *branding* of the bank's use of the product concerned is a source of comfort—indeed, for the bank this is a specific example of a moment when the bank's brand is brought directly to bear by lending credibility to the insurance product.

Third, a key advantage is seen from a *customer sales opportunity* perspective. The customer is sitting right there thinking about (for example) the new home for which the bank is offering a mortgage loan. The same customer has insurance needs that can be resolved there and then. This is a much easier proposition than for some insurers, where the sales process can require a pre-sale excursion simply to establish the insured's renewal date so that the timing of a competitive renewal offer can be judged accurately. Some insurers employ telephone sales clerks whose job is to telephone potential customers and ask for their Property and Motor renewal dates; for the bank that is in the middle of selling a loan for a new purchase, this issue scarcely arises.

Extending this is the *transactional data advantage* that a bank enjoys with the benefit of its prior knowledge of already knowing its customer. In some jurisdictions the use of such information is strictly controlled.

A fifth advantage held by the Bancassurer is the ability to *control the renewal process*. This can easily act to the significant disadvantage of the consumer (a point discussed below under Regulatory Issues for Banks). From the bank's point of view, however, it may be dynamically important that the borrower maintains proper insurance in relation to the loan—whether that be the Property insurance where the loan is secured by a title to property, or Life insurance in regard to the securing of the income stream intended to repay the mortgage, or otherwise. So the bank has a key position in being able to oversee and ensure the safe renewal of the underlying insurance.

An additional issue here is that the longevity of the insurance is of general assistance to the wider process of communicating to the community the value created by insurance. The borrower who perhaps at first did not understand the details too clearly will quite possibly notice the annual deductions for the cost of insurance and ask in more detail about why the insurance remains part of the loan agreement. The more that occasions like this arise, when the general public attains greater appreciation of the purpose and value of buying insurance, the more effectively these issues will be accepted by the wider community.

Distribution Disadvantages

In contrast to the five points mentioned above favoring Bancassurance as a distribution mechanism, numerous negative issues point to limitations for Bancassurance.

One problem is undoubtedly that the training of sales personnel is a complex and expensive process. Banks certainly have to give careful thought to the cost of training the sales personnel, which can never be as cost efficient as, for example, an Internet program can be. This is the principal reason why success in Bancassurance has been mainly limited to Life and Property products.

A second lies in the motivation of sales personnel. In some countries the motivation process is limited to gifts such as holidays, microwave ovens, and the like; in others, depending upon the history and culture of the organization, varying forms of remuneration linkage can encourage the process. But these things again cost more, both in money and in management time, than a computer program. Allied with this is the potential for a misalignment of interests—the sales personnel may want one outcome (because of how they are motivated), but the bank may be aiming for another outcome. This could be a cultural matter, and the potential for cultural clashes is a further concern.

A third and structural point is that the “~~key~~ moment” in Bancassurance comes at the key moment when (for example) the loan is sold. Once the customer checks the value-for-money of the product and decides that a superior—or at least a cheaper—product can be purchased elsewhere, almost no chance remains to recover the customer’s business. This lies in sharp contrast to the Internet search engine business model, when each year the search engine can test the market and offer the customer whatever is the most recent and most attractive alternative.

In the end it is the cost ratio that counts over the long term. Bancassurance generally has cheaper cost ratios than almost all traditional agency-based sales processes. It is less competitive than the most modern Internet-based alternatives. But even where there might be a cost issue, Bancassurance has the “~~key~~ moment” advantage of having

the customer wanting to conclude a wider loan transaction. This is not easily replicated anywhere.

The Bank as “Trusted Adviser”?

Underpinning all forms of Bancassurance lies the proposition of encouraging the consumer to accept the bank in the role of trusted financial adviser.

This is a ~~two~~-edged sword,” as we shall see. Banks across the planet have a mixed record. In a significant number of countries, the banking system has taken undue levels of risk, and the wider community has been forced to resolve the ensuing systemic breakdown. In several of these instances, the state has not ended up losing money, but in many cases the cost to the community has been high. It would not be possible to argue that the banking sector generally has had a good track record of keeping its own financial status in sound condition over, say, the past century.

Banks also have a doubtful record in regard to the giving of good advice and conducting themselves in ways that the wider community would regard as appropriate. In many countries one can point to examples of banking groups overcharging the personal lines sector to meet losses sustained in their commercial and international loan books. The individual consumer is generally a soft target for profit in the mind of the bank—only a low proportion of consumers are really alert to what their options are or what a financial transaction means to their counterparty.

Accordingly, caution should be exercised in any context in which financial regulators are looking at encouraging financial enterprise that passes undue power to the banking sector. In the discussion above, we reviewed one specific example in which the banking sector in the United Kingdom overstretched itself in the sale of a particular insurance product. In this example the banking sector attracted much criticism for the perceived abuse of its status as ~~trusted~~ adviser” in inappropriate overselling of one form of insurance. It should be clear that a firm regulatory hand is likely to be needed.

On the other hand, the hazards of a too-powerful banking sector may be a modest concern when viewed alongside the critical questions of how best to promote stable growth in developing countries. Insurance, with all its wide applications to every aspect of personal and commercial interests, is a vital tool for the promotion of stable growth.

The balanced position should therefore be to encourage the use of Bancassurance as a development tool while setting up regulatory mechanisms to monitor the potential for abuse and to introduce appropriate competitive freedoms to ensure a healthy development environment. Below we will offer suggestions as to a suitable regulatory framework.

Factors Affecting Bancassurance Development

Naturally a wide range of factors affect the positive or negative development of Bancassurance.

The Legal, Regulatory, and Taxation Framework

The legal and regulatory framework can easily stifle development, as the example of Korea shows. Before 2003 the insurers were given extensive protection against the possibility of the banks growing strongly in their field and subsequent liberalization has continued to be resisted. Similarly in the United States the Glass-Steagall restrictions on links between banks and insurers has made Bancassurance there a tiny fraction of what its potential has been shown to be elsewhere.

Taxation is also a dynamic driver of sales potential. Before 1998 in France, material tax advantages were available on a range of capital redemption contracts, including for some years a tax deductibility of up to 25 percent on Life insurance premiums. Following the 1998 and 1999 tax reforms, the appeal of these products dropped significantly, and sales reduced by some 15 percent, although more recent data show that this was temporary and that the Bancassurance arena has been impressively resilient. More generally, the taxation reliefs allowed to Life insurance sales in France, Italy, and Spain were clearly important drivers of the successful growth of Bancassurance in those countries.

Thus a sensible legal and regulatory framework is a key factor in creating a platform from which Bancassurance might be encouraged. Likewise sensible taxation allowances will make an important difference.

The Arbitrage Potential

The range of issues here is really too complex to discuss in any detail, but it should be mentioned that wherever the regulatory environment provides scope for a bank to use Bancassurance to develop profit potential through the use of one or another form of arbitrage, the likelihood is that such a situation will be exploited—sometimes damagingly for the wider community.

The Customer-Bank Relationship and Distribution Network Density

Generally speaking, the denser the network offering the product, the more successful it is likely to be. The Spanish example is helpful here. Spain has one of the densest bank networks in Europe, and they provide a very high level of direct customer responsiveness. With customers ready to conduct business and comfortable with

interaction in their banking environment, Spanish Bancassurance sales are naturally developing smoothly.

This is in contrast to matters in, for example, the United Kingdom, where automization and telephonization of many banking functions has led to much reduced levels of confidence and sympathy between customers and their banks. The imposition by U.K. banks of punitive levels of charges for minor overdraft incursions has also been a cause of damage to the banks' branding, which has created a consumer reluctance to take advice from banks about the purchase of insurance products.

So an open branch network and a good quality bank-to-customer relationship are important foundation stones for success in Bancassurance.

Good-Quality Products

The flexibility of the range of features on offer in the Bancassurer's insurance products is a third key success issue. Too much flexibility tends to lead to indecision and low take-up rates. Insufficient flexibility, on the other hand, can hamper growth.

Similarly the product design needs to reflect the reality of the sales environment. If an insurance product is mainly an investment vehicle, it will compete inefficiently with the investment products that the Bancassurer's employee is also trying to sell.

Price and Provider Choice

A fourth issue concerns price and the perception of choice. Both of these issues, which are naturally interrelated, are likely to help. Whichever insurance product is being considered, the option of different service providers and perhaps different price levels for minor differences in product (such as deductibles in Property insurance) makes for a desirable level of consumer choice and gives rise to a healthy level of competition between insurance service providers.

It should be recognized that some disincentive exists for both the bank and the insurance provider if there are too many providers –“on the menu” as far as the consumer is concerned. This is partly because of the dilution in potential market share, and partly because of the risk that offering a panel of possible insurers creates another level of sales complexity that might deter buyers.

However, in the wider scheme of things it is undoubtedly a healthy discipline for the insurance provider in any sales pitch to be set side by side with at least two other providers, to allow the consumer a sensible level of choice.

Regulatory Issues for Banks

Standard Coverage on a Sound Basis

Much is to be gained and little to be lost if the insurance market operates from a starting point of a limited number of transparent standard coverages. It is not important whether these emerge from the insurance regulator's office, from the office of the national insurance companies' association, or from some other source or process. Without a basic standard coverage as a reference point, however, the consumer is easily bewildered as to the purpose and value of the product on offer.

The second principle of coverage must be that it includes the critical perils required. Property insurances should include all natural perils and adopt only limited war and nuclear exclusions. Motor insurances should cover all forms of third-party liability, up to the national legal limit required.

There is scope for variations—with Motor, most obviously, for one's own damage to the vehicle, and with Property, for theft perils. But a transparent standard for basic coverage is a key “building block” in the process to enable a consumer public with little appreciation of the finer nuances of insurance to be given a starting point for their understanding of the different financial products on offer.

Use a Panel of Insurers

It is an open question how best to address the customer's choice of insurers. If a bank or other agent offers the consumer only a single insurer, the customer should rightly be concerned whether he or she is being offered the best product at the best price. Choice is at the heart of healthy practice.

On the other hand, the bank is going to be significantly more motivated to promote the insurance if the business is being channeled to the bank's preferred insurer. This is more notably the case if there is a shareholding linkage between the bank and the insurer.

Many difficulties are seen in regulating the sale of insurance by a bank where the insurance provider is not under competitive pressures, especially if there is a shareholding linkage between bank and insurer. There is no easy answer here, because it is absolutely an open possibility that a bank should convince a borrower to buy a supposedly relevant insurance as part of the loan sales process, and yet the alert borrower might easily check the situation afterwards and discover that the arrangements in the end were quite unsuitable. This type of problem occurred very extensively in the United Kingdom with Unemployment insurance, where in the end billions of pounds of premiums were eventually refunded to consumers. No research

is available regarding the appropriateness of Bancassurance sales in the Life and Property classes—one could imagine that it would be reasonable for the bank to sell Life coverage to match the value of the loan, enabling the surviving spouse to pay off the loan in the event of death of the principal borrower, but there must be some cases in which this outcome would be a form of over-insurance and thus be an inappropriate sale.

For these and many other reasons, a panel of insurers is strongly likely to deliver the healthiest outcome to the consumer.

Even in the case that the bank establishes a panel giving the consumer some basic choice, scope still remains for matters not to run as one would expect. The sales people can be trained to slant the sales pitch in favor of a particular insurer, and the other panel members may have wanted to offer cheaper terms in pursuit of greater volumes of business. The regulator may find it suitable to issue guidelines that outline this type of concern and take steps to check whether the spirit of a fair sales process is being adhered to or not.

Ensuring the Consumer Has a Fair Choice

If the consumer is not being offered a balanced choice at the point of original sale, the regulatory process ought to ensure that the consumer has free choice to change insurer at his or her discretion. The operating protocol for the bank should avoid the possibility that the bank sells a loan with the condition that the borrower maintains insurance *with the insurer nominated by the bank*. It may be reasonable that the bank should take steps to be assured that the insurance is in place. This would arise, for example, where Property insurance is required to ensure the security underpinning the loan is in good state. So a loan condition that provides for example that *the borrower should maintain [a specified] insurance and notify the bank of its terms and conditions annually* would be reasonable.

Making the consumer aware of the right to a fair choice of insurer would also be very desirable. It would be sensible for the consumer to be required to sign to acknowledge a clear statement such as “I am aware that I have a choice as regards the insurer and that I am free to change insurer after the first 12 months.”

Limiting the Bank’s Fee

A final safeguard should be considered regarding the fixed fee being taken by the bank. Many consumers would be significantly concerned if they knew the size of commission being retained by the bank in many of these types of transactions. As so often is the case, full and plain disclosure of the state of affairs is a key way to ensure fair play. The regulator could set a base commission level (such as 20 percent of premiums), up to where there might be no need for “full and plain disclosure.” But if

commissions to the bank are higher than that base commission level, a sensible protection mechanism should be required—for example, that the consumer should be required to sign specifically against a statement making plain the size of the bank’s commission.

Regulatory Issues for Insurers

The other side of the coin in regard to regulatory work on Bancassurance is that numerous issues must be addressed regarding the insurers.

A Fair Chance to Be Involved in a Bancassurance Panel

Where a panel of insurers is to be involved, a healthy selection process should be in place to enable all insurers to have a chance to be named on the bank’s panel. The bank has a right to choose insurer partners that meet its standards, but if the bank is to avoid the more restrictive regulatory processes that would be needed to protect the consumer in the case of a sole insurer offering, then the panel selection process needs to be seen to be objective and fair.

It would be open to each regulator to take appropriate local steps to ensure a fair selection process.

Adequate Insurer Security

This is a much wider question than arises specifically in the case of Bancassurance, but it is nevertheless important to say that the bank should be required to offer insurance only with insurers who are within the national insurer insolvency scheme (or, in the absence of such a scheme, insurers that the regulator might determine as being acceptable for the purpose).

In the case of a panel of insurers, it could be appropriate for the bank to be required to disclose the relative security standings of the insurers concerned, as measured by, for example, an external credit rating agency.

Appropriate Reinsurance Coverage

A further check would be appropriate on the status of the insurer’s reinsurance program. It is not necessary to go into undue detail here, but it would not be hard for the regulator to ask for the status of the current program and the basic information that would enable the regulator to assess whether the program is adequate.

Fair Claims Handling Record

A further test on whether the insurer is suitable for a Bancassurance panel would be the insurer's performance with fair claims handling. A test on the number of consumer complaints or referrals to the national insurance claim complaints scheme would not be hard to create and monitor.

Chapter Two

The Dynamics of Bancassurance in Practice

Chapter 1 has provided a review of Bancassurance issues from a general strategic viewpoint. We turn to consider the actual experience of a wide range of countries to comprehend the Bancassurance dynamic. This chapter will first engage with the observed practice of insurance market development. The first section may be passed over by the reader who is keen to review the range of practices in the selected individual markets, which are set out in the second section, and the range of policy issues facing emerging markets, which are set out in the third.

Approaches to Understanding Insurance Development

We start this chapter with a review of the observed reality of various aspects of how insurance develops, to cast a clear perspective upon the potential for Bancassurance to play a key role.

Insurance Market Development

The development of insurance markets is strongly correlated with GDP per capita, as will be seen in figure 2.1.

Figure 2.1 Relative Development Paths: P&C and Life Insurance against GDP per Capita, 2009

Sources: AXCO reports, IMF database, World Bank analysis.

Numerous other inferences can be drawn from this chart:

1. The scatter of the non-Life dots is much closer together than the scatter for Life. This shows that GDP per capita is a stronger predictive variable for P&C insurance than for Life—in other words, if you know the GDP per capita figure, you have a better chance of guessing the non-Life penetration than you do of guessing the Life penetration.
2. P&C tends to develop earlier than Life insurance, but Life tends ultimately to dominate once high-income levels are attained.
3. Variability around the regression line is greater in low-income than in high-income countries.
4. A power curve (that is, a networking effect) applies for both Life and non-Life. In other words both Life and non-Life penetration tends to grow faster than GDP growth, with Life increasing faster, once required income thresholds are reached.

The scatter in figure 2.1 is nonetheless wide, especially in Life insurance. It would be helpful to understand this better. Recent research (Feyen, Lester, and de Rezende Rocha 2011) has helped to identify numerous variables that account for a significant proportion of the scatter. These variables are shown in table 2.1, and many of them are strongly predictive. A number of them are correlated with GDP but still show strong predictive capacity even when due allowance is made. In particular,

- The size of the vehicle fleet is important for the development of Motor and thus P&C insurance
- Life insurance development is held back by high inflation rates and low population densities and
- Government control of the insurance sector, limited legal rights, and certain cultural settings tend to be negatives for both Life and P&C.

Table 2.1 Insurance Density: Additional Key Explanatory Variables

Variable	High Inflation	Population Size ²	Population Density	Legal Rights	Private Credit	Vehicle Fleet Size	Middle Class Size	Government Control
Life	–ve	+ve	+ve	+ve	+ve	n.a.	+ve	–ve
Non-Life	?	–ve	?	+ve	+ve	+ve	+ve	–ve

Source: Feyen, Lester, and de Rezende Rocha 20011.

Note: n.a. = not applicable.

The Link to Bancassurance

One of the strongest positive predictive variables shown in table 2.1 is the development of private credit (that is, mortgage and personal loan markets). This is consistent with other studies that show a relationship between the development of the banking and insurance sectors, with causality possibly running in both directions (Arena 2008; Webb, Grace, and Skipper 2002). The exact nuance as to how and why Bancassurance is a strong driver in the effective development of insurance will become clearer as we conduct our analysis in more detail.

Before going further, it will be helpful to test whether the key effect of private credit development is driven by the role of the bank as an intermediary, or the broader role of institutional investors. Research shown in figure 2.2 shows the direct link with GDP per capita. Both bank intermediation (proxied by M2 [money and quasi money] as a ratio of GDP, shown by the red dots) and the role of institutional investors (assets under management as a ratio of GDP, shown by the blue dots) increase with income levels. However, institutional investors tend to become the major intermediaries between savings and investment only in the highest-income countries.

Figure 2.2 Development versus Income (PPP, GDP per Capita): Bank Deposits and Institutional Investment, 23 OECD Countries

Sources: IMF, OECD, World Bank analysis.

Looking at Development from Base Principles

The development of insurance in new markets can also be analyzed using an ontogenic (embryo to maturity) approach, whereby the range of insurance products available gradually expands as incomes increase and needs arise (table 2.2).

Table 2.2 Stylized Insurance Development Model

Stage	Need	Class of Insurance
Early development	Transport/trade	Trade credit; marine, aviation, transport (MAT)
	Agriculture	Crop, rainfall
	Microinsurance	Credit Life associated with microfinance finance institutions (MFIs)
Mid-development	Motor vehicle	Compulsory motor vehicle liability
	Personal loan	Credit Life
	Construction	Contractor's liability (sometimes compulsory)
	Industrial	Fire, boiler, and others
	Education savings	Medium-term savings and protection
Transition	Mortgage debt	Household fire, mortgage lenders risk, Credit Life
	Motor vehicle damage	Comprehensive Motor insurance
	Commercial and industrial	Fire, loss of profits, worker's compensation (this is still part of social insurance in many countries)
	Health/medical	Annual A&H insurance, group medical

	Motor vehicle damage Catastrophe	Comprehensive motor vehicle Flood, earthquake, and others (sometimes compulsory)
	Retirement savings Investment	Tax-supported long-term savings Investment-linked contracts
Industrial	Tort exposure	General and professional liability, pollution, and others
	Households	Multicoverage householders insurance
	Financial planning	Complex Life insurance products

The distribution strategies associated with this growth model have historically been oriented to brokers, agents, and direct sales. Agency-based channels in particular have proved to be highly expensive to establish and can take decades to reach profitability. They have also been subject to high wastage and potential loss of consumer trust. In highly developed markets (aside from the United States, for path-dependent reasons) the agency distribution system is gradually being replaced by the following:

- Direct sales for commodity products
- Bancassurance for simple savings and
- Credit-related insurance products and certified financial advisors for complex needs.

India, where the insurance market was opened to private insurers only a decade ago, provides a good example of the relative cost structures of long-established agency insurers (LIC), recently established agency insurers, and the recently established Bancassurers (ICICI and SBI; table 2.3). Recent studies of European insurers demonstrate a distinct cost advantage for Bancassurance, even where agency-based insurers are more developed (Davis 2007, chap. 8).

Table 2.3 Relative Expense Ratios: Indian Life Insurers 2009–2010
percent gross premium

	LIC	SBI	ICICI Lombard	Others
Acquisition cost ratio	6.5	7.5	3.6	8.9
Administrative cost ratio	6.6	6.5	15.5	25.3
Total	13.1	14.0	19.1	34.2

Source: IRDA annual report, 2010.

Bancassurance is suited to retail (that is, Household) insurance needs. Typically these first arise when motor fleets begin to grow and third-party liability insurance becomes mandatory. To the extent that purchases of motor vehicles are funded by personal loans, banks have an opportunity to write Credit Life and Motor damage and liability business. In practice they are competing with the car dealers and vehicle-testing stations. The latter two classes will have usually been written by the time the bank becomes aware of the transaction. In addition Motor insurance requires an infrastructure and skill base that is generally not found in banks.

Better opportunities arise in meeting medium-term savings needs. These, together with investment-linked contracts, usually form the product range that generates the early rapid growth of the Bancassurance sector. For this reason a strong correlation tends to be seen between the emergence of Bancassurance as a major channel and the number of banks per unit of population. Additional contexts for the growth of Bancassurance include an effective banking culture (that is, a constructive role of banks in the community) and the role of personal savings in meeting life-cycle needs. Where a good education has to be paid for privately and public pension provision is capped, banks have a distinct opportunity to expand their product range in areas that their front-line staff will be comfortable marketing and servicing. These conditions obtain in Southern Europe and parts of East and North Asia, and it is in these two regions that the model is most developed. Where Bancassurance development has been delayed in these regions, regulatory constraints normally are, or have been, in existence (for example, Korea and the Philippines).

Thus the linking of insurance marketing to bank distribution and client bases appears to be an important mechanism for hastening the development of the insurance sector (for other insurance sector developmental levers see Lester 2010). However, this innovation needs to be handled carefully, because mis-selling and overly aggressive use of financial arbitrage (for example, arising from different capital rules) can lead to strong and potentially negative official reactions. Examples of strong regulatory and supervisory responses have already been seen in the United Kingdom, the Middle East, and North Asia.

Bancassurance in Emerging Markets

Selecting Representative Emerging Markets

Representative emerging markets were selected using the following criteria (table 2.4):

- A credible regulatory and supervisory regime is in place
- Bancassurance data are available
- Population is more than 10 million
- M2/GDP is greater than 50 percent

- Bank branches per 100,000 adults are more than 10^3
- Life premium/GDP are greater than 2.0 percent or non-Life premium/GDP greater than 1.5 percent.

India and China were included in light of their large and growing middle classes and active approach.

Despite a wide diversity of approaches, common features are found in emerging markets, including the following:

- The preponderance (until recently) of single-premium investment-linked contracts as alternatives to deposits (thus leading to considerable volatility in Life Bancassurance revenue data in line with returns in equity markets)
- Bank dominance of consumer credit insurance and
- Their generally low share of non-Life markets.

Most of the countries listed either already have data privacy protection laws in place or are planning to introduce them. The Latin American and Maghreb countries have been influenced by historical links to the leading Bancassurance markets (France, Portugal, and Spain), and the EU Accession countries have been influenced by the presence of Western European insurers. The development of Asian Bancassurance has tended to be more country specific, although the global insurers have had some influence.

What non-Life business is written tends, naturally enough, to be associated with lending, mainly in relation to Motor loans and mortgages. In some of the higher income markets, Bancassurers are adopting sophisticated segmentation of their customer bases. This enables them to align better their marketing mixes (product, service level, point-of-sale environment) with income level (table 2.4). A major challenge will be the move from high-volume low-margin single-premium Life products to regular premium savings contracts.

Table 2.4 Leading Emerging Bancassurance Markets

Region/country	GDP per Capita (\$)	M2/GDP (%)	Bank Branches per 100,000 Adults	Life Premium as % GDP	Non-Life Premium as % GDP ^a	Life (Estimated % Bancassurance)	Non-Life (Estimated % Bancassurance)
Latin America							
Brazil	8,360	66	12	1.3	2.0	77	12
Chile	9,484	79	15	2.5	1.6	35	28
East Asia							
China	3,739	167	n.a.	2.4	1.2	48	n.a.
Malaysia	6,920	134	12	2.7	1.5	32	7
Thailand	4,151	110	11	2.4	1.2	31	10
North Africa							
Morocco	2,884	106	12	0.9	1.9	60	3
South Asia							
India ^b	1,077	70	9	3.7	0.6	7	35
EU Accession							
Hungary	12,837	60	17	1.6	1.6	20	n.a.
Poland	11,296	53	33	1.9	1.9	43	4

Sources: World Bank Development Indicators, IMF database, Axco Reports, 2008–2009 data.

Note: Unadjusted Life insurance percentages tend to favor the bank distribution system because of the higher proportion of single-premium business sold through bank branches. n.a. = not available.

a. Including Health and Accident.

b. Bancassurance accounts for 19 percent of non-LIC Life sales in India.

Latin America

Brazil

Regulation: No limit is placed on insurer/bank cross-ownership, except for government banks, which may hold no more than 49.9 percent of an insurer. In practice all insurance transaction must be intermediated through a registered broker, and Bancassurers normally nominate in-house officers to be registered as brokers. In addition all insurance premiums must be collected via a banking institution. This unusual requirement has actually had an important impact on the development of Bancassurance in Brazil.

Segment overview: The Brazilian Bancassurance model closely follows the successful southern European model, with integrated Bancassurers dominating premium income and the tax regime providing incentives for medium- and long-term savings. The two largest banks account for 30 percent of total insurance revenues in the country, and the insurance arms of the major banking groups account for approximately 80 percent of total insurance profits in Brazil, based largely on their dominance of individual Life and pension products. Sales are supported by point-of-sale technology that facilitates illustrations and efficient data capture.

Consumer protection: The Consumer Code bans tied selling (that is, the requirement that a specified product be purchased with a primary product or service). This does not appear to have prevented the sale of Credit Life tied to lending. The supervisor has a consumer complaints division, and a voluntary code of ethics has been introduced by the industry association. The supervisor is considering whether to introduce minimum requirements for brokers' representatives. A data protection law is in place.

Chile

Regulation: Despite active lobbying by the banks, they may not establish insurance companies under the banking law. Banks may sell insurance through subsidiary brokers and are permitted to sell certain products (basically voluntary pensions and simple insurance products) in their branches. Banks are not allowed to own pension administrators.

Segment overview: The leading insurers operating in the Bancassurance sector are the international arms of the leading French (Cardif) and Spanish (Santander) Bancassurers. Between them they account for nearly half of total Bancassurance premiums in Chile. Most Bancassurance business is lending related and written on a group basis (that is, the bank creates the group). Banks control 98 percent of Credit Life premium revenues.

Consumer protection: No Bancassurance-specific consumer protection rules exist in Chile. The supervisor maintains a consumer assistance unit, and the main consumer organization has a specific section dealing with policyholder rights and recourse options on its Website. The industry association has created an ombudsman to handle claims not being handled by the supervisor, by arbitration, or through the courts. A data protection law is in place.

North Africa

Morocco

Regulation: Cross-ownership and holding company structures are allowed for banks and insurers. No prohibitions are in place on insurance company representatives operating out of bank branches. Under the insurance law, bank staff are allowed only to sell a limited range of products including Life insurance, Credit insurance, and Assistance insurance. All other insurance products may be sold only by licensed brokers and agents, the supply of which is controlled through an examination system.

Segment overview: Most insurers are composites, and all major insurers are parts of financial conglomerates. Until recently an important Bancassurance product range consisted of low-margin single-premium investment contracts. At least one leading Bancassurer is now trying to achieve a more profitable product balance, and this has seen aggregate Life Bancassurance volumes plateau in recent years. Most individual pension business is intermediated through banks, and this offers considerable opportunity. The main non-Life products sold by banks are Property (that is, mortgage related) and Health (a significant part of Health insurance remains with private sector insurers).

Consumer protection: The main consumer protection mechanism involves the training, examination, and licensing of intermediaries and a range of requirements relating to the handling of policyholder moneys.

East Asia

China

Regulation: A prohibition on cross-ownership of banks and insurers was relaxed on an experimental basis in 2008. Six major Chinese banks have since acquired majority holdings in a number of relatively small Life insurers, and one major insurer has acquired a bank. Until this reform, insurers normally arranged agency agreements with individual bank branches. Insurers agents and staff have not been permitted to sell in a bank branch since November 2010.⁴

Segment overview: There appears to be no restriction on telemarketing to banks' customer bases. This is likely to be the major focus of the newly acquired insurance subsidiaries. Past sales data, which saw Bancassurance account for a peak of 60 percent of Life insurance sales in 2010, are not a good indicator of future performance, following the banning of insurers' staff and agents from bank branches. Accounting changes that will encourage insurers to focus on regular premium contracts also pose a challenge to the previous Bancassurance business model.

Consumer protection: Extensive requirements have been introduced in recent years to protect bank customers purchasing insurance products:

- Branch Bancassurance agreements must have a term of at least one year and be signed at the head office level. Respective responsibilities must be clearly defined.
- A bank branch may not have agreements with more than three insurers.
- Staff selling insurance products must hold Insurance Agent Professional Qualification Certificates. Insurance staff are not allowed to operate out of bank branches.
- Investment-linked contracts (including variable annuities) may not be sold at deposit, and counters and the sales staff involved must have at least 12 months experience and 40 hours of special training.
- Insurers must separate the accounting for their Bancassurance business.
- The skill level of the bank staff involved should match product complexity.
- Unit-linked sales must be accompanied by a “know your customer exercise,” and the resultant analysis must be signed by the customer and the sales person.
- Contracts with a term of more than one year sold by banks must be accompanied by a “bring to attention letter” laying out relevant product risks and a signed document in the consumer's own handwriting confirming that they were appropriately informed.
- Insurers are required to follow up within the cooling off period to ensure that the contract is acceptable.
- Commission caps apply in practice.

A complaints function exists within the insurance association, and consumers can file complaints with a supervisor.

Malaysia

Regulation: Bancassurance is actively supported in Malaysia because it is seen to lead to a more efficient financial system. Banks may own insurers but insurers may not own banks. Bank staff who sell insurance products are required to satisfy the same minimum qualification and continuous professional development requirements as insurance agents, and to comply with the same code of ethics.

Segment overview: All Bancassurance models have been employed in Malaysia, but the major operators tend to follow a group-based integrated approach. At least one insurer is devoted purely to Bancassurance through an associated bank. Credit-related products have accounted for most growth with short-term endowments and investment-linked products accounting for much of the balance.

Consumer protection: Extensive rules were introduced in 2004 to protect Bancassurance consumers:

- Commissions must be spread over at least 10 years for regular premium savings contracts. In addition the present value of the commissions is capped.
- Savings available from the Bancassurance distribution system must be shared with policyholders.
- Commission and policy charges have to be disclosed in sales material and at the point of sale.
- A data protection law has been in place since 2010.

Good practice market conduct rules are also in place for the insurance sector, including the following:

- Full disclosure of an intermediary's status and authority
- A requirement that needs analyses are carried out and
- The recording in writing of advice given and the reasons why in the case of Life insurance sales.

Insurers are required regularly to submit lists of complaints received. An integrated dispute resolution center called the Financial Mediation Bureau has been established. However, the insurance supervisor also has a unit established to receive complaints and inquiries.

Thailand

Regulation: Most banks have direct or indirect links with insurers, sometimes through family group holdings. Banks are defined as corporate brokers by the supervisor but, unlike independent brokers, are not required to make security deposits. Insurance agents and brokers are required to be licensed. Banks are theoretically allowed to market insurance only to existing customers, and the rules specify that there may be only one licensed individual per bank branch.

Segment overview: Bancassurance accounted for 53 percent of Life insurance new business in 2010. All Bancassurance models operate in Thailand, and referrals (that is, the prototype approach) have been common until relatively recently. Banks typically have agreements with more than one Life insurer. New business is largely lending

related, comprising term Life and simple savings products. To overcome restrictions on branch sales, banks are marketing insurance to noncustomers through their credit card divisions. Non-Life sales are focused on A&H insurance.

Consumer protection: There is no specific Bancassurance consumer protection law. The insurance supervisor accepts complaints and can mediate. A Life insurance policyholder protection fund exists.

South Asia

India

Regulation: No limitations are in place on the Bancassurance model that may be employed. Banks are classified as corporate agents if they sell insurance. However, if a bank wishes to set up an insurance subsidiary, it must have a net worth of at least Re 5 billion (approximately \$110 million) and a three-year track record of positive profitability. Ineligible banks may invest up to 10 percent of their net worth or Re 500 million (whichever is the lesser) in an insurer. Bancassurers are required to have a senior manager responsible for insurance activities, and staff who sell insurance are required to meet the individual agent-training requirements specified by the supervisor. Banks may not operate as brokers.

Insurance agents may operate out of a bank branch, but banks may have only an agency with one Life insurer and one non-Life insurer.⁵ This rule is under review, with the likely outcome being that a zonal system (essentially differentiating between rural⁶ and urban customers; see box 2.1) will be established.

Box 2.1 Draft Rules Regarding Bank Insurer Agency Agreements in India

–The IRDA's exposure guidelines on Bancassurance have said that banks cannot tie up with more than one Life, one non-Life and one stand-alone health insurance company in any of the States.

–Further, provided that in case the agreement of general insurer/s does not have any health product to distribute, the Bancassurance agent may tie up with one more general insurance company carrying on exclusive business of health insurance.

–The regulator has also said that insurers other than the specialised insurer cannot tie up with any Bancassurance agent in more than nine States or Union Territories in Zone A and six States/Union Territories in Zone B.”

Source: Business Line, November 23, 2011.

Under the referral model, customers must be given a choice of insurers. Where insurance representatives are present in bank branches, formal agreements must exist between the bank and insurer concerned and initially cannot be for more than three years.

Segment overview: Banks accounted for more than 8 percent of total Life insurance new business in in the 2008–2009 financial year, and considerably more for some private insurers. This figure is likely to increase rapidly as the traditional agency model comes under cost and profitability pressures for insurers other than LIC. LIC is also increasingly employing bank agencies. The most common model employed involves a joint venture between a bank and another entity (typically involving a global insurer and a local promoter or another bank). A foreign insurer may hold more than 26 percent in an Indian bank with which it has a Bancassurance agreement and at least one does. The two largest Bancassurers effectively have an integrated structure. A constraint to date has been poor point-of-sale information systems. Considerable unrealized potential exists.

Consumer protection: Insurance agents in India are subject to a Code of Conduct that is officially recognized, and noncompliance can lead to revocation of license. Banks are responsible for the behavior of insurers' representatives operating out of their branches. The supervisor has a capacity to receive complaints, and 13 independent insurance ombudsmen operate across the country.

EU Accession Countries

Hungary

Regulation: No limitations are in place on Bancassurance models, point-of-sales approaches, or products that may be sold through banks.

Segment overview: All Bancassurance models can be found in Hungary, with most leading insurers having ties to banks. As a possible indicator of the impact of new capital rules, at least one move has occurred from an integrated model to partnership. However, in this case (where a leading French insurer took over a Hungarian bank subsidiary) a 20-year agreement has been signed. Various forms of joint venture are also in place, including a “supermarket” arrangement involving a Life and non-Life insurance couplet providing products to numerous banks. A significant proportion of Bancassurance sales arise from related mortgage lending.

Consumer protection: No specific Bancassurance consumer protection rules are in place. Hungary has adopted the EU Mediation Directive (which is currently under review).⁷ The supervisor can accept consumer complaints but has no powers to enforce settlement. The supervisor issued guidelines in 2007 with a view to increasing

commission transparency and is monitoring the effectiveness of these guidelines. A private organization (the Association of Insured People) provides advice to complainants.

Poland

Regulation: No limitation is in place on Bancassurance models, point-of-sale approaches, or products that may be sold through banks.

Segment overview: Partnership and joint venture are the two most common models adopted in Poland, with a large French bank associated insurer taking a leading role. Banks often write individual Bancassurance business on a group basis with the bank forming the group. Sales were driven until recently by attaching insurance wrappers to short-term investment linked contracts, thus providing a tax advantage to the policyholder.

Consumer protection: No specific Bancassurance consumer protection rules are in place. Poland has adopted the EU Mediation Directive and an Insurance Ombudsman's Office has been established. In 2010 the Polish Banking Association published a list of Bancassurance good practices following allegations of credit card-related misselling. The bank supervisor is monitoring the effectiveness of these and is likely to introduce mandatory rules if the good practice guidelines are deemed inadequate.

Policy Issues in Emerging Markets

Numerous issues specific to Bancassurance have been identified in the country overviews. Most relate to the *design of the consumer protection regime* as it applies to Bancassurance.⁸ The treatment of capital in Bancassurance arrangements is beyond the scope of this policy note.

We examine the design of the consumer protection regime under the following headings:

- Transition
- Disclosure
- Linked selling and packaging
- Wealth management and investment products
- Licensing, training, and remuneration of point-of-sale staff
- Privacy of client records.

Transition

Where an effective insurance agency and/or broking sector has already been built up, strong pressures can be placed on governments to slow or even ban Bancassurance activities. Examples of this can be found in Canada and Morocco⁹ (table 2.5), where banks are limited in the range of products they may sell directly. Another example is in Kuwait, where Bancassurance is effectively banned.

Table 2.5 Canadian Bancassurance Constraints

Activity	Authorized Types of Insurance	Other Types of Insurance
Sales	Can be sold in bank branches.	Can be sold through insurance subsidiaries of banks, but not bank branches.
Advice/Referrals	Can provide advice on an authorized type of insurance or a service in respect to an authorized type of insurance.	Can provide advice that is general in nature and not related to a specific risk, insurance policy or service, or insurance company agent or broker. Cannot refer customers to particular insurance companies, agents, or brokers.
Promotion	Can promote policies of authorized types of insurance as well as companies, agents, and brokers that deal only in authorized types of insurance.	Can promote these types of insurance to all customers or credit charge card holders who receive regularly mailed statements of account or to the general public, outside of bank branches. Cannot target "target market" customers, that is, cannot segment the customer base and promote specific types of insurance to elected customers. The same restrictions apply to bank promotions of companies, agents, and brokers that sell these types of insurance.

Source: Starky 2006.

In Korea, Bancassurance was phased in, against the strenuous objections of more traditional insurance intermediaries (box 2.2). In the United States, banks were allowed to sell insurance products only relatively recently. They still face strong

opposition in this regard from consumer groups. On the other hand, certain countries such as Malaysia have recognized the potential for Bancassurance to provide a lower cost source of household risk management products and are actively supporting its development.

Box 2.2 Transition in Korea

Following the 1997/99 East Asian financial crisis, the Korean government introduced numerous reforms designed to increase the efficiency of the financial sector. Some of these, including allowing banks to sell insurance, were bitterly opposed by sections of the insurance industry. Thus although Bancassurance was introduced on a restricted basis in 2003, its full implementation was soon extended from 2007 until 2008, and then deferred indefinitely. The main concern related to the large number of agents (mainly housewives and widows with limited levels of professionalism at the time Bancassurance was first permitted) selling protection products. A more professional sales force is being developed but is still less than 25 percent of the total agency force. Only Credit Life and pure savings/retirement and investment contracts were available through banks until 2005, at which time accident, critical illness, and long-term care were added. Virtually all Life insurers now have Bancassurance agreements, and by 2010 Bancassurance accounted for 66 percent of aggregate Life insurance new business.

At date of writing, banks are not allowed to have exclusive arrangements with insurers, and large banks must have arrangements with at least three insurers, none of which can write more than 50 percent of the bank's insurance business. Every participating bank branch is limited to one bank staff selling non-Life insurance and one selling Life insurance, and the bank and insurance products must be sold and serviced at separate counters.

Rules established purely to protect politically connected intermediaries are not justifiable. However, agents and brokers can play legitimate roles if they are properly trained, are not overly influenced by commission structures, and can operate where other distribution systems are not appropriate or available. For example, bank branching is often inadequate in rural areas of developing and emerging markets. Here agents can fill an important access role, particularly if mandatory insurances are required: In Morocco, rural agents are allowed to earn a higher commission on mandatory Motor insurance, and in India a special category of microinsurance agent has been recognized. Best practice would ensure that the product range being sold is suited to the point-of-sale process and the consumer's needs and level of sophistication. Thus one practical approach would be to limit the product range in rural areas (where agency development may be desirable and where a less sophisticated population lives) but allow a more comprehensive Bancassurance product range in urban branches. This would still have to be accompanied by

appropriate training and licensing of agents and brokers under more general consumer protection requirements.

Best practice example: Korea.

Disclosure

A situation that has led to strong regulatory reactions in some countries involves the sale of insurance products when the consumer has believed that he or she was purchasing a bank product. Typically the consumer has not been informed of the early duration surrender penalties that apply (which in turn mainly cover sales costs and commission). In two large countries, family members influential individuals were allegedly the recipients of missold products, leading to strong regulatory responses. In at least one country, the bank supervisor has prevented any new Bancassurance arrangements from being entered into with nonbank-controlled insurers following complaints related to misselling by nonbank staff not certified to sell insurance. The banking and insurance supervisors and the insurance industry association are now attempting to develop an acceptable set of rules.

At the very least the following should apply:

- The consumer is made aware of the key features of the product, including
 - a. The fact that it is an insurance product
 - b. Any lock-ins or early termination penalties and
 - c. The name of the insurer involved.Ideally the consumer will acknowledge this in writing.
- The consumer is made aware of whether the sales person is an employee or representative of the bank, or a representative of the insurer. Again, ideally the consumer will acknowledge this in writing.

Under the Gramm-Leach-Bliley Act (1999), which enabled banks to sell insurance in the United States, the following disclosures are required of the Bancassurer in its promotional material and at the point of sale:

- That the insurance product (including annuities) is not insured by the Federal Deposit Insurance Corporation (FDIC), or the bank, or any of its related companies and
- That the insurance product is not equivalent to a deposit and may be subject to investment risk.

Nondisclosure by U.S. banks can lead to class actions legal procedures. In addition the Consumer Financial Protection Bureau has put pressure on banks to modify

disclosure so as to better explain value for the customer's money under credit-related insurance.

Best practice example: United States.

Tied Selling and Packaging

Where the bank does not control the insurer (or vice versa), and linked selling of a product is taking place, a traditional agency system is effectively in place. The core issue is whether disclosure provides sufficient protection. In these situations the bank has an incentive to maximize commission because it has limited interest in the fortunes of the “~~manufacturing~~” insurer (particularly where systems are not integrated and a long-term partnership has not been arranged). Commonly the customer may feel pressured into accepting the proffered insurance contract at the time of executing the borrowing contract.

In such situations (that is, where the bank is purely an agent, broker, or referral source), cooling off periods—during which the consumer may cancel the insurance contract and purchase acceptable insurance from another insurer without having to forfeit the bank product—could apply to even relatively simple contracts. An alternative is to require that bank should provide more than one insurer's credit-related insurance products at the loan counter or to allow switching to another insurer after a defined period.

Where the bank has a significant equity relationship with the insurer and systems are integrated, a more complex dynamic applies. This business model accounts for much of the opposition to Bancassurance from consumer groups and traditional intermediaries, who have noted the large profit margins available in some countries from tied Credit Life products. The following discussion supplies a suitable remedy, which is also strongly to be recommended in more general contexts.

An obvious possible option for consideration as a legal requirement would be to *ban the bundling of products*. This is increasingly adopted, for example, in Canada, France, and Poland and has an effect when the sale of a credit product is contingent on the purchase of insurance. This issue was discussed in chapter 1, where we saw that this would not be the only solution available. For this approach to be effective, full disclosure of the right to seek alternative quotes would need to be provided at the time of the primary sale, coercive selling would need to be defined, and significant sanctions for noncompliance would need to apply. An intermediate approach is desirable, because an integrated approach potentially offers the opportunity for consumers to avail themselves of efficient loan or insurance packages, and the outright banning of tied selling could reduce sectoral performance.

Best practice example—France.

Wealth Management and Investment Products

Bancassurers in a number of emerging markets are beginning to segment their customer bases into mid-market, high income, and affluent. For the latter groups, these banks are beginning to offer financial advisory and wealth management services through separate distribution arms, supported by higher margin insurance products.

As noted above, in some advanced markets (Australia is possibly the paradigmatic example) the traditional agency system has already contracted significantly and has been largely replaced by a combination of

- Direct and retail sales (for commodity products such as mandatory Motor insurance)
- Bancassurance (for simple savings, investment, and protection products) and
- Certified financial advisors for more complex needs.¹⁰

A simplified regulatory approach to this segmentation has been achieved in many developing markets by limiting the products that may be sold through bank branches, although the protection of entrenched agency systems has also been a factor. China has moved one further step by requiring that the point-of-sale location and process be appropriate to product complexity.

A more challenging issue is the sale of short-term investment-linked contracts with insurance wrappers when stock market returns appear to be superior to returns on deposits. Here the main issue is proper disclosure of the nature of the product and the potential for losses. Full disclosure of expense loading and redemption conditions is also desirable, as are prohibitions on the use of such words as deposit. As noted elsewhere in this paper, some countries require that investment products be sold at a counter separate from the deposit counter by suitably qualified staff.

Best practice example—China.

Licensing, Training, and Remuneration of Point-of-Sale Staff

The nature, training, and certification of the staff who may be selling insurance in bank branches varies widely between countries. In some countries no requirements are in place. In other countries the insurance salesperson may need to be employed by a broker (which may or may not belong to the bank) or be a trained and certified bank employee. The most efficient (that is, integrated) Bancassurance models tend to follow the last of these approaches, with the employee being salaried with modest incentives. As noted above, the level of training of the salesperson and the location of

the transaction should be appropriate to the complexity of the customer's needs and the sophistication of the products involved.

For partnership and referral arrangements, the traditional Life insurance agency model (that is, based upon high commission, high turnover, and low persistency) would not be welcomed by most banks, who will be concerned about their reputation and customer retention. Thus ideally bank staff will again be employed where relatively familiar savings products are involved. These could possibly be trained by resident staff of the insurer (or trainers trained by such individuals). For unfamiliar pure protection products (other than whole of Life), staff employed by the insurer or by the intermediating broker may have a more legitimate role within a bank branch. Ideally all individuals selling insurance products should have verifiable relevant levels of training and be registered in some manner.

Best practice example—Malaysia.

Privacy of Client Records

Data protection is now a key consumer protection issue around the world (figure 2.3).

Figure 2.3

Source: Munir 2010.

Note: China and Indonesia have been working on data protection laws. Korea passed its law in March 2011. The U.S. Privacy Act applies only to public databases. Other relevant U.S. laws tend to be subject specific.

In some countries (such as France) strict prohibitions are in place on the transfer of bank client data to insurers.¹¹ In other countries, opt-in or opt-out requirements are common.

Key required elements of any data protection regime allowing for data transfer are as follows:

- The consumer is made aware that data are being collected
- The consumer has access to his or her data
- The consumer can correct any errors and
- The consumer has the option of preventing that data from being shared with third parties (the definition of third party may or may not include related group companies).

A recent case review in Hong Kong SAR, China, concluded that where the right to transfer data is not specified in detail in the acknowledgment form, the relevant clauses in supporting material should be listed in the acknowledgement form (Office of the Privacy Commissioner 2011).

Best practice example—Hong Kong SAR, China.

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Chapter Three

Study in a Developed Market—France²

Origins and Development

Bancassurance is originally a French term. Its universal use reflects the fact that this business model is most developed in France. Although the natural synergies between bank marketing mixes¹² and Life insurance products have been recognized at least since the 1960s, the initial growth spurt had to await the mid-1980s when a change in the French banking law¹³ enabled the concept to reach its full potential (table 3.1 and figure 3.1). The French data provide some indication of the ultimate potential in a developed market.¹⁴ Bancassurance has attained higher relative penetration in less developed markets such as Portugal.

Table 3.1 French Life Premium Income through Bancassurance Channel
percent

	1990	1995	2000	2005	2009
Bancassurance	39	56	61	62	60

Source: FFSA.

Figure 3.1 Bancassurance Penetration within Banks

Source: Milliman.

The Life insurance product range initially focused largely on short- to medium-term savings products and risk products linked to lending, with the mid-market as its main target. Life insurer liabilities now account for the largest share of household financial assets in France (figure 3.2).

² The authors would like to thank to Wolff Didier for his contribution.

However, as this product strategy has achieved saturation, Bancassurers have expanded into new products less connected with their core activities. Initially this has been into Motor, but later it has extended to Health insurance. Then they have begun to offer products and services aimed at the more affluent of their customers—principally investment-linked and flexible Life contracts.

Figure 3.2 Allocation of Household Assets in France

Patrimoine total des ménages
10 800 Mds €

Loose translation:

Total household assets €10.8 trillion

Actifs non financiers = Nonfinancial assets

Liquidités = Cash

Epargne contractuelle = Contractual savings

Titres = Securities

Assurances = Insurance

Source: FFSA.

France more than most countries took full advantage of the introduction of universal banking. Integrated bank/insurance groups now account for the largest share of Life insurance premium income (table 3.2).

Table 3.2 French Market Leaders: Life Insurance, Based on Premium Income

Insurer	Overall Market Share 2010 (%)	Share Direct Business (%)	Equity-Linked Bank in France	Nature of Model
CNP	18.2	16.7	BPCE, La Banque Postale	JV/Partnership
Predica	14.8	14.6	Group Credit Agricole	Integrated
AXA	10.7	7.3		Partnership
Natio Vie, CARDIF, Natio Insurance	8.6	8.7	BNP Paribas	Integrated / partnership
Generali France	8.0	7.2		Partnership
SOGECAP	7.4	6.6	Societe Generale	Integrated
Groupama–Gan Vie	6.0	3.3	Groupama Banque	Partnership/ integrated
Allianz France	5.6	4.3		Partnership
ACM	4.7	7.4	Credit Mutuel	Integrated/ partnership

Source: AXCO, FFSA.

Factors Supporting Bancassurance in France

The success of Bancassurance in France may have been due to the fact that, aside from the liberalization of the banks' scope of operations, various other factors have supported the Life Bancassurance model in France:

- The French taxation system encourages savings. In particular, Life insurance products held for a minimum period are exempted from tax on the proceeds. This benefit has been diluted in the last decade, but it continues to drive sales.
- Banks were able to distribute insurance products at marginal cost because their fixed overheads were covered by their large established deposit taking and lending businesses.
- Bank and Life insurer groups have effectively been able to extend the term of their liabilities through the creation of longer-term contracts.
- Banks have been able to retain distribution income in-house and generate asset management fees.
- The relatively weak Solvency I requirements have facilitated a degree of regulatory arbitrage, although this benefit has been diluted through the Financial Conglomerates Directive.

Banks have been the main providers of investment advice in France. The Anglo certified financial advisor model remains underdeveloped.

Two of the insurers listed in table 3.2, while associated with banks, have partnership strategies and actively develop relationships with other financial institutions and adviser channels. These strategies reflect their origins, with Cardif working with non-BNPP banks and CNP operating through a formerly state-owned financial advisor network as well as its two quasi-public bank shareholders. Both Cardif and CNP have foreign operations, again working through partnerships, with Cardif actively following an international strategy.

Some of the challenges arising from elements of the insurance value chain that are not found in banking have been successfully addressed in France:

- Life risk underwriting has been partly dealt with by taking a group underwriting approach to products sold with lending products.
- Expert systems using socioeconomic and other nonintrusive indicators have also been developed.
- In more extreme cases, if an application for insurance has been declined by insurers after two medical examinations, it can be submitted to one of two reinsurance pools established to accept nonstandard risks. The original pool covers HIV-positive borrowers, and another more recent pool includes placements from insurers and reinsurers that are members of the two French insurance associations.

Non-Life Insurance Has Proved Less Effective

The Bancassurance business model has proved to be less suited to non-Life insurance in France, with most gains having been made in the 1990s, when general agents gave up approximately 10 percent of market share to the banks (table 3.3).

Table 3.3 French Non-Life Distribution

percent

	General Agents	Brokers	Salaried	Mutuals—Direct	Bancassurance	Direct—Internet and others
2000	35	17	3	34	8	3
2010	34	18	2	33	11	2

Source: AXCO.

Credit Agricole and ACM account for more than 60 percent of non-Life Bancassurance, with household insurance being the most successful product. The postal service began to distribute retail insurances through its local offices in 2011

(with Groupama as its joint venture partner in a new insurer called La Banque Postal Insurance) and is expected to gain significant market share in the Motor and Household insurance sectors. More than 200,000 non-Life policies had been sold at the time of writing.

The French Bancassurers have also been able to innovate where non-Life value chain processes can potentially inhibit bank sales and service. In this case the main concern has historically been the denial of non-Life claims and subsequent impacts on other business the customer has with the bank. The solution adopted has been to establish a common claims-processing center, which is seen to be independent of the distributor banks.

Emerging Challenges

The main challenges facing the French Bancassurance sector arise from new capital requirements under Basel III and Solvency II, from a more demanding consumer protection regime, from the development of Internet-based marketing for commodity products, and from the development of certified financial advisors for more complex needs (that is, the U.K. model). A risk may also be imminent of a secular shift regarding attitudes to trusting the banking sector.

Capital Issues

The capital challenge is made up of several elements:

- Numerous insurers are likely to have to significantly increase their solvency levels if they are offering strong guarantees for Life products.
- The cost of implementing Solvency II is likely to be high, particularly in terms of systems requirements and governance structures.
- Basel III will affect the capital requirements for universal banks and bank holding companies (figure 3.3).

Figure 3.3 Impact of Basel III

Regulatory proposals will decrease attractiveness of investments in insurance companies ...	
Basel III	Description
Capital deductions (Basel III)	<ul style="list-style-type: none"> Equity discounts for non-consolidated equity investments to be fully deducted from core tier 1 (vs. 50% tier 1 and 50% tier 2 in Basel II)
Exposure limited	<ul style="list-style-type: none"> Insurance investments will be limited for holding companies Excess investments will increase holding capital requirements (50% tier 1 and 50% tier 2)
Solvency II – Increased capital requirements	<ul style="list-style-type: none"> More volatile capital with dynamic market-based approach More differentiated requirements, affecting specially traditional life and “long tail” P&C¹ business² Strong penalties for investments in equity and corporate bonds (45% and 3% respectively)

Source: Banco Espirito Santo.

Likely responses will see some banks with integrated models reverting to joint ventures with insurers to raise capital, or sharing insurers with other banks to reduce their holdings, and others becoming pure distributors. The larger fully integrated groups may focus on products that require less capital and source capital-intensive products from nongroup insurers.

Privacy and Data Protection

France has always had strong privacy laws, and this has closed off the opportunity for insurers to gain access to bank customer records. Thus insurance sales have been generated from the sale of associated bank products and otherwise from the relatively frequent number of interactions between bank staff and customers in France. More recently the EU Mediation Directive and various domestic initiatives and consumer association concerns have imposed further requirements on Bancassurers.

Requirements include the following:

- Bank staff involved in insurance sales must disclose their financial and contractual ties to supplier insurers.
- They must explain in writing the justification for recommending a specific insurance product.
- From January 2011 the intermediary must be able to prove that purchasers of unit-linked contracts understood the inherent risks.

- Consumers of personal and mortgage loans have had a free choice of Credit Life insurer since 2010 following a large number of complaints about linked selling.
- Insurers and distributors must jointly clear promotional material and ensure that it is consistent with the relevant product.

These are all desirable reforms but will increase the costs and frictions inherent in the Bancassurance model.

Internet-Based Distribution

Direct Internet marketing is still a small channel for insurance products in the heavily banked southern European countries, but it has shown its potential elsewhere. This is particularly true in the United Kingdom, where the average Motor policy is purchased only after four competitive quotes have been obtained online, and where a vigorously competitive market exists between providers of online search engines to offer as many as 30 competitive quotes in a matter of a very few minutes. An online comparison Website in France called LeLynx.fr began operations in January 2010. The response of the Bancassurers is likely to be to develop their own direct marketing capacity (within the constraints of the relevant EU directives). Groupama, for example, has set up a specialist subsidiary for this purpose called Amaguiz, which offers an innovative Motor insurance product.

Moving to Distribution of Investment Products

Some Bancassurers are also developing specialist high-level advisory capacities. At this stage these efforts are in their infancy, and it is not possible to discern how effective they will be in the medium term.

Potential Secular Movement

The final potential challenge that should be considered here is the reality that, when one contrasts the success story in France with the relative failure of Bancassurance in some other developed economies, concern must be expressed regarding the risk of a secular movement in consumer attitudes. German insurance agents, with their long-standing status in small communities as respected advisers, face a similar secular challenge. If a pattern emerges in France whereby the broad consumer trust in banks shifts into a culture that is more determined to probe and check the value for the customer's money in any given proposal, then other more efficient routes to these products may well be found.

Summary

There is no doubt that the high level of community-oriented culture in France has made individuals particularly comfortable to accept products distributed through banks. This perhaps more than anything else explains the success of Bancassurance in France. However, many reasons may be given to regard the French success as something that can readily be replicated. These include the willingness of the banks to invest in training, the sympathetic tax regime, and the reality for banks that service-based income streams have an independence from their core systemic weaknesses. Banks can only see those independent income streams as desirable.

The challenges ahead for Bancassurance in France certainly include a range of capital issues, the possible backlash of increased privacy and data protection concerns, the advent of increasing consumer comfort with Internet-based sales processes, and the possible secular shift to consumers asking much more forceful questions about whether they want to buy so much through their bank.

These challenges nevertheless cannot prevent the observer from concluding that Bancassurance in France has been an outstanding success and looks set to continue to be so.

Chapter Four³

Study in a Developing Market: Mexico

Introduction

The Bancassurance model generally adopted in Mexico is based on the relationships established between a bank and an insurance company. Insurers that belong to financial groups take advantage of that relationship by distributing insurance products through bank branches. However, some insurance companies do not belong to financial groups, and they have been able to sell insurance products through the banking system as a result of specific commercial agreements.

The bank branches are the point of sale for simple insurance products that, mostly, are bundled within existing offers of banking products. The bank's sole responsibility is the distribution, and policy administration and risk management are the responsibility of the insurance partner.

In recent years, banks have played an increasing role in the commercialization of insurance products in Mexico. The main lines of business in which banks have participated are Life, P&C, and Motor insurance. In the case of Life insurance products, in addition to traditional insurance, Bancassurance has had an important participation in the sale of insurance products with saving components (flexible Life policies). Banks sell various types of P&C products, many of which are related to credits and mortgages.

In general, the largest insurance distribution channels in Mexico are agents and brokers. Nevertheless, Bancassurance activity has increased its relevance as a distribution channel for insurance products. Bancassurance is particularly active in the Life insurance market in terms of premiums and policies. In the case of P&C and A&H insurance, Bancassurance is notably strong in terms of policies issued; this suggests the importance of this distribution channel. In terms of premiums, Bancassurance holds the fourth position, but in terms of number of policies issued it holds the second position, with a 25 percent share.

Legal Framework

Insurance companies in Mexico are regulated by the General Law of Insurance Institutions and Mutual Insurance Societies (Ley General de Instituciones y Sociedades Mutualistas de Seguros, or Insurance Law). The Insurance Law foresees that sales formalized through insurance adhesion contracts can be carried out by legal entities other than insurance agents or brokers (for example, banks, automobile

³ The Authors would like to thank to Manuel Aguilera for his help and contribution.

dealers, and commercial entities). Therefore, banks are allowed to sell insurance products, provided they conduct the appropriate training programs for their employees according to the insurance products that the bank will sell.

Insurance companies that belong to financial groups are also subject to the Financial Groups Law (Ley para Regular las Agrupaciones Financieras). This law regulates the organization and operation of financial groups, and it establishes general consumer protection rules.

The Bancassurance Market in Mexico

The relationship between banks and insurance companies, among other operational, strategic, and technological synergies, enables insurers to take advantage of a massive distribution channel with benefits in terms of intermediation cost.

Financial Groups

In 2011 the Mexican insurance industry¹⁵ comprised 102 insurers, out of which 15 were integrated into a financial group. This set of insurers participated with 32.1 percent of the total premium of the insurance market, 9.9 percentage points higher than in 2005. The average premium growth of this group during the 2005–2011 period was 14.2 percent, 6.8 percentage points higher than the average premium growth of the total market. This growth suggests that, among other drivers, insurers belonging to financial groups have taken advantage of the bank distribution channel (table 4.1).

Table 4.1 Insurers That Are Part of Financial Groups: Market Share (Top 5)
percent

Insurer	Market Share	
	2005	2011
Seguros Inbursa	6.1	7.0
Seguros BBVA Bancomer	4.2	5.8
Seguros Banamex	2.4	4.5
Seguros Banorte Generali	3.0	3.7
Pensiones Banorte Generali	^a	3.0
Aseguradora Interacciones	1.2	^a

Source: CNSF.

a. This insurer was not part of the top five in that year.

Distribution of insurance products through the banking system has allowed insurance companies that belong to financial groups to reach new market segments and to offer standardized insurance products linked to banking products. Examples are Motor insurance linked to auto credits, and Life and P&C insurance sold in conjunction with

mortgages. Moreover, through the Bancassurance mechanism, insurers have also increased the distribution of insurance products with saving components. In 2005 insurers that belong to financial groups sold 31.9 percent of the premium of flexible insurance products; in 2011 their share reached 42.2 percent.

Almost half of the portfolio of insurers that belong to financial groups is concentrated in Life insurance; since 2005, this share has remained without significant change. The share of portfolios covering P&C insurance has increased from 17.3 percent to 26.1 percent, and that of Motor insurance decreased from 24 percent to 15.6 percent (table 4.2). Although Motor insurance decreased its market share, it had a 9.7 percent direct premium real annual growth in the 2005–2011 period. In the case of Life, A&H, and P&C insurance, real annual growth was 18.3 percent, 15 percent, and 26.2 percent, respectively. A significant part of this growth can be attributed to Bancassurance.

Table 4.2 Insurers That Are Part of Financial Groups: Market Share by Line of Business
percent

	2005	2011
Life insurance ^a	48.2	49.3
P&C insurance (without Motor)	17.3	26.1
Motor insurance	24.0	15.6
A&H insurance	10.5	9.0
Total	100	100

Source: CNSF.

a. Does not include Pension insurance derived from social security laws.

In 2005 flexible Life insurance products represented 8.4 percent of Life insurance sales in the Mexican market; in 2011 this type of insurance product reached 17.5 percent share of the market. The importance of flexible Life insurance products is shown by their growth during the last six years. Traditional Life insurance had an average real growth of 8.3 percent between 2005 and 2011; meanwhile the flexible Life insurance products' average real growth was 22.4 percent.

An important advantage of using bank branches as a distribution channel for insurance products is the lower acquisition cost. Between 2005 and 2011, insurers that belong to financial groups faced considerably lower brokerage commissions—almost four times lower than those faced by the total market (table 4.3).

Table 4.3 Intermediation Commissions
percent

Year	Financial Groups ^a	Total Market ^b
2005	3.3	7.6
2006	2.7	7.2
2007	2.6	7.0
2008	2.5	6.9
2009	1.8	6.2
2010	1.9	6.4
2011	1.6	6.3

Source: CNSF.

a. Intermediation commissions/direct premium.

b. Acquisition cost/direct premium.

In sum, insurance companies that belong to financial groups have achieved an important market share in the total insurance market in the last few years, with a considerable premium growth rate. The growth of insurers that belong to financial groups is explained in an important way by the synergies between the bank infrastructure and the insurance undertakings.

Bancassurance Participation in the Mexican Market

As mentioned above, in 2010, 15 insurance companies sold products through banks, seven of which belonged to financial groups. The other eight insurers did not belong to financial groups but sold insurance products through bank branches based on specific commercial agreements.

Total premiums sold through banks in 2010 represented 13.6 percent (\$1,826 million) of the in-force premiums of the Mexican insurance market. Most of the Bancassurance operations were concentrated in insurers that belonged to financial groups. The top five companies held 89.7 percent of the in-force premiums (figure 4.1).

Figure 4.1 Bancassurance In-Force Premium Market Share, Top Five Insurers, December 2010

Source: CNSF.

a. Includes insurance that does not belong to financial groups.

Bancassurance was highly concentrated in the Life insurance business (61 percent), followed by Motor insurance (27 percent). This participation was mainly achieved through contracts associated with property mortgages and Motor loans.

Insurance products sold through bank branches hold the fourth position in insurance intermediation, with respect to other distribution channels. In terms of both premium issued and policies in the total market, agents are the most important distribution channel, with market shares of 46.1 percent and 30.3 percent, respectively. Regarding premium, brokers intermediate more than banks; however, bank branches hold the second position, pointing to greater access to customers (table 4.4).

Table 4.4 Distribution Channels
percent

Business Line	In-Force Premium (2010)					
	Banks	Agents	Brokers	Direct Sales	Massive Sales	Others
Life	61.2	38.5	7.8	26.3	30.5	58.4
Motor	27.0	26.7	38.5	20.6	48.1	21.6
P&C without Motor	6.0	13.2	36.0	40.3	11.7	8.4
A&H	5.8	21.6	17.6	12.8	9.7	11.7
Total	100	100	100	100	100	100

Source: CNSF.

Bancassurance has played an important role in the development of the Life insurance market in Mexico. Sales through bank branches represented a quarter of the total premium of Life insurance and more than a third in terms of Life insurance policies.

In this line of business, although agents have the largest market share, Bancassurance intermediates more than brokers and other types of distribution channels.

In 2010 sales of Motor insurance through banks represented 12.6 percent of the total market, in terms of in-force premiums, similar to the participation in terms of policies (13.1 percent). P&C insurance (excluding Motor) is an interesting case, because a contrast is seen between the low participation of Bancassurance in terms of the premiums (3.9 percent) and the number of policies (26.1 percent) issued. Similar behavior is observed in the case of A&H insurance, where only 4.6 percent of the premium was sold through bank branches, but banks sold 34.2 percent of the total market policy count (figure 4.2).

Figure 4.2 Market Share by Line of Business, December 2010
percent

Total

Life Insurance

Motor

P&C (Excluding Motor)

A&H

Source: CNSF.

Summary

Bancassurance has increased its importance in the Mexican insurance market significantly. It has been used both by insurance companies that belong to financial groups and by other insurers. Both have taken advantage of the interface offered by the banking infrastructure to reach a large number of clients.

The large participation of Bancassurance in the insurance policies issued indicates an important potential for growth in most lines of business. Although traditional channels are still the main mechanism of insurance distribution, sales through bank branches are a market practice that represents a distribution channel with a high potential to increase market penetration, being able to reach population segments in Mexico that still remain with little or no access to insurance products.

Conclusion

The reader who has persevered thus far will surely be in little doubt as to the potential for Bancassurance to assist in the development of the use of insurance, both Life and non-Life. The wide range of examples will have shown how many different countries have come from different starting points and have encountered different challenges along the way. These merit detailed study. A wide range of regulatory challenges are faced as well, not least those relating to consumer protection. Further, it should not be assumed that Bancassurance is a “panacea” to solve all problems: Bancassurance itself has limitations, as some entrepreneurs have shown in the use of the telephone and the Internet as means to distribute insurance on a cost-efficient basis.

All these aspects, however, once studied, will leave the reader aware of the aspects that need careful consideration as well as, one hopes, enthusiastic to embrace this key channel as a dynamically potent force in the future well-being of all communities across the globe.

¹ White goods are major appliances such as refrigerators and stoves; brown goods are electronic products such as televisions and stereos.

² Smaller countries tend to have more active international trade.

³ This metric is typically between 40 and 60 for industrial countries.

⁴ This restriction was introduced by the banking supervisor who was concerned about the banking sector’s reputation. The main issue was nondisclosure of surrender penalties to customers who thought they were buying bank-style products.

⁵ Insurers in contrast usually have agencies with multiple banks.

⁶ At present rural bank branches typically provide promotional material and a telephone number rather than face-to-face sales and advice.

⁷ Particularly with respect to tied sales.

⁸ More general consumer protection issues are covered in other World Bank documents (Rutledge 2012).

⁹ In Canada only insurance closely related to credit may be sold through bank branches. However, banks may own insurers.

¹⁰ A trend is now being seen in advanced markets (such as northern Europe and Australia) toward banning commissions where financial advice is being provided.

¹¹ Medical record privacy applies in most countries.

¹² Marketing mix refers to the combination of product, promotion, distribution, price, and service approach adopted.

¹³ The new law opened the door to full universal banking, under the terms of the second EU Banking Directive.

¹⁴ Adoption of the model in Italy was somewhat later than in France.

¹⁵ In 2011 the direct premium issued by the Mexican insurance industry amounted to 274,163.3 million pesos (about \$20,000), which represented 9.8 percent real annual growth.