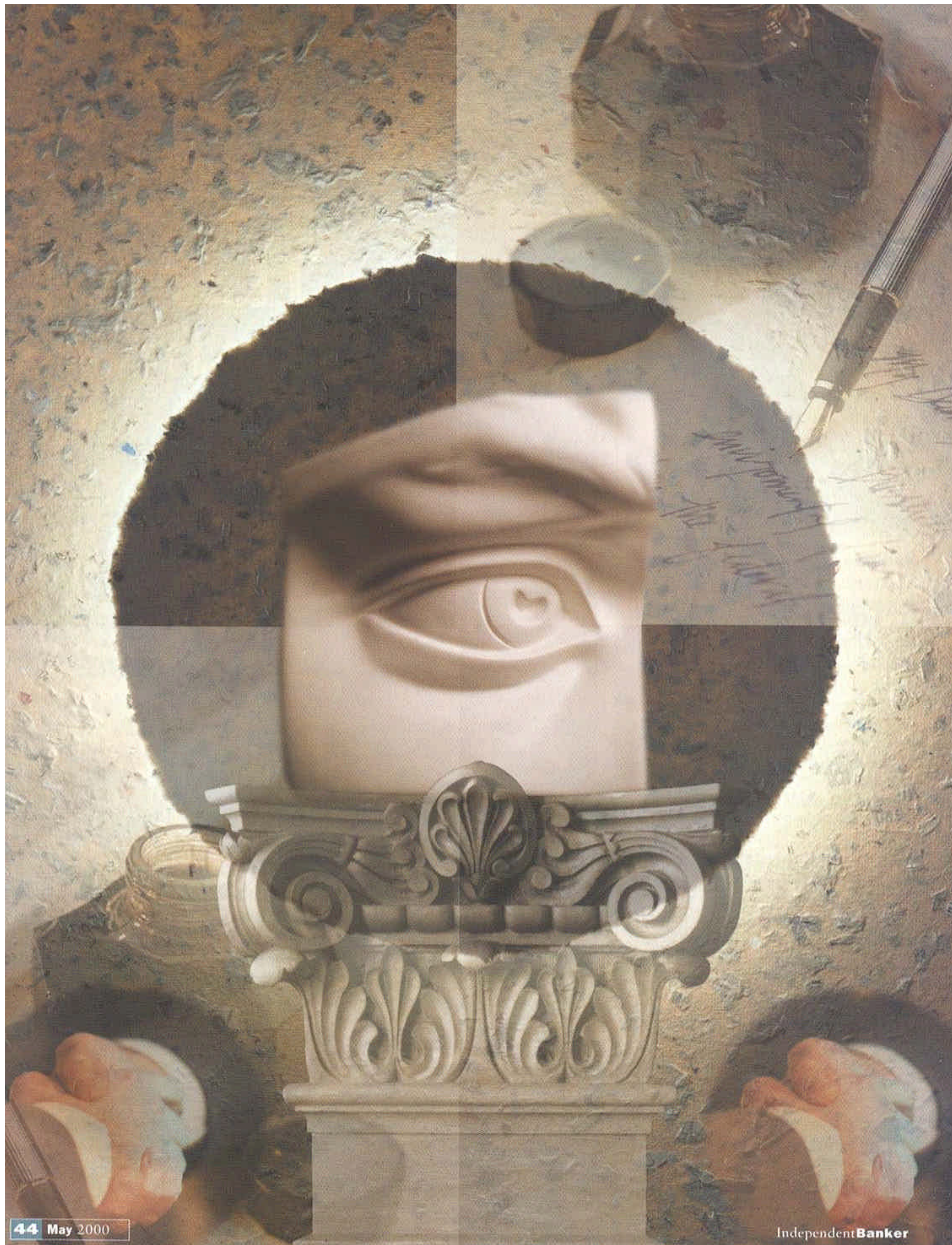

By Michael D. White

Wisdom of the Greeks

Thales, Greece's first philosopher was once asked to identify the most difficult thing a person can attempt to do. His response, "To know thyself."

But knowing oneself is an essential first step in understanding. Bankers entering the insurance marketplace needs to "know thyself."

To do this, they must understand everything from their bank's core banking businesses to their key consumer transactions to the average number of accounts customers possess. They must articulate financial and nonfinancial objectives, both for their bank and its incipient insurance program. And they must identify meaningful, actionable and profitable customer segments.

Know Thy Customer Bases

An insurance chief at a large bank recently said his bank had a particular mortgage portfolio with several tens of thousands of borrowers. It diligently tried to make money direct-marketing and remarketing homeowners insurance to his portfolio of customers. The bank's insurance efforts were intensive and non-stop.

But, after some time, he reanalyzed the portfolio's potential and wondered why his bank kept marketing homeowners insurance to this portfolio of borrowers that frequently shopped mortgage rates, refinanced with other lenders and had, at most, a 5-year duration. The bank's sales penetration was typical for direct-marketed insurance. Premiums were low and earned commissions did not even cover the bank agency's direct expenses, let alone indirect soft-dollar costs.

After what he called a long overdue analysis, this bank insurance executive dropped this program and turned to other insurance activities that produced significant profits.

Know Thy Points of Sale

One regional bank was among the largest institutions in its state. From the beginning, the bank's executives were most interested in selling auto insurance. After examining the data and asking questions, however, the bank discovered that only 500 of its 52,000 auto loans were made directly through the bank. The great majority of its auto loans were made indirectly through a third-party car dealer.

In preliminary efforts to know its bank, management had equated all auto loans with car insurance sales. But indirect auto loans are virtually useless to a bank's insurance activities. Indirect borrowers are not really a bank's customers; the bank is not at the point of sale where the transaction prompts discussion of insurance needs.

This bank did not understand how the insurance marketplace works. Nor did it realize that auto dealers have agencies that sell insurance.

Still, the bank wanted to sell auto insurance and believed that it could build a customer database as it received loan documentation from the auto dealers. The bank believed that, because the loan documentss contain useful information about borrowers' insurance policies and expiration dates, the bank could offer borrowers new auto policies when existing policies were about to expire.

BANKS WEIGHING INSURANCE SALES SHOULD "KNOW THYSELF" AND MORE

Know Thy Profit Potential

This is true in theory, but does a direct-marketing penetration rate of even one percent against a portfolio of 60,000 indirect borrowers – 600 auto policies – justify the considerable investment in database development, staff, and time needed to make these sales?

Assuming average policy-premiums and commission rates of $1,200 and 12 percent, respectively (and assuming the bank could obtain satisfactory carrier contracts with competitive prices), it would gross $86,400 in insurance revenues.

Can the bank afford to build this database, hire the requisite personnel, and launch such a marketing program based on this kind of return? No. The results are at odds with the 15 percent return on investment previously established as a key financial objective.

Additionally, if the bank were to solicit auto insurance from the indirect borrowers, it would anger the very dealers who lend the bank's money to car buyers. Anyway, the question is moot, since this bank's state – like many other states – has a new law that forbids the use of insurance-related information obtained through a

loan application for solicitation of insurance.

Know Thy Customer Profiles

In a banker's world, knowing oneself also means knowing one's customers. This means knowing the transactions customers execute, the kinds of bank accounts (assets) they have; the events in their lives triggering insurance needs; and their aspirations to be achieved or problems to be solved. It means knowing what insurance products are strategically right for a bank's customers.

One bank dug up data that indicated more than one-fourth of its customers – twice the percentage of state residents – were age 55 or older. Such a large segment of older banking customers meant a larger-than-normal group of candidates for estate preservation and retirement. It also meant more prospects for investment products such as long-term care insurance, annuities and joint-life-and-survivor life insurance.

Conversely, because the bank's customer base was disproportionately older, its younger customer base was shrinking. The bank immediately responded to this newfound knowledge with new banking products and marketing campaigns to appeal to a younger crowd, while focusing on older customers' specific insurance needs.

Know Others

The Greek comic playwright, Menander, had another take on the maxim "know thyself." In many situations, he advised, it is better to "Know others."

That's good advice for an increasing number of bankers who are receiving joint-venture proposals based on a prototype designed by a national agent trade association that has fought banks' authority to sell insurance.

Bankers should be aware – and beware – of pro forma projections made for insurance premium volumes, commissions and earnings for agency-bank joint ventures. Many of these projections are based on unrealistic assumptions about the average $250 million-asset bank.

Some assumptions require that this average community bank services 15,000 ing locations. Under some projections, this average bank annually issues more than 3,000 direct auto loans and possesses a portfolio of nearly 11,400 auto loans. This average bank also supposedly originates 1,250 new home loans per year, with an existing book of 6,250 mortgages. Such assumptions regarding these new and existing loans result in a number of loans 50 percent greater than the bank's customer base.

More exaggerated are projections of annual penetration rates for personal lines and life insurance sales. Some pro forma projections show annual penetration rates of 10 percent for this average $250 million-asset bank's retail customer base, meaning the bank must sell 1,500 personal lines and 1,500 life insurance policies each year.

What's wrong with these numbers? Grossly inflated, they constitute a sales program based on agent body count, not enhanced productivity.

Adding the Numbers

Consider what it takes to sell if a bank insurance program attains a 25 percent closing rate instead of the typical 10 percent by traditional agencies, its insurance sales force would have to book 6,000 appointments with qualified prospects to sell 1,500 life insurance policies per year. Six thousand appointments in one year represent 40 percent of this average bank's entire retail customer base!

Weekly, the sales force would need 120 appointments to close 30 sales, requiring on average, 24 appointments per day. Even if agents are inexhaustible, time is not. This bank needs at least four life insurance agents, and possibly as many as eight, to achieve those results.

Applying the same reasoning to the sale of personal lines of auto and homeowners insurance, the bank needs four to eight property-casualty agents. Already, there are between eight and 16 agents selling in the bank's seven locations. More agents are needed to sell other insurance products covered in the pro forma.

One might humorously surmise that, under this scenario, at any given time, branch than bank employees and customers combined.

And what would the bank earn from this pro forma's joint venture with its enormous cast of characters? Annual first-year life insurance premiums are projected at $1,125,000, for which the bank receives less than $25,000, the equivalent of 2.2 percent. Sales of personal lines produce $1.5 million of new premiums annually, for which the bank gets about $15,000, or 1 percent.

Why would any bank go for this kind of deal?

Such projections do not represent a sensible bank insurance strategy. If bankers understood that it took that many agents to produce fewer than $40,000 in bank earnings, bankers would rightly say, "Why bother?"

The truth is that many pro forma projections are unfair to bankers and agents alike. Their unrealistic expectations and inevitably disappointing results set up everyone for discouragement.

To sell insurance, bankers cannot be know-nothings. They must not only know themselves, they must also know their customer bases and natural points of sale.

They must calculate premiums and commissions based on closing and penetration ratios they can realistically achieve.

They should be able to compare and critique potential partners and their proposals.

They should also know enough to recognize when they would get skinned. When bankers do not understand something about insurance, an entirely new line of business, they should have the courage and good sense to say. "I do not know what you mean. Explain it again."

After all, sometimes part of knowing thyself is recognizing what another Greek, Socrates, said: "All I know is that I know nothing."

This article first appeared in
Independent Banker
May 2000, V.50 N.5, pp. 44-46
*"**Wisdom of the Greeks**"*
BankInsurance.Com — Internet Version
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