In this second issue of the Bancassurance Bulletin, we look at how some of the regulatory issues facing our industry are impacting the way banks approach and serve their customers, with some predicting a ‘market correction’ that sees a whole new approach to product design, pricing and distribution. While this is not unique to banking, it could be the opportunity for the industry to take the offensive as the ‘good guys’ in trying to shape the way customers fulfil their savings, protection and wealth ambitions.

We are delighted to introduce a new feature called ‘Hotshot in the hotspot’. Ian Martin from HSBC kindly agreed to be interviewed and highlights the issues and opportunities facing his business. We are seeking other volunteers for our next issue.

We have also included a perspective on the Polish bancassurance market, as it is starting to mirror some of the challenges that the UK has addressed in recent years.

Finally, we have included a snapshot of our latest Global Insurance Digital Study, Insurance in a digital age – the time is now. It certainly provides food for thought and poses the question where does your business position itself?

We do hope you enjoy this latest issue and as ever welcome the opportunity to discuss any article further.
Do banks have a social imperative to find a new financial advice model?
Fast-forward seven years since the Financial Services Agency (FSA) first launched its proposals for the Retail Distribution Review (RDR), and the provision of financial advice by banks to the mass market has almost totally disappeared. Since the implementation of the RDR there has been a series of high profile withdrawals from high street retail advice. Each announcement has formed a depressingly similar narrative: it is no longer economically viable to offer advice to the man on the street with modest amounts to invest – the lifeblood of the bancassurers. In short, if you're not wealthy, you're on your own.

Essentially, the market reached the point where banks gave more advice than customers either needed or wanted, which almost inevitably led to mis-selling and mis-buying, at least partially fuelled by over-zealous sales approaches. Interestingly, in the wake of the RDR, the market may have reached the point where customers in need of advice now need their bank more than banks need some of those customers. And this, we believe, could be the tipping point for a new model that works for both parties.

Some might argue that the conduct of banking advisers may have, at times, fallen short of the standards we would like to see in the industry. But, in our view, the unintended consequence of the RDR has been to throw the baby out with the bath water; you don't address a massive savings gap by starving the mass market of advice.

Banks have a central role to play in meeting the financial planning needs of the nation. For the majority of people in the UK, their sole regular interaction with financial services is via their bank. Most of them have relatively basic planning needs – they need to save more, and they need to ensure that they (and their family) are protected against catastrophe. However, without an intervention, a high percentage of these people will sleepwalk into an uncertain future. The challenge for banks is to find the people who know they should be saving more and to help them meet their needs. The initial customer research on pension auto-enrolment has shown two things: firstly, the opt-out rates so far are lower than anyone expected (<10%); and, secondly, the overwhelming feedback from consumers is relief; people knew they should be saving, but it had never reached the top of the list.

If banks can find these consumers, the second (and arguably bigger) challenge is to help them. The days when most customers formed an orderly queue at the branch counter on a weekly basis have long since passed. Many customers rarely, if ever, physically interact with the bank. And even if you can catch them in the branch, you can't give them advice. So what is the new model for bancassurance?

There is, of course, no ‘one size fits all’ solution. The correct approach will depend on the profile of customers, their life stage and their relationship with the institution. In our interview with Ian Martin on page 8, he talks about the need for ‘intelligent bancassurance’ – ensuring that you present relevant propositions to customers at the right time, through the right media. We agree. Through their unique and privileged relationship with their customers, banks must ensure that they are intelligently using customer data to ensure product marketing is useful.

But getting the data right is only half the story. For most mass market customers, we believe that online (non-advised) will be the right distribution channel. However, banks must ensure that they are offering engaging and compelling tools to help customers through the buying process. Much has been made of the potential for algorithms to provide a proxy for advice – clearly a nice idea. However, there is no substitute for simple, jargon-free, well-placed engagement throughout a buying process. We believe this is an area which no one has so far got right, although new propositions are emerging which are a vast improvement on their forebears.

Over the past 12 months, we have been starting to help clients through this journey. Our Enterprise Intelligence practice is helping banks and insurers to redefine their approach to data, whilst our Customer practice has unique insights around innovative use of digital tools within financial services. We believe the time has come for banks to be bolder about the social imperative to help their customers plan for the future.
Caveat vendor: the TCF (r)evolution
In its early days, the FCA made clear that it wants to be regarded as the ‘consumer champion’ – its mission statement, ‘to make markets work well so that consumers get a fair deal’, underlines that.

As consumers, we often behave illogically, ignoring facts and common sense in favour of glamour, status and whim. We’re often prepared to pay a premium for products and services that make us feel or look good. We observe this buying behaviour with items such as clothes, shoes, mobile phones and tablet computers.

Companies that can spot consumer trends and create demand for goods do well for their shareholders, as they deliver higher profits than competitors offering similar, and sometimes better, products that don’t have the same ‘magic’ appeal. That’s how markets work.

Contrastingly, the FCA has made it clear that it wants to up the ante to ensure that customers get value for money and are not exposed to products or services that are inappropriate, or deliver unsuitable outcomes. Indeed, in its first Annual Risk Outlook published earlier in 2013, the FCA identified five key risks, three of which focused on fair value and appropriate outcomes:

1. Firms do not design products and services that respond to real consumer needs or are in consumers’ long-term interests.
2. Distribution channels do not promote transparency for consumers on financial products and services.
3. Poor understanding of risk and return, combined with the search for yield or income, leads consumers to take on more risk than is appropriate.

At first glance, this does not bode well for shareholders in companies that manufacture financial products; it appears to imply obligations to customers that go well beyond treating customers fairly (TCF). It raises the following questions:

► Is there an undertone that manufacturers are making ‘excessive profits’?
► Is ‘fairer value’ sufficient, or is a cap on margin the decent thing to do?
► Does fair value still enable sufficient economic return to make market participation worthwhile?
► If there is sufficient margin, how do you create sufficient demand economically?
► Are there major implications for operating models, over and above the more obvious changes required to product development and governance processes?
► Could it be the catalyst for a whole new industry mindset towards customers and products?
Caveat vendor: the TCF (r)evolution

The diagram below sets out EY’s interpretation of the potential extent of the challenge facing the industry. Our sense is that the future is most likely to be on the right-hand side of the spectrum, which implies dramatic changes to industry economics and operating models.

The big questions
- What does value mean and where does it lie for your organisation?
- What is the optimal sourcing model?
- How do you charge?
- How do you capture customers and distribution?
- How will technology evolve and when will it become a hygiene factor?

Key performance indicators
- Clarity of: Proposition
- Customer comms
- Remuneration

Strategic implications
- Tactical ‘housekeeping’
- Relatively short term

Potential extent of the TCF (r)evolution

This marks a significant change in our market, which has always had caveat emptor (buyer beware) as one of its core principles. Increasingly, the market is one in which the principle of caveat vendor (seller beware) will apply.
Hotshot in the hot spot:
Ian Martin, CEO Insurance UK, HSBC
Hotshot in the hot spot: Ian Martin, CEO Insurance UK, HSBC

Ian Martin is CEO of Insurance for HSBC in the UK. He lives in Tunbridge Wells, Kent, and, when not in the boardroom, can be found playing premier league badminton, relaxing with his wife and two daughters or hitting the open road on his motorcycle en route to the Le Mans 24-hour race! He talked to us about his views of the bancassurance market.

A number of UK banks have recently announced changes to their bancassurance propositions, including many deciding to withdraw from giving advice. Do you still see the potential for growth in this space?

It’s important to remember that just because the regulator and the industry have changed, it doesn’t fundamentally change the underlying consumer need for advice. That need is still there, and the UK remains the third-largest wealth pool in the world.

I think the regulator has recognised that advice for consumers can be very problematic now. The economics of providing mass-market advice is just not viable for the customer or the provider. There is an absolute need to change business models to make sure that we can meet customer needs in a way that works for them, in terms of channel, and for the bank in terms of economics.

As the dust continues to settle on the RDR, how do you see the future of bancassurance developing?

There is likely to be only a handful of providers left in this space because you need the scale, the brand, the customers and the distribution – there just aren’t many firms that can put that together in a way that is compelling for customers. I think, for this reason, bancassurance has a bright future – due to the interaction between peoples’ day-to-day money management and the opportunity that banks have to present relevant propositions. The models of the future that I call ‘intelligent bancassurance’ represent a massive opportunity because we do already have a privileged relationship with customers.

Can HSBC learn lessons from elsewhere in the globe?

Our wealth management customers are a community of internationally minded people who are mobile in their careers and, whether it’s coffee or cars, the world is globalising around brands and experiences. Our customers should be able to experience HSBC in a consistent way across the globe.

Many of the changes we are making emanate from the UK – across the Group, we are applying the highest global standards around the value that the proposition offers to customers. We are also able, however, to bring to our UK-based customers the best ideas and practices from across the world. We believe our brand stands for certain values and it’s got to stand for those things everywhere we operate.

Do you believe that you have the customer mandate to be that trusted provider?

It’s a fair challenge. Across the board, the relationship of trust upon which banking is founded has been fractured – I think that we can only repair this day by day, by everyone doing the right thing, in the right way. There is no one special advertising campaign that offers a shortcut. We have to earn our customers’ trust hour by hour and that’s a journey that we have to make.

Is it a particular challenge for bancassurance?

There is a duty of care on us as banks, when we lend money, that we have an appropriate conversation about the protection that our customers need to have. For example, the impact on a family suffering following a catastrophe can have an impact on future generations. I believe bancassurance has a very important role and responsibility in overall society.

We have approaching 15m retail customers across HSBC/First Direct/M&S Bank and, therefore, a major opportunity to influence the financial outcomes of a significant proportion of the UK population. If we do it really well, people will be better prepared for retirement and they won’t find themselves in financial hardship if they suffer tragedy or serious misfortune in their lives. We have to rebuild that trusting relationship with UK consumers – it sounds a bit grandiose, but I truly believe it.
What role do you see for direct-to-consumer distribution?

Building much better tools, better direct distribution, better self-service and self-discovery for customers in simple ways is now required. Not all of our customers want to access our services face to face, so we have an obligation to improve our digital capabilities to meet their needs.

There are certain moments when customers would really benefit from financial advice. For example, when the retirement planning switch gets flicked or you want to start saving for your children’s education; when those moments come, people look to a brand they can trust.

Do you think it is important to have an ‘aspirational’ brand to be a successful bank in wealth management?

Our group CEO tells a story and brings to life a time when a company would be proud to put on their accounts that HSBC was their banker. We are in a challenging time for our industry, but we still aspire to the sentiment behind that; we want our corporate, commercial and retail customers to feel reassured that they deal with us.

Do you think the products of today are fit for the customer of the future?

The vast majority of the population’s needs can be met by some straightforward products bought direct, with no advice required and which ‘do exactly what they say on the tin’. For a period of time, the industry has sometimes thrived on complexity at the expense of customers. The RDR is a response to some of those issues.

It is only when you get to the sophisticated end of the market, where you have substantial wealth, complex tax issues and the opportunity to be more efficient with your wealth management, that you should have to pay for advice and the additional product opportunities that creates.

Income drawdown is a good example of where we believe advice is essential. The industry must not allow customers to agree to things, knowing that they won't understand what they are signing up for; we must clearly explain the risks involved.

Closing thoughts?

I believe that we have a special opportunity to make a real difference to the lives of our customers. I don’t underestimate how hard this all is though. There is significant investment required to make these strategic changes; it is not for the faint hearted, and you really do have to follow through. It’s clear our customers and the bank will benefit if we get it right.
Equity release: unlocking the potential
For decades, industry observers have suggested that the UK equity release market is poised to explode, but sales remain stubbornly languid. Can banks help the product break out of this malaise and into the mainstream?

A small number of banks have dabbled in the market, only to withdraw due to adverse publicity or the failure of equity release partners. The financial crisis and the subsequent damage to the reputation of financial firms have also created inertia in the market.

Intuitively, equity release would seem to fit well with banks’ broader propositions. During the ‘accumulation’ phase of their life, most people have entrusted their biggest life purchase — their property — with their building society or bank. It seems to make sense that, when the time comes to unlock some of this value, the bank should be the first port of call.

When the Housing Act of 1980 gave council house tenants the ‘right to buy’, Britain became pre-occupied with the notion of home ownership. Over the last 30 years, the significant shift towards Britain as a ‘nation of home-owners’ has continued to permeate the national consciousness.

Conversely, successive governments have struggled to implement effective pensions legislation. Employers have increasingly withdrawn final salary schemes, transferring risk and responsibility for retirement planning to their employees. Retirement saving in the UK has remained depressed – with the result that many retirees now find their pension income to be inadequate.

In 2011-12, some 18m pensioners’ disposable income was below 60% of median household income (£367 per week, after housing costs). This means 14% of all pensioners were in the Department for Work and Pensions’ (DWP) definition of relative poverty. Whilst auto-enrolment may help future generations (although the extent is debatable), for many the changes are too little, too late.

For many years, the insurance industry has seen equity release as one of the solutions which could help to address this problem. Behavioural data shows that, despite changes in their housing requirements (as dependants leave the home), people entering their retirement years are often unwilling to realise some of the value in their property by moving to cheaper accommodation. Equity release would seem to offer a viable solution to unlocking this value whilst allowing people to stay in their home.

The figures seem to support the view that there is latent and growing demand in this market:

► £750b: unmortgaged housing equity held by the over 65s
► £7,000: the average amount that people approaching pension age over-estimate their projected retirement income
► 5.3m: increase in the number of people aged 65 or over during the course of the next 20 years (+48%)

Nonetheless, growth in the equity release market has been sluggish. The initial equity release products, launched in the 1990s, were often expensive and gave the home owner insufficient protection. The spectre of eroding away all the equity and losing your home loomed large. There are also considerable buyer-side barriers to overcome; many people have seen their house predominantly as a legacy to be passed to their children and are nervous about allowing this to be depleted.

Modern equity release products have addressed many of the issues of the initial wave. All products which are recognised by the Equity Release Council offer consumers enhanced protection – meaning that they will never have to leave their home. The equity release code of conduct also enshrines a ‘no negative equity guarantee’, meaning that no debt will ever be left to the estate. Also, customers are able to move their plan to another suitable property, so that customers are not anchored to the property they live in at the point of purchase.

We believe that the market dynamics and quality of solutions have now shifted to the extent that banks should seriously evaluate (re)entering the market. It is clear that there is a real customer need, and we believe the market is currently artificially depressed by a lack of providers, capacity and public awareness. Banks have an opportunity to lead in this space and create solutions that can enhance the later lives of their customers.

We would welcome the opportunity to talk to any bank considering the market; we have worked closely with a number of existing providers and can help to provide insight and support from product development, including financial engineering, to launch.

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International perspective: will consumer activism help Polish bancassurance ‘leapfrog’ the UK?
The attractiveness of the Polish insurance market has not been lost on the 40 or so international insurers that have entered the market since liberalisation in the early 1990s. As the Polish economy has continued to develop faster than most other European Union states, the insurance market has delivered double-digit rates of growth virtually every year — the single exception being 2009, due to the financial crisis. With the rate of insurance penetration around a third that of the UK, Poland clearly offers scope for plenty more growth.

Bancassurance is a key channel for the distribution of life insurance — representing more than 50% of total life premium income (although less than 10% of the general insurance market). This level is much higher than the UK and places Poland firmly in the group of European ‘bancassurance-friendly’ countries such as France, Spain and Portugal. One of the biggest single drivers of growth for Polish bancassurance was the exemption of life insurance products from the 19% capital gains tax (CGT) that was introduced in 2004. Although the financial crisis put an end to the growth of these mainly single premium products, the vast majority of Polish bankers still see more potential for combining banking and insurance services.

The regulatory landscape in Poland is developing rapidly and demonstrates a strong gravitational pull towards Brussels. Poland is keen to be seen as a model European citizen, and the insurance regulators are actively participating in major European projects such as the Insurance Mediation Directive 2, Markets in Financial Instruments Directive 2, Packaged Retail Investment Products and Solvency II. Regulation has focused mainly on increasing the transparency of products and prices rather than intervening directly in their structure.

Confirming the global trend, consumer bodies in Poland are increasingly vocal. The Polish Insurance Champion has been active in raising complaints to the regulators around loan and credit card protection and, equally, has raised issues about the performance of investment products that have failed to deliver the returns expected when they were purchased. The EY Insurance Customer Survey, published in 2012, confirmed that consumers globally are increasingly willing to engage actively in the research, selection and purchase of insurance products, and Poland is clearly no exception. Polish bankers are taking careful note of these trends and are very keen to avoid the perils of mis-selling scandals and aggressive regulatory intervention.

Although Polish banks are coming under increased regulatory scrutiny, they have largely avoided the reputational damage caused by the financial crisis, and many demonstrate a highly commercial and entrepreneurial spirit. The combination of a pragmatic regulator and an active consumer base may help Polish bancassurers move directly to a future model where products are developed to meet true end-customer needs directly — avoiding the impending advice gap and regulatory fall-out experienced in the UK.

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Insurance in a digital world: the time is now
Our new survey, Insurance in a digital world: the time is now, shows that insurance is lagging behind other industries in the one key area that is transforming consumer behaviour and business models: digital technology. Insurers have been slow to adopt digital technology because this challenge requires a different set of skills and culture.

In light of this imperative, EY surveyed more than 100 industry players in three major geographic regions – Americas, Asia-Pacific and Europe – in the second quarter of 2013 to understand how the digital agenda is reshaping the sector and to what extent life and nonlife insurance companies are grasping and exploiting the shift to digital. To complement these insights, our report outlines examples of digital innovations and, based on our experience, suggests practical areas that insurers should prioritise now to tackle the challenges ahead.

Key findings

► Insurers acknowledge their current low levels of digital maturity and the need to take action. Almost 80% of respondents do not see themselves as digital leaders, trailing the spectrum in customer engagement, analytics and adoption of mobile and social media.

► Companies have high digital ambitions – but are they grounded in reality? Two-thirds of insurers have delivered some easy quick wins, but only 10% cite transformational changes to digital capabilities.

► Insurers are holding themselves back. Internal factors – legacy technology, slow pace of delivery and cultural constraints – are hindering digital progress.

► It’s all about retention through improved customer experience. The two biggest drivers of digital strategies are ‘enriching the customer experience’ and ‘regaining more direct control of the customer relationship.’

► Distributors and agents are digital customers, too. Insurers cite intermediary and agent channel strength or resistance as one of the top three inhibitors in implementing a digital strategy.

► Analytics are critical to digital success. Segmentation, customer data analytics and predictive modeling emerged as the digital skill set most in demand, followed closely by technology and marketing capabilities.

► Insurers need to embrace the mobile and social media wave. Disparities exist between online and mobile functionality; 86% of insurers say branding or online presence is the main purpose of social media in their digital strategy.

At a time when the speed of digital is changing so rapidly – that standing still means falling further behind – this new survey provides actionable insights into how insurers can respond to and grow their digital presence.

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