Analysis and prospects of the French bancassurance market

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"Bancassurance" was created in France in the 70/80's, motivated by a new context of the life insurance market, new needs on the part of the consumers. The positioning of the banks permitted the "bancassurers" to exceed 60% of market shares in 2000.

Since then, bancassurance has been highly successful, as today most of the major French banks have set up their own insurance companies, which take in a significant part of the life insurance market.

This success coincided with a favorable taxation for life insurance products, as well as with the consumers' growing needs, in terms of middle and long term savings, which were due to an inadequacy of the pension schemes in France.

The links between bank and insurance have taken place through various ways (distribution agreements, joint ventures, creation of a company ex nihilo) and have given rise to a complete upheaval concerning marketing strategies and the setting up of insurance products' distribution.

To start with, the bancassurers focused on the sale of products linked to their banking activity, but then diversified their offers and can now be found in most insurance branches (life / non life), with a recent development centered on health, property / casualty insurance.

The objectives of this paper are :

- to describe the French bancassurance market, the various players and their specifications

- to study the conclusions to be drawn from the past experience, concerning technical and marketing approaches, product distribution and synergy created in the financial groups

- to analyze the current development of the model and the European regulation in term of financial conglomerates and solvency of banking groups or insurance groups.

I. The French bancassurance market

I.1 Background

The starting point of the tremendous development of bancassurance is due to the French law of 1984, which unabled credit institutions to wide their activities.
As the legal scope had changed, the banks could carry out additional and related activities, such as life insurance.
This rapid expansion took place mostly in the 80's. Consequently, they could reach a 39% market share of life insurance in 1990. Since then, the distribution through banks networks has been composed of two periods :

- the first one goes from 1990 until 1996 with a steady development up to 61% market share
- the second one more stable then (see table #1)

<u>French life insurance market 1990-2000</u>

	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000
Intermediaries (brokers, agents, employees)	57%	52%	49%	44%	42%	38%	35%	33%	35%	35%	33%
Desks (banks and post	39%	42%	46%	51%	54%	56%	59%	61%	59%	60%	61%
Direct sales	4%	6%	5%	5%	4%	6%	6%	6%	6%	5%	6%
Total	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%

Table #1 : premiums divided up by distribution – from FFSA

For all that, it is significant to mention that the life insurance premium incomes in France has tripled during that time.
The increases according to the different distribution in between starts from 46% to 315%.

In practice, most of the deposit banks own subsidiary dedicated to life insurance.
The top 10 subsidiaries represents 40% of the French Insurance market's assets in 1999. (see table #2)

<u>Top 10 bancassurer's assets</u>

Life Insurance Company	Banking Group	Total assets in 1999 (EUR bn)
Predica	Credit agricole	66 350
Ecureuil Vie	Caisse d'Epargne	41 085
Natio Vie	BNP Paribas	29 460
Sogecap	Société Générale	27 635
Assurances Fédérales	Crédit Lyonnais	21 715
Cardif	BNP Paribas	18 060
Fructivie	Banques Populaires	15 655
Socapi	CIC Crédit Mutuel	13 690
Suravenir	Crédit Mutuel Bretagne	9 940
ACM Vie	Crédit Mutuel	9 655
	Top 10 TOTAL	**253 245**
	TOTAL Market	**630 000**

Table #2 : Top 10 bancassurer's assets in 1999 – from CCA

The Credit Institutions take market shares proportionally to the size of their networks, as the example of Predica, subsidiary of Credit Agricole, which has become the third national player in life insurance since 1995.

The bancassurers have succeeded in capturing the French market by imposing their conception of the life insurance products, with simple and standardized products including low acquisition and administration charges.
The growing of the premium income is partly based on new numerous clients, with middle or small estate who traditionally had the reputation of not being profitable.
The products have taken advantage of the French people's enthusiasm for a favorable taxation.

The part of life insurance in the financial estate of French people increased from 12% in 1990 to 30% in 1999.

I.2 Present Situation

If the example of life insurance can be seen as a success, the distribution of property casualty products to individuals is still limited (from 5% to 6% market share in 2000), but steadily growing.
Car and household insurance are the next targets of bancassurers.
But the issue is different : this activity is considered as less profitable, as a consequence, the banks have mostly opted for partnerships with the main insurers of this market.
Considering the large size of the bank networks, some prospective analysis evaluate their potential market share of the property casualty market of 20% in a future from 5 to 10 years.

II. Lessons to be drawn from this expansion

II.1 Concept

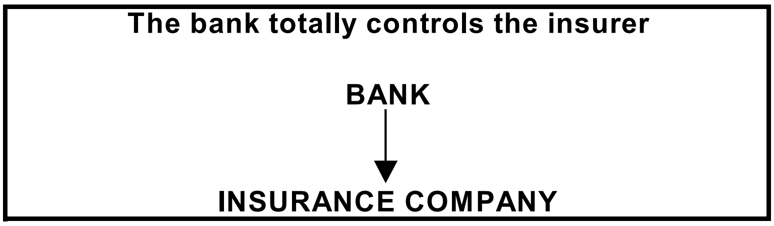
In France, the word "bancassurance" refers to credit institutions which have created an insurance activity. The expression "assurfinance", which is less used, corresponds to the reversed outline.
Originally, the banks had to face :
- the pressure of competition
- the growing automatization and computerization of the tasks.

As a result, the banks were obliged to look for an additional income allowing them to amortize their fixed costs, in order to reach to profitability objectives.
In practice, selling a new product generating very low marginal costs in a banking network, has allowed them to become fearsome competitors.

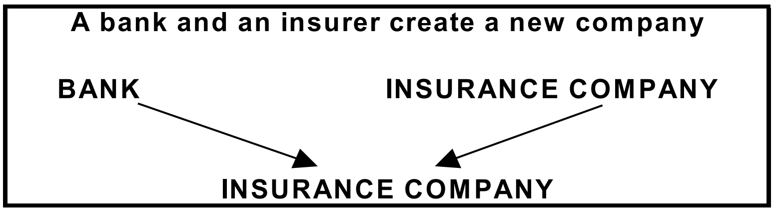
The initial investment for the setting up of the subsidiary was low. The training of the banking staff, as well as the investment in information systems represented the main expenses.
According to the French regulation, the banking staff who sell insurance products have to be specially trained and to be the holder of a professional card.

At last, the significant growth in the 80's corresponds also to a strong demand from the clients in terms of global financial offers. It permitted the banks to improve the development of the customer loyalty.

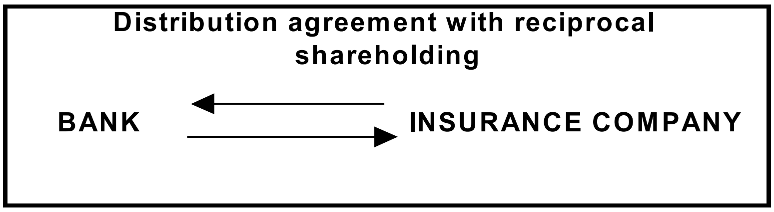
II.2 Main bancassurance systems



This type is considered as the reference in France, and has been widely used as " life insurance subsidiary" of banks.



This type refers to the creation of a new common subsidiary between two players. It is currently expanding in France, particularly in property casualty insurance.



This type is less common in France, but can be complementary to the previous one.

II.3 Business approach

The main objective of bancassurance remains the use of the banking distribution network, in order to sell additional products.
Nevertheless, life insurance has reached such a popularity among the clients that it has become an essential pillar in the banks' global offers.

Legally speaking, life insurance in France is considered as a related activity to savings products in banks. It can be sold without any limit at the desks.
The case is different as far as property casualty insurance, which is part of "extra banking" activities.
As a result, it levels off to 10% of the bank global activity. This limit is not seen as a problem at the moment, since it is developing slowly.

Improving productivity in banks can not be alone without improving profitability of their distribution networks. Those networks, composed of agencies in which clients are welcome, have a heavy cost in the banking overheads.
So, the banks have set up a strategy based on the fixed costs amortization on marginal integration costs products, such as life insurance.

In practice, most of the acquisition commissions go back to the bank. Their employee get a higher fixed salary than the insurance agents, but lower commissions.
We can also notice that the banks have reduced the administrative tasks trough computerization, and have increased the commercial and customer management staff.
The frequent contacts between the bank agencies and their clients is another part of the success of bancassurance, even if the recent development of telling machines and the growing use of internet do not favor those contacts.

The setting up of a global offer and the use of crossed sales have multiplied the number of contracts, thus allowing to saturate the consumers' needs and to develop their loyalty.
These are possible only with the use of powerful and efficient softwares , which implies significant investments, but not always successful results. Life insurance business profitability often depends on the way data bases between banks and insurance companies are matched.
In order to increase the range of products which generates long term relationships and develops loyalty (linked to the global offer from the players), the French bancassurance model will undoubtedly evolve.

After the development of this "industrial" strategy, the banks have diversified their actions by fine-tuning the segmentation of :

- the clients (mainly affluent people), by offering them a global approach for their financial estate
- the products, by adding to the range provident benefits or health insurance

Lastly, most of them have decided to sell property and casualty products, but with a limited success at the moment (6% of the market)

The negative aspect of this hard sell policy results in the saturation of the distribution network – the range can reach up to 200 products – and the loss of the main bancassurers' advantage : the link with banking products.

II.4 Financial approach

In the 80's, the savings products market was prevailed by short and middle term savings products generating a low profitability.
The favourable taxation permitted the bankers to transfer a significant part of their assets to life insurance.
Concretely speaking, the consequence on the banking groups' balance sheets is often a change in the liabilities.
This consequence brings other aspects of synergies between banks and insurance companies to light :
- different duration for the assets
- reversed production cycle
- different impacts resulting from the interests rates variations

Life insurance has also enabled the banking sector to increase its asset management activity. Parallel to that, long term capitals management brings steady incomes.

Bancassurance groups could apply efficient intra-group hedging strategies. It has brought substantial savings compared to a traditional life insurance company, which buy similar products on the financial markets.

On the life insurance subsidiaries' balance sheets, we can also find in the assets debt issues from the banking group. Doing that can raise problems, in terms of control and respect of the asset management rules. For example, the dividing rules can be easily circumvented, bringing significant advantages to the banks and then substantial margins.
The European commission has considered bancassurers and insurbankers as a natural evolution of the market for a long time.
The important growth of the financial savings market in Europe as well as the competition have led the players to mergers and settings up of financial conglomerates.

The steady increasing of intra-group transactions have led the European regulation authorities to react by preparing the following directives :

- the first one deals with an additional supervision of the insurance groups
- the second one which is still at the planning stage, is about financial conglomerates.

III. A regulation turning towards financial conglomerates

III.1 Insurance groups directive versus financial conglomerate directive

After the vote passed for a directive about the supervision of insurance groups at the end of 1998, the European Commission defined a project for directives concerning the additional supervision of financial conglomerates.

This directive directly concerns all the entities which include either insurance companies or credit institutions.

Considering the generalization of the Bancassurance, we have to keep in mind that a high number of players on the domestic market may be brought to build up connections with credit institutions in the future.

Many insurance companies are already linked to credit institutions through the equity or a previous cooperation. Therefore they can be considered as financial conglomerates, as the directive puts it, that is to say groups which activities consists mainly in offering financial services. Besides, they include at least one insurance or reinsurance company and also another company dealing with another financial industry.

As the directive covers a wide domain, several cases can be distinguished :

<u>The homogeneous financial group :</u> It comprises credit institutions, insurance companies but has a prevailing (bank or insurance) element.

The financial conglomerate : It is only made up of financial companies such as banks, insurance companies and investment companies. However, the level of activity is high in each of the 3 lines of business.

Mixed financial company : which holding company is not a financial company but it controls a financial conglomerate . This last brings much business into this new group (see chart # 1)

At this stage, the project of this new directive poses problems :

This directive acknowledges that an additional supervision is useless in a mixed financial company. The non-financial activities (industrial, services and so on) represent more than 50 % of the total activity. This rule would not take into account some financial conglomerates which work within huge composite conglomerates, therefore they are less than 50 % of the group. This measure poses the problem of equal terms of competition.

Rightly, the directive highly recommends to monitor the accumulation of financial risks and the intra-group operations but it does not define what the intra-group operations are. Without any clear definition strong disagreements are likely to appear between managerial staff and the supervising authorities regarding the scope of the additional supervision.

Its main goal is to avoid equity double gearing to evaluate the consolidated solvency of composite financial groups. In order to do so, the current rules seem inappropriate if we consider the system suggested to avoid the double gearing: it consists in deducting all the equity participations exceeding 10 % in the banks or insurance companies from the solvency margin of the parent company.

III.2 Banks' rules versus insurance companies' rules

In extrapolating the future changes in the legal field, we could ask ourselves what the solvency rules of future conglomerates will look like. It naturally leads us to compare the banks' methods and the insurance companies' methods.

The New Basle agreement :

This new agreement, adopted in 2001, but still at the implementation stage, will be set up in 2004.

The project comprises 3 different categories of rules :

- Minimum request of equities, taking the credit, market and operational risk into account.
- A prudential monitoring supervising process which forces the banks to have internal procedures in order to assess the level of their own funds according to the risk
- To consolidate the discipline of the market by establishing standards for publishing information.

Even if the requirements for minimum capital have been supplemented with the starting of the new operational risk, the banking prudential system only deals with assets risks.

Self regulation takes a significant part in the project. In practice a need for a margin is not automatically created besides each identified risk. A process of internal managing of each bank , while monitored by the national authorities, allows this risks management.

This approach contrasts with the RBC approach (risk based capital) which includes in one calculation all the risks taken by an insurance company. The supervising authorities have an essential role to play when the solvency margin is not covered.

If this new banking model was to be set up, it could pose the problem of the equal terms of competition because of the power of members of the supervising authorities as well as their actions are very different from one country to another. As a consequence, 2 banks covering the same branches could have 2 different amounts of allocated capital . The managerial staff of credit institutions could also choose to set up certain sorts of banking services in certain countries according to the domestic practice.

In order to overcome these potential problems, the Basle Committee has imposed the following limits :

- The risk analysis is to be based on the same system of reference which is commonly accepted and translated into 3 categories of risks : credit, market and operational risks.
The supervising authorities will be able to have the internal model modified and so to adjust the capital requirements. The insurance industry has at its disposal a common system of reference in each country, more precisely actuarial guides, but there is no international system of reference at the moment.

- Freely defining the margin's requirements implies, in return, an increasing power of the supervising authorities. This could be done only with a minimum of formalization. It will be interesting for actuaries to have a closer look to the setting up of process which could quickly turned into insurance.

IV. Conclusion

Insurance industry has national common rules as actuarial or controller guidelines but still not has international regulations like Bank industry.

Bancassurance groups have competitive advantage: they can make a choice between the different firms of the group to optimize requirements of solvency margin according to each type of financial operation.

They also can carry out important transactions "intra-group" sometimes without correct risk evaluations.

This new scheme of global organization leads easily insurance players to a serious calling into question.

The actuaries won't escape from this movement and have to prepare themselves to the extension of their business in being inspired by banking models and financial conglomerates.

We must jump at opportunity to assert our skills, and to propose a real international alternative insurance agreement with the insurance industry.

Chart # 1 : Project for European directive concerning the additional supervision of financial conglomerates.