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Rethinking U.S. Life Insurance Distribution

Financial Services Practice

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Introduction

Slow growth has been persistent in the U.S. life insurance market. More recently, changes in customer needs and expectations are adding layers of complexity to the growth challenge. However, these shifting customer behaviors are also creating an opportunity for life insurers to revitalize their approach to distribution. Traditionally, life insurers have turned to boosting agent-driven sales in low-growth environments, but this approach may no longer deliver the results needed. While agents still sell about 90 percent of new policies, growth in the agent channel is shrinking, and no clear alternative has emerged. Compounding this challenge, in the next 10 years, more than 20 percent of experienced agents will reach retirement age.

Life insurers now have an opportunity to strengthen their traditional face-to-face agency model and to develop alternatives that allow them to meet the full range of customer needs. Three distribution models will continue to emerge:

Life insurers now have an opportunity to strengthen their traditional face-to-face agency model and to develop alternatives that allow them to meet the full range of customer needs.

- **Tech-enabled face-to-face holistic planning.** Carriers need to invest further in enhancing the face-to-face model to get the most value from their current captive force assets or third-party distribution. Improvements include innovative planning tools that deliver advice, digital tools (e.g., budget tracking) that improve client engagement, analytics that improve advisor productivity and advisor teams with expertise in protection and investments. The tech-enabled model will allow carriers to meet the needs of the vast majority of consumers who still prefer a local agent.
- **Remote advisory.** Remote advice from a single individual, through

multiple channels, can address consumers' increasing desire for more convenient access to advice, product education and sales. This model will provide customers with enhanced advisor availability and a range of convenient interactions, while still offering comprehensive advice and recommendations.

- **Direct engagement and sales.** This model will target self-directed customers with online tools, education and targeted offers. The goal should be to provide a positive customer experience and streamlined products through a direct channel. Essential to this model will be managing the acquisition costs associated with direct response.

A number of trends—including changing customer behaviors, agent demographics and new regulations—are creating an environment in which life insurers need to rethink how they distribute their products and connect with consumers.

Winds of Change

Sales of life insurance and annuity products in the U.S. are growing at less than 2 percent annually, below the rate of GDP growth. Household penetration is now approximately 65 percent, compared to 83 percent in 1990. This decline cuts across all wealth bands. Among affluent households (liquid financial assets in excess of $1 million), life insurance ownership has declined by 10 percent in the past 20 years. During the same period, penetration in the mass affluent segment (individuals with $100,000 to $1,000,000 in liquid financial assets, or an annual household income over $75,000) declined by approximately 5 percent.

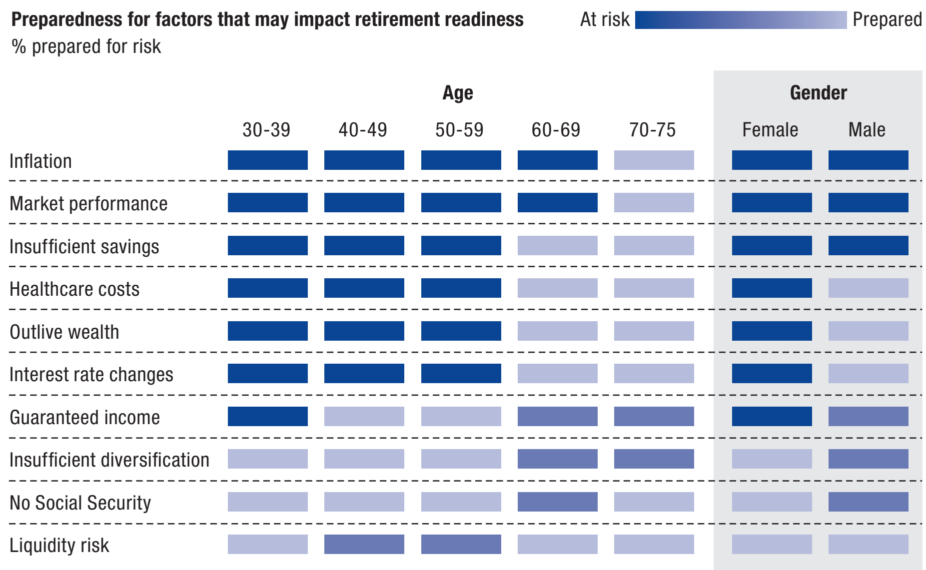
A number of trends point to the need for a new approach:

- **Consumers want comprehensive solutions.** According to McKinsey's research,[1] affluent consumers feel unprepared to address issues related to retirement readiness and are looking for holistic advice that spans multiple needs (e.g., healthcare costs, outliving assets, low interest rates) (Exhibit 1). Put another way, consumers are moving away from pure mortality protection and toward solutions that address the risks of morbidity and outliving their assets.
- **The need for financial planning is largely unmet.** Financial planning and advice is viewed both by affluent consumers and their advisors as critical to ensure retirement readiness; however, 60 to 70 percent of U.S. affluent consumers do not have a financial plan (Exhibit 2). Current planning approaches are considered intimidating, because they emphasize ambitious long-term goals without laying out the steps for achieving them.
- **Consumers want multichannel, tech-enabled options.** Affluent consumers across all age groups are increasingly comfortable with receiving their financial advice online or remotely. Thirty-five to 45 percent of affluent consumers would prefer to complete the process for life insurance quoting and sales online.
- **However, affluent and mass affluent consumers still want an advisor.** They may start their research online, but roughly half of the affluent and mass affluent U.S. consumers McKinsey surveyed said that they would prefer to purchase through an agent or advisor. Twenty to 25 percent

[1] McKinsey Affluent Consumer Insights Survey (ACIS).

Exhibit 1

Consumers are looking beyond simple protection in retirement towards other concerns



Source: McKinsey Affluent Consumer Insights Survey (ACIS) 2014

of those in their 40s and 50s said they would only be comfortable working with an advisor in a face-to-face session.

- **The distribution force is shrinking.** The life insurance distribution force is getting smaller and older. In the U.S., according to a LIMRA-McKinsey Financial Advisor Survey, 20 to 40 percent of agents are within 10 years of retiring or selling their practices. More than half have no succession plans for their business, which threatens continuity of service for their customers.

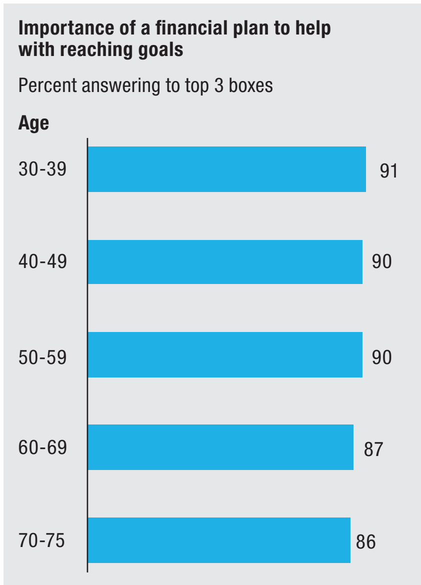
- **A captive sales force is increasingly hard to maintain.** Maintaining and growing a captive force is more challenging and expensive than ever. It takes three to five years for a new hire to ramp up to an average level of productivity. This, along with a four-year retention rate that is under 20 percent, means that life insurers must continuously invest in training and developing new hires. Few networks show net gains in the number of advisors every year, and most are shrinking.

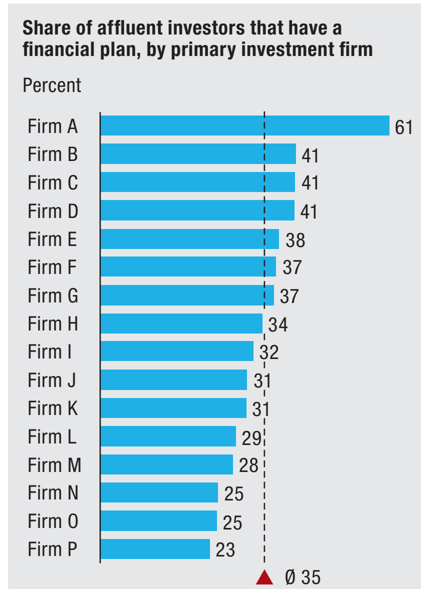
- **Third-party distribution is not the solution.** Carriers that distribute primarily through captive channels see substantially higher year-over-year growth in book value: 11.1 percent from 2003 through 2013, versus 5.1 percent for carriers using primarily third-party distribution. This superior productivity may be due to the ability to better control access to distribution or to focus the efforts of a captive sales-force on the products that have the most value for carriers.

- **The regulatory environment will impact distribution and advice models.** The Department of Labor's

Exhibit 2

Affluent consumers consider a financial plan critical, but most do not have one





Source: McKinsey Affluent Consumer Insights Survey (ACIS) 2014

fiduciary standards ruling requires carriers to make significant changes to their distribution and advice models in the next two years. The rule puts downward pressure on fees and requires a shift toward commission structures for advisors or the introduction of "fee for advice" models. Increased focus on delivery of appropriate advice to consumers may require carriers to push for greater consistency and centralized management of advisory services.

To grow in the face of these headwinds, carriers should consider expanding their captive forces and building a portfolio of distribution models that increases their reach across customer segments.

A Portfolio of Distribution Models

To meet the wide range of consumer needs and behaviors, life insurers should consider a portfolio of models. The first, described below, is an enhancement of the traditional agent model. The second represents a dynamic way to reach customers who demand personalized service but are fully open to remote channels. The third is an economical direct model designed to reach the underserved mass market through a low-cost digital interface (Exhibit 3).

Tech-enabled, face-to-face holistic financial planning

A tech-enabled, face-to-face holistic financial planning model enhances the traditional face-to-face approach with interactive financial planning, goal-tracking, integrated protection and investment solutions, and analytics to improve advisor productivity. Digital planning, aggregation and tracking tools enhance ongoing advisor relationships and deepen customer engagement by providing advisors with real time access to changes in their clients' behaviors. Instead of meeting every six months to review progress, an advisor can interject at critical moments throughout the year. Traditional life insurance advisors will no longer simply make transactions, but will work with their clients continually over time. In addition, teams of advisors will enable carriers to deliver a range of protection and investment products within the face-to-face channel, while improving productivity.

Face-to-face distribution augmented by financial planning and digital tools would help carriers better serve their most profitable customer segments, who value the ability to see an advisor when they want to, and need actionable financial plans that address a holistic set of needs. Seventy-five to 80 percent of profits from protection products and 90 to 98 percent of profits from retirement and wealth management products are concentrated in the affluent and mass affluent segments. The economic benefits of this model include higher advisor productivity (and higher/less volatile advisor income), a more consistent client experience, and reduced administrative costs. The challenge will be shifting advisor behavior from selling products to providing holistic planning solutions.

Exhibit 3

Three distribution models are needed to meet evolving consumer expectations and preferences

Model	Tech-enabled face-to-face holistic planning	Remote advisory	Direct engagement and sales
	Traditional face-to-face model for consumers with preference for relationship-based advice Augments advisor force with multichannel tools and access to improve productivity and customer engagement	Serves the needs of consumers who prefer convenient access to live advice, education and sales Centralizes and streamlines management of advisor force, allowing more consistent advisor experience Digital and analytic tools to improve customer experience and engagement	Targets self-driven customers through optimization of online tools, education and offers An economical model that can effectively reach mass market customers
Defining capabilities	Integrates online and digital planning tools (including aggregation of financial accounts) as part of ongoing advisor relationship Uses enhanced data and analytics to more effectively predict and target needs of customers Advisor "teaming" to serve diverse client needs	Develops on-boarding and training for inexperienced advisors through a defined career path Uses digital tools to standardize customer experience and enable effective remote collaboration Increases engagement through advice, regularly scheduled check-ins on financial goals and advisor discussions	Includes direct and digital marketing (e.g., search engine and aggregator optimization) Provides targeted "entry" offers to engage consumers Includes online product education, mass advice and simplified underwriting for lower-cost products

Source: McKinsey & Company

Remote advisory. In a remote model, dedicated advisors based in a centralized location would connect with customers through phone and online channels. The remote advisory model provides similar value to the face-to-face model, but can increase consistency of service and improve on the economics of the traditional captive agency model. As advisors help customers track their financial goals, they can continue to engage and develop the relationship. Mass affluent consumers seem particularly interested in remote advice—more than 30 percent say they would be comfortable with an advisor they did not meet face-to-face.

The benefits of this model include enhanced advisor productivity and retention, particularly for newer advisors. On-boarding, training, consistent coaching and capability development are easier in a centralized advisor center than in a distributed agency force. New compensation models (e.g., salary plus bonus) could enhance carrier economics.

Carriers will need to find economically viable ways to drive volume to remote advisory centers. To date, carriers have been pursuing a number of approaches including affinity partnerships with other financial institutions (e.g., regional banks, credit unions), aggregators, targeted direct response marketing, and outbound calling on orphaned policies.

Direct engagement and sales. The third model represents an economically viable approach for reaching self-directed customers and the middle market. In McKinsey's affluent consumer insights survey of 10,000 consumers with more than $100,000 in liquid financial assets, more than 30 percent of consumers say they would likely purchase some life insurance online (through a carrier's or third party's website), and 35 to 45 percent say they would prefer to get quotes and complete their purchase online.

A direct model, like remote advisory, would leverage digital marketing (e.g., search engine optimization), digital aggregators, direct response marketing and partner referrals to reach consumers early in their decision journey. An intuitive digital experience would combine online education and mass-customized advice based on several key factors (e.g., age, number of dependents, income/assets), and call center reps would lend support as needed. Low-cost, simplified product offers would be an important part of this model, drawing customers and encouraging them to close the "anchor sale" while minimizing underwriting and administrative expense. After the sale, advice algorithms could generate additional cross-sell leads for outbound calling and follow-up sales.

The economic viability of this model hinges on the costs of drawing clients to a predominantly direct channel, and it will likely require a combination of affinity-style partnerships to generate referrals and stronger brand awareness and marketing.

Making the Transition

Making the transition from a predominantly captive agency-based distribution system to a portfolio of models will require carriers to change the way they operate in several important areas:

- **Adopt a more customer-centric mindset.** Carriers often focus on the needs of advisors when building new capabilities. In order to succeed with more direct models, carriers will need to reorient and focus on the needs and preferences of their customers.

Carriers that succeed will be well positioned to capture tremendous growth, improve profitability and provide comprehensive solutions to consumers, many of whom are underserved today.

- **Relentlessly communicate a cohesive distribution strategy.** Disruption to the field sales force is perceived as one of the biggest risks associated with a portfolio approach to distribution. To minimize potential disruption, carriers can communicate clearly about how new models can help existing advisors and open the doors to a set of consumers that are currently underserved. In the P&C personal lines market, carriers have addressed this challenge in a number of ways, in some cases creating distinct brands for their direct models. And some life insurers have developed separate brands to serve younger, less affluent clients through an end-to-end direct-to-consumer model.
- **Build for the next five years, not the next quarter.** The new distribution models represent significant shifts in how carriers and their advisors will interact with consumers, and each has its own set of challenges. Effective and lasting innovation should be viewed as a multiyear journey, not a quick fix.
- **Focus on the most critical end-to-end customer journeys.** As they develop new distribution models, carriers should focus on the five or 10 most critical customer journeys (e.g., research, planning, product purchase) and rethink those journeys from end to end. This means going beyond optimizing touchpoints to optimizing interactions across channels and across functional silos.
- **Test and learn.** Carriers will need to be comfortable testing, learning and refining their go-to-market approach within each distribution model. This is particularly critical given the new capabilities that will need to be de-

ployed, but can be tremendously difficult for carriers that are used to making incremental improvements to their existing business.

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Growth has been a long-standing challenge for U.S. life insurers, and changing customer behaviors is yet another obstacle to growth. However, these changing behaviors represent an opportunity to rethink distribution in ways that meet the needs of customers and address the economic challenges associated with traditional agent-based distribution. Carriers that succeed will be well positioned to capture tremendous growth, improve profitability and provide comprehensive solutions to consumers, many of whom are underserved today.

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