

INSURANCE COMPANY AND BANK PARTNERSHIP AS A DISTRIBUTION CHANNEL OF INSURANCE PRODUCTS

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JEL Classification: G11, G15, G21, G34

Original Scientific Papers

Primljeno / Received: May 27, 2013

Prihvaćeno / Accepted: October 29, 2013

Abstract

The main distribution channels of financial products that insurance companies and banks use, as well as key benefits of joint product selling are investigated in the article.

The cooperation of insurance companies and banks in order to promote financial products is examined in the article. The study describes three basic models of cooperation: model in which bank-leader has initiated the cooperation, model in which insurer - leader has initiated the cooperation and joint ventures which sales financial products of insurance company and bank together. The basic advantages that insurance companies and banks can gain from such cooperation are explored in the article.

Key word: *partnership model, partner company, insurance company - leader, bank -leader, joint venture.*

1. INTRODUCTION

Cooperation is a necessary competitive advantage for leading financial intermediaries' (banks and insurance companies) functioning due to increased riskiness of the modern market environment and fierce competition in all areas of trade today. Only partnership, but not competition allows them to generate additional revenues, reduce costs and minimize risks. One of the most important benefits of this collaboration is ability to increase customer loyalty to insurance companies and banks.

Nowdays there is no accepted common scheme of cooperation between the insurance company and the bank in the world because of influence of historical, demographic, economic and political climate of the country (Nikolenko 2007). Insurance company and bank partnership provides preservation of the independence

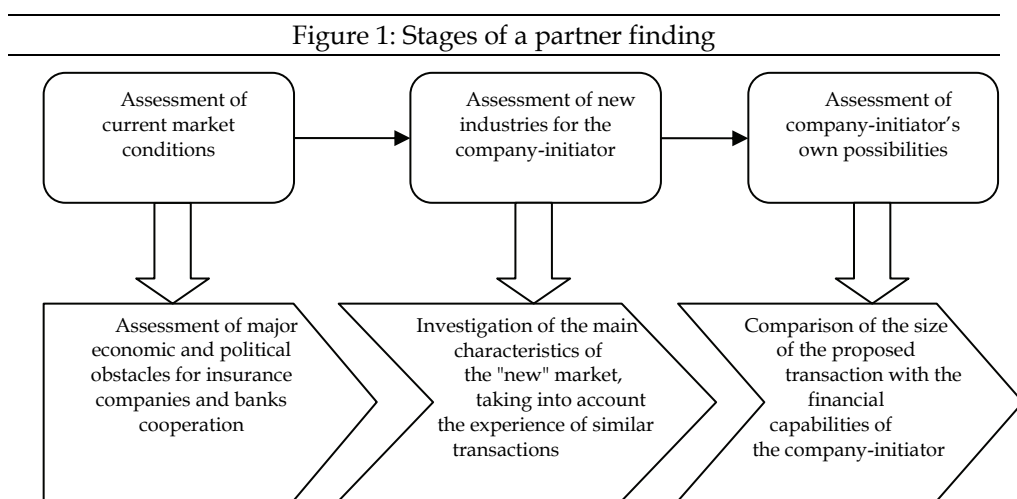
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of both companies, although the capital of the companies could be merged (Mun-chener Ruck-Gruppe with ERGO/HVB, AMB-Generali /Commerzbank, Sparkassen - Sektor, as well as V+R - Sektor), the company can act differently according to their financial and strategic objectives. The most widespread types of partnerships between the financial intermediaries that are studied in the article are the next: a partnership model in which the insurance company is a leader; partnership model in which the bank is a leader; a model of a joint venture of insurance company and the bank.

2. THE PARTNER COMPANY SEARCHING

The searching of potential partner company may include the next three steps (Fig. 1):



Source: developed by the authors

Assessment of current market situation requires development of the research project on the political and economic situation in the country by a company - initiator in order to avoid obstacles to cooperation. This assessment may include: analysis of the legal framework that adjusts business alliance, the tax treatment for this kind of alliances, the macroeconomic situation, the availability and experience of these associations, consumer attitudes to financial conglomerates etc. If these conditions are favorable for the interaction of the insurance company and the bank, the next step of the company-initiator is target industry analyzing. Singling out a potential partner for mergers / acquisitions and assessment of its financial condition are the key issues on the way of cooperation of financial institutions. Errors that can be made at this stage, such as the wrong choice of partner and high price for it, lead to the entire project exclusion.

Self-empowerment assessment of the initiating company is a comprehensive analysis of its financial results, prospects, performance management and marketing, reputation in the market etc conducted by internal or invited experts before making reorganization.

When choosing a partner, it is important to analyze the impact of a number of criteria that will significantly reduce the risks of joint venture:

- Companies' reliability. Only reliable company can be chosen for the partnership, otherwise any problems of a partner company (financial, organizational, and managerial) may adversely affect the joint business conducting;
- Compliance of business. Companies should take a similar position in their markets. In other words, partnership of the companies will be less effective if one of the partners is a bank, which is among the ten largest in the market, and another partner is a small insurance company, or vice versa.
- Direction of business. Cooperation of insurance company that primarily works with corporate clients and the bank that builds business for private clients is not ineffective. Partners should focus on common lines of business, for example retail bank - retail insurance company. It will be easier for partners to build a business together with experience in the same market segment. However, there may be reversible cases. If retail insurance company wants to enter the corporate market it has to be integrated with the corporate bank.
- The transaction cost. The size of the required investment in the acquisition of a company or joint venture organization is very important when choosing a partner. It is necessary to assess the effectiveness of planned investments and the term of recoument.
- Value purpose companies. This criterion implies that it is difficult to build an effective partnership model, if the target companies planning integration, diametrically opposed and conflicting.
- Territorial location. Large banks and insurance companies, as a rule have an extensive network of branches on the most territory of the country. Regarding to this fact, the coincidence of the branch networks of partners is very important as it can help to organize joint work in a short time.
- Image and reputation of companies. The presence of a positive image and reputation greatly reduces the risks of doing business together, since there is no need to overcome the negative attitude of company's clients to its partner.

3. MODEL "INSURANCE COMPANY LEADER"

Insurance companies and banks partnership model, in which insurance company is a leader is not only a stable channel for insurance products distribution and mutual use of the total customer base, but also the expansion of strategic and marketing opportunities. The insurer is a leader and initiator of partnership in this model by signing an agreement with the bank or several banks.

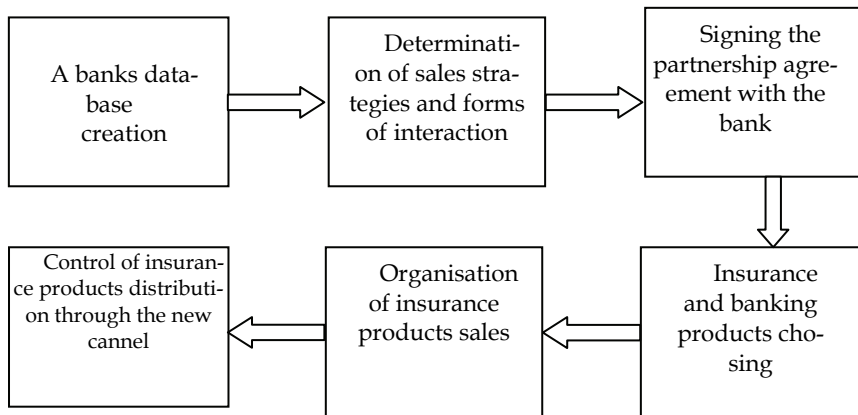
Expectations of the insurance companies from this partnership model are the following:

- Premiums increasing by attracting new customers (customer base of the insurance company increases by gaining access to the customer base of the banks);
- Quality of customer service improving due to consultations with banks, car dealers, real estate companies etc.

While insurance companies often limit themselves to use only a client base of the bank, which the insurance company choosed as a partner, but as for proactive companies this model of cooperation can maximize their own potential and capabilities of the bank to create optimal conditions for the client.

In this case, the insurance company does not have to be big and famous. Sometimes small insurance companies can benefit from this partnership. For example, access to car loans can afford to get a significant increase in premiums of compulsory civil liability insurance. So the first step of insurance company and the bank partnership model in which the insurer is a leader is to create a database of potential banks - partners and negotiate with selected according to certain criteria banks (Figure 2).

Figure 2: Scheme of building of insurance company and the bank partnerships model



Source: developed by the authors

Successful sales of insurance products through banking networks are necessarily based on good reputation among the main part of the bank's regular customers, and the condition of the marketing process integration into the daily routine activities of both companies.

Common insurers' mistake is the pursuit of partnership with all the banks at once. But the insurance company can not be limited with one partner bank, even if

the agreements of insurance products placement are concluded. For example, the Russian "Insurance Company ALICO" (a subsidiary of MetLife Inc) cooperates with several banks, including: VTB 24, Alfa -Bank, Sovcombank, Trust Bank, Citibank, UniCredit Bank, Raiffeisenbank, GE Money Bank, Barclays.

If the insurance company is set up for the long cooperation, staff also needs to have their attractive side of this cooperation in addition to the bank commission. The work with an authentic bank, which is close to the insurer in its size and strategy, culture, customer service, speed decision making and other parameters is successful.

If the insurance company is retail, then it is easier to work with the retail bank. If the insurance company is versatile and large, it is easier to negotiate and work with a universal bank.

In order to negotiate with the bank successfully, the insurance company must:

- Choose an authentic bank;
- Determine the right sales strategy and forms of interaction;
- Identify their competitive advantage.

The next steps of the implementation of the banking sales technology are sales strategy development and interaction form choosing, which can be one-sided, two-sided, interaction with the intermediary. Defining sales strategy, insurance companies and banks can make the next step in the implementation of the partnership model and define the forms of interaction within chosen strategy.

The next step in the distribution of insurance products through the banks is the legal form of the agreements reached between the bank and the insurance company approving. The agreement between the insurance company and the bank must include:

- The subject of the contract;
- Order delivery and reception services and mutual payments;
- Product range and tariff policy;
- Duration of the contract and termination of the procedure;
- Financial cooperation of the partners;
- Applications (list of insurance regulations and bank remuneration, insurance products and insurance rates, affiliates of the partners, the act of reception and transmission of insurance documentatio, especially forms of strict accountability, certificates of insurance agreements, rules of interaction between the insurance company and the bank).

The most important step in the bancassurance implementation is insurance and banking products choosing for the organization of their sale through partnerships with banks.

To organize sales of insurance products in a bank, one have to build a sales pyramid in such way to cover all possible categories of potential policyholders.

The organization of practical work of the sale of insurance products in a bank includes the following activities:

- Sales forms choosing and sales implementation;
- Bank staff training;
- IT software development;
- Bank employees engaged in sales motivation;
- Logistical support.

Western experience as well as native experience suggests that critical factors of success of insurance products selling in the partner banks are bank staff awareness and effective information technology. Depending on the "advancement" of the insurance company and the bank, IT programs may consist of directories, electronic calculators, programs, statements of policies, automated formation of databases on customers and bordereaus.

IT support of the insurance company that works in a bank must be easily adapted to banking software products and should not cause the need for banking professionals retraining. The interface of these programs should also be unique and easy to handle. Today, insurance companies have already established in the bank workstations that allow on-line mode to work with the database of the insurance company (Tkachenko 2004).

Depending on the complexity of the insurance product, the amount of the bank employee's core work, IT solutions performance, qualification of bank employees and the type of customer, the main subjects of insurance sales in the bank are:

- Employee of the bank;
- Employee of the insurance company;
- Account Manager;
- The agent of the insurance company;
- Combination option.

Sale of common and well known insurance services is conducted by bank employees. When it is innovative and complex products, bank employees should involve the insurance company. In this case, the bank staff is not engaged in actual sales it is engaged in presales.

The technology of personal customer sales in which a personal customer manager of an insurance company is assigned for each legal entity is more successful for corporate clients. This manager solves all the problems of the client not only under a contract of insurance, but also at the stage of maintenance during the period of insurance. In addition, the insurance company can apply the technology of Direct marketing for these clients (personalized direct mail , email or telephone calls - Pasko 2008).

If we are going to talk about work with individuals - customers of the bank, there may be bank employees, or employees of an insurance company or agent sales technology.

For example, German insurance company ERGO and HVB Bank signed a partnership agreement differentiated by consumer groups, in which the insurance company acted as the initiator and leader. The contract involves the attracting of bank employees only to serve consumers with high incomes in providing customized services. Also insurance company's services, designed as a baseline are provided by the insurance company on their own without the involvement of bank partner staff.

Tangible and intangible incentives of bank employees are important for the development of insurance sales in the bank system. Incentives models can vary - depending on the goals and objectives of stimulating, corporate culture of the bank etc. The main forms of motivation of bank employees are a personal incentive, collective incentive, mixed stimulation. The partnership between the insurance company and the bank has the following advantages:

- Possibility to work with several banks at the same time;
- No significant financial losses at termination of cooperation for both companies;
- Little investment in the organization of cooperation between the partners;
- Competitiveness increasing by creating new products;
- Customer base increase with the help of cross-selling organizations;
- Additional points of sale of insurance products.
- However, such partnership model in which the insurance company is a leader has the following disadvantages:
- Inability to create high-tech joint products;
- A small number of branches and representative offices of insurance companies in the country;
- Low efficiency of interaction between the partners;
- Low yield of partnership activities;
- The staff have to master the product and sales organization process of the partner company;
- Low awareness of benefits of insurance.

Unreasonable "rat race" commissions should be considered as the downside of cooperation with such strong partners as commercial banks. When working with some banks, their claims for commission payments can exceed 50 % of the insurance premium. Not accidentally the state regulation of determining of the commission on the sale of insurance products through a channel of cooperation with banks is lately introduced in Europe.

4. MODEL "BANK - LEADER"

In this model, the bank assumes the leadership in the sales system, and one or more insurance companies "deliver" to it their insurance products for distribution within bancassurance. As in the first case, it is assumed that the bank is the leader, has a large structure with well -developed distribution network that includes multiple channels: branches, ATMs, sales phone, Internet, etc.

Supporting of competition on a qualitative and quantitative level between insurance companies (quality services selection, the trust accounting, and insurers' brands) is one of the main factors for the profitable realisation of the bansassurance strategy. In this model, insurance companies benefit from increased sales and at the same time bank gains commission on sales and reducing the unit cost of sales as a result of a full load. The main motivations that encourage banks to work with insurance companies are:

- Insurer's customer base using to promote bank products;
- Providing additional benefits to existing customers and rising opportunities to attract new clients;
- Expanding the boundaries of the core activities and product range with the implementation of advanced information technologies;
- Credit base increasing by attracting reserves of insurance companies;
- Generate additional revenues and reduce costs.

The revenues of the bank increase due to:

A. Receiving commissions on selling insurance products to corporate and individual customers through its own sales channels. Simple and affordable insurance products such as motor insurance, accident insurance, insurance when traveling abroad etc., are sold mostly through banking channels. Implementation of these operations doesn't require special skills and isn't time consuming. However, in many developed countries, where the integration of banking and insurance sector reached its highest form, sales of more expensive insurance products, such as property insurance, voluntary health insurance etc. are practiced. Fee income of the bank depends on the amount of sold insurance policies and bank employees receive appropriate bonuses for selling insurance products.

B. Getting additional profit from reserves of insurance companies located in the bank. By placing surplus funds in the bank account the insurer receives proper interest, and the bank uses the money in investing activities and gets investment income.

C. Reducing bank's own costs with the help of an established partnership with one or more insurance companies. Bank may purchase a number of products, collateral under the loan insurance, workers and clients insurance, banking assets: buildings, facilities, storage facilities, vehicles, equipment on preferential terms (discount).

A wide range of financial services provided in a one company allows retaining the existing customers and attracting new ones. According to research of the Association of American banks a bank customer retention is directly proportional to the number of services purchased by him: when opening a current account the likelihood that the customer will stay is 50 %, while placing a deposit - 66 %, and the current account and deposit together increases probability of customer retaining to 90%; the current account and deposit and loan debt in the bank increases probability to 94%. If a consumer receives a full range of financial services in the bank, he will be customer of this financial institution by 99% (Nikolenko 2007). Bank insurer is essentially a unique organization that can effectively combine all business processes of the client in a single financial service. This greatly simplifies the perception of financial services by the client.

5. MODEL OF "JOINT VENTURE"

Insurance company and the bank collaboration model, which is conducted by creating a new joint venture, is popular in many European countries. Typically, a joint venture is formed on the basis of an existing bank branch or by creating a new insurance company (under the brand name of an existing one).

Usually, the bank acts as initiator and main investor in the creation of such company getting profits not only from the distribution of insurance services, but also in the form of dividends from the new company (Demchenko 2004). The insurance company, in turn, provides a brand to new company (usually already quite famous in the market). According to this model, bank and insurance company partner develop a new strategy of the company, manage it and create its product line together. There are many advantages of establishing the new company by the bank and the insurance company including the following:

- The new company has the brand of the insurer and instantly gets an array of clientele and reputation that immediately solves the initial problem of any business - winning its market niche.
- There is no need to integrate management structures: each partner has a clearly defined its own part of responsibility and control of Bancassurance.
- As in previous phases, a broad customer base of the bank is a potential field of the new company that allows to segment group of consumers according to their needs.

Working with the insurance company as part of the agreement, the bank gets its experience, products, and technological developments. Insurer gets the loyalty of clients and even after the expiration of the agreement will serve this client array. High initial investments of the insurer and the bank that go to create a new company and purchase of equipment, hiring qualified staff, promotions, etc are the main drawbacks of this agreement (Demchenko 2004).

6. THE MAIN ADVANTAGES OF THE INSURANCE COMPANY AND BANK PARTNERSHIP

Competitive position saving and then market share increasing are great advantages. Market share growth is achieved by combining the efforts of partner companies to build joint business, merging their customer bases, new financial products creation and so on. Effective marketing policies of the companies allow two "brand" save their own clientele and attract new customers. In addition, operations scaling and its diversification give the access to large projects.

Expansion of the product range. Together in a single structure with centralized management and shared objectives, financial intermediaries provide each other products of their own with the proper software, which significantly improves the quality of each of them. Also, one of the important features of interaction between banks and insurance companies is the creation of innovative financial products that are able to satisfy the customer, both in the banking and the insurance sectors. These integrated financial products are another competitive advantage of the banking and insurance associations.

Geographic diversification, which allows not only to increase significantly its customer base in a lot of regions, but also to avoid the accumulation of risks in the same area (Demchenko 2004).

Diversification of risks. As a result of vertical integration there is risk sharing between insurance and banking business, the probability of financial distress for the company as a result of problems in the banking and insurance sector is reduced significantly.

Economies of scale and synergies achieving. Unique opportunities are faced by companies as a result of their association.

Economies of scale are defined as the value of the services dependent on the scale of their production. During the bank and insurance companies interaction economies of scale are achieved by reducing costs in the following areas:

- Joint advertising of financial intermediaries;
- The distribution of fixed costs between the insurer and the bank (rent, interest payments on loans, etc.);
- Attracting highly skilled staff, experienced in both the banking and the insurance sectors;
- The new technologies using and the introduction of automation of financial services;
- Any type of research and the creation of new competitive products.

Synergy Effect is a relatively new concept in economy, which is often considered to be synonymous with cooperation. K.Marx pointed out that synergy is a new force that collects many forces into one during its merging. In the context of current trends of mergers and acquisitions synergy effects are considered to be ac-

cumulated effects arising from the interaction of two or more components, which are significantly higher than the effects that are created separately by each component. Synergy effect is achieved if the value of an integrated company is greater than the cost of the separate bank and insurance company. Due to the size of synergy the final transaction price is formed and side-initiator accepts or rejects the decision of the interaction.

7. CONCLUSION

Banking and insurance are similar in nature, their cooperation is beneficial for both partners, and insurance and banking services are equally important and essential for consumers. The cooperation between insurance companies and banks is very widespread in the global financial space, the most common feature of which is the sale of insurance products through bank distribution network. It should be mentioned that elements of marketing of financial products joint selling and alternatives of building a business is only static models that are sufficiently rare in practice in its purest form. Typically, a joint venture of bank and insurance company changes dynamically because of influence of many external and internal factors.

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