By

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Banker, Know Not Only Thyself, But ...

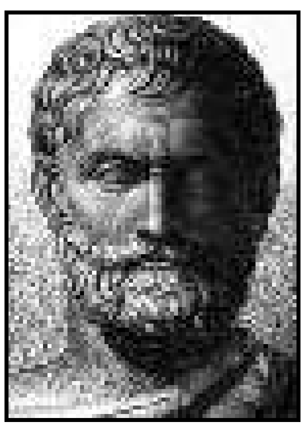
The inscription on Apollo's temple at Delphi read, "Know thyself," an aphorism ascribed to the great Athenian lawgiver Solon. Solon is one of 16 great lawgivers in world history portrayed in the frieze in the chambers of the U. S. Supreme Court. This wise objective of knowing thyself seems, on the surface, easy to achieve.

However, Thales, Greece's first philosopher and a contemporary of Solon, knew better. According to Diogenes Laertius, first historian of Greek philosophy and author of *The Lives of Philosophers*, when Thales was asked to identify the most difficult thing a person can attempt to do, he responded, "To know one's self."

Banker, know thyself, know thy customer bases

But knowing oneself is an essential first step in understanding. This is true in business as well. A banker entering the insurance marketplace needs to "know thyself." He or she needs to understand the bank's core banking businesses, key consumer transactions, size and makeup of different types of loan portfolios, nature of the depositor-base, proportion of multiple-account holders, and average number of accounts customers possess. Bank management must articulate its financial and nonfinancial objectives for the bank and its incipient insurance program, and it must identify meaningful, actionable and profitable customer bases or segments.

The insurance chief at a large banking organization recently told me that his bank had a particular mortgage portfolio with several tens of thousands of borrowers. It diligently tried to make money direct-marketing and re-marketing homeowners insurance to this portfolio. The insurance efforts given this mortgage portfolio were intensive and non-stop.



Thales

But, after some time, he re-analyzed the portfolio's potential and wondered why he 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. 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 or 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 of our regional bank clients was among the largest institutions in its state. From the beginning, the bank's executives were most interested in selling auto insurance. We agreed that, after gathering requisite bank data, our first priority would be to evaluate the bank's potential for selling auto insurance. After examining the data and asking questions, we discovered that, of the bank's 52,000 auto loans, only 500 were direct.

In preliminary efforts to know their bank, management had equated all auto loans with car insurance sales. But indirect auto loans are virtually useless to a bank's insurance initiatives. Indirect borrowers are not really the bank's customers, and the bank is not at the point of sale where the transaction prompts insurance needs. These bankers did not understand how the insurance marketplace works, nor did they realize that the auto dealers have agencies that sell insurance. (Indeed, they thought my reference to "those F-and-I guys" was a contraction for some obscenity.)

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Still, these bankers wanted to sell auto insurance and believed that the bank could build a "customer" database as it received loan documentation from the auto dealers. They believed that, since the loan docs 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.

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 minimum 15 percent ROI previously established as a key financial objective.

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 and depend on "those F-and-I guys" to improve their dealerships' margins. Anyway, the question is moot, since this bank's state – like many other states – has a law that expressly 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: the transactions they execute, the kinds of bank accounts (assets) they have, the events in their lives signifying needs to be met, aspirations to be achieved, or problems to be solved. It means knowing customers' overall financial positions, their family members, their short-term needs and long-term goals, and what products are strategically right for a bank's customers.

One bank client provided us 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, retirement and investment products like 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.

One community bank CEO told me he decided to act on the advice he had frequently read encouraging banks to get rid of unprofitable accounts by penalizing them with new charges. He assigned an employee to compile a list of "under-sized" savings accounts. The bank then sent notices to these depositors informing them of the additional account charges levied for not maintaining a suitable balance.

Imagine his chagrin when one of the wealthiest ladies in town called to complain about the bank's new policy. She had set up one of these "under-sized" accounts for her granddaughter, hoping to instill in her the virtues of thrift and goal setting. A trust customer with an additional $300,000 in the bank's short and medium-term certificates of deposit, this lady was in the process of considering buying from the bank a large annuity with outside funds. Can you see the banker's embarrassment over the many factors he failed to consider when he decided to rid himself of "unprofitable" account-relationships? Lesson learned, he quickly revoked his new policy.

Know others

The Greek comic playwright, Menander, had another take on the maxim "know thyself." Menander advised, "'Know thyself' is a good saying, but not in all situations. In many, it is better to say, 'Know others.'"

Menander

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.

Responding to member-requests for training in how to approach and work with banks, this agent association hired a firm to prepare a marketing packet that projects premium volumes, commissions and earnings for an agency-bank joint venture. Subsequently, a major banking trade association tacitly endorsed these projections by issuing a publication using the agent association's pro forma projections for these "joint ventures."

Bankers should be aware … and beware … of these pro forma projections. They are based on unrealistic assumptions about the average $250 million-asset bank.

This allegedly average community bank services its 15,000 retail household customers at 7 banking locations. It is said to issue annually over 3,000 direct auto loans and possess a portfolio of nearly 11,400 auto loans. It supposedly originates 1,250 new home loans per year, with an existing book of 6,250 mortgages. The assumptions regarding these new and existing loans result in a number of loans 50 percent greater than the bank's customer base, a circumstance I have yet to encounter.

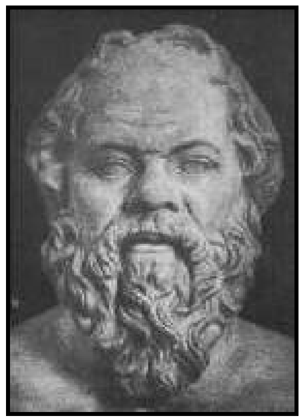
More exaggerated are the projections of annual penetration rates for personal lines and life insurance sales. The agent association's pro forma projects annual penetration rates of 10 percent of the bank's retail customer base, meaning that sales are projected to be 1,500 personal lines and 1,500 life policies each year. What's wrong with these numbers?

Grossly inflated, they constitute a sales program based on agent body count, not enhanced productivity. Consider what it takes to sell 1,500 life insurance policies. In the open market, an agent needs 10 appointments to close one sale, ergo, a sales closing ratio of 10 percent. A key premise of bank insurance marketing is that it enhances productivity with coordinated generation of warm leads, higher closing rates, and more agent sales.

This isn't bank insurance, it's body count

If a bank insurance program attains a 25 percent closing rate instead of the more 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 the 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. Therefore, this bank needs at least 4 life insurance agents, possibly as many as 8, to achieve those results.



Socrates

Applying the same reasoning to the sale of personal lines' auto and homeowners insurance, the bank needs 4 to 8 property-casualty agents. *Already*, there are between 8 and 16 agents selling in the bank's 7 locations. And we still have yet to consider the numbers of agents needed to sell the pro forma's other products like commercial insurance, employee benefits, auto warranty coverage, title insurance, credit insurance and crop insurance. One might humorously surmise that, under this pro forma's scenario, at any given time, there will be more agents in any given branch than bank employees and customers combined.

And what does the bank earn from this "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, or 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 1.0 percent. Why would any bank go for this kind of deal?

These projections do not represent a sensible bank insurance strategy. If bankers understood it took that many agents to produce less than $40,000 in bank earnings, bankers would rightly say, "Why bother?" Truth is, these pro forma projections are unfair to bankers and agents alike. Their unrealistic expectations and inevitably disappointing results set up everyone for discouragement, and they do nothing to advance the ostensible advantages of bank insurance marketing, namely, enhanced productivity, cost-effective distribution, and efficient delivery of services.

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 know enough to recognize when they are getting skinned. And, when they do not understand something, bankers should have the good sense to say, "I do not know what you mean; explain it again."

After all, sometimes part of "know thyself" is recognizing what another Greek, Socrates, in Plato's *Phaedrus*, told us: "All I know is that I know nothing."

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