The Framework For Insurance Marketing Changes

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ABSTRACT

The movement of large life insurers into multiple-line insurance has attracted much attention in recent years. However, this movement should be viewed as the natural consequence of past changes that have taken place in the insurance industry and the business community as a whole, as well as basic social, political and economic changes. The marketing power of the thousands of debit life insurance agents promises to make the life insurers major factors in the future multiple-line insurance marketing system. Early results of Prudential Property and Casualty Insurance Company indicate impressive marketing ability and underwriting performance. The first full year of operation of Hanseco, Inc., was not impressive in either area.

The movement of large life insurers into the property and liability insurance field is sometimes viewed as a new development. It would seem more appropriate to think of it as a continuation of a movement that started at least fifteen years ago, with roots reaching back at least to World War II.

The diversification of life insurers into multiple-line operations is not a spontaneous development. It was the results of developments within the property and liability insurance industry and within the business community as a whole.

The Rise of Direct Writers

The earliest seeds of the movement were sown in the decade of the twenties. In 1922, State Farm Mutual Automobile Insurance Company was founded, to be followed nine years later by the establishment of Allstate Insurance Company. As one might expect, both companies had relatively modest beginnings, but modest beginnings were to be followed by rapid growth. These two companies, with others which followed similar operating methods, were to challenge successfully the market dominance of the old established agency companies and to bring many changes to the insurance industry.

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By 1941 the four leading direct writing insurers held only 5.3 percent of the automobile insurance market, as opposed to the 10.3 percent held by the four leading agency companies. Thirty years later the share of the four leading agency companies had grown from 10.3 percent to 12.6 percent, but the share of the four leading direct writers had grown from 5.3 percent to 25.9 percent.[1] One direct writer, State Farm, had become the largest writer of both automobile and homeowners insurance. State Farm is now the nation's largest property and liability insurance company in terms of premiums, with 6.4 percent of the total market. Allstate is second with 5.5 percent of the market.[2]

Direct writers as a group have enjoyed a much higher growth rate than the agency companies. The Stanford Research Institute reported that the market share of the direct writers increased from 9 percent of the total property and liability insurance market nationally in 1947 to 19 percent in 1965.[3] By 1969 their share of the national market had increased to 30.3 percent.[4] A Florida study showed an increase from 6.3 percent of the state market in 1949 to 30.3 percent in 1969.[5] A later study showed that the direct writers had captured 31.9 percent of the national market and 34.5 percent of the Florida market in 1972.[6]

All-Lines Groups

While rising to preeminence in the property and liability insurance market, Allstate and State Farm were among the pioneers of another change which foreshadowed the movement of life insurers into the property and liability insurance market. Both State Farm and Allstate formed life insurance affiliates at a relatively early time. State Farm Life Insurance Company, founded in 1929, had become, by 1972, thirteenth among the nation's 1,800 life insurance companies in terms of new insurance issued, twenty-first in terms of insurance in force, and fortieth in terms of total admitted assets. Allstate Life Insurance Company, founded in 1957, had risen to fifteenth in terms of new insurance issued, twenty-fourth in terms of insurance in force, and eighty-ninth in terms of assets.[7] Nationwide Life Insurance Company, founded in 1929, and Country Life Insurance Company, founded in 1928, also are affiliates of direct writing property and liability insurers.

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[1] John C. Burridge, "Personal Auto: An Analytic Comparison of Market Share," *Dialogue 3*, Special Issue, 1972, published by Insurance Company of North America.

[2] "Insurance Premium Distribution," *Best's Review*, Property/Liability Insurance Edition, July, 1973, p. 10.

[3] Stanford Research Institute, *The Stanford Report*, (New York: National Association of Insurance Agents, 1967), p. 2.

[4] Tom C. Johnson, "Facts are Stubborn Things," an address before the Florida Association of Insurance Agents, Miami Beach, June 12, 1970, p. 2.

[5] J. Finley Lee and John R. Lewis, *Market Dynamics in Property and Liability Insurance: The Florida Report*, (Tallahassee: Florida Insurance Education Foundation, 1970), p. 25.

[6] "Bend in Trend," *Agents Confidential*, June 22, 1973, p. 2.

[7] "Leading Life Insurer in Three Categories," *Best's Review*, Life/Health Insurance Edition, May, 1973, pp. 42-43.

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The success of these direct writers in selling life insurance through property and liability producers did not go unnoticed by the other property and liability insurers. In the last half of the decade of the fifties, when competition and overly restrictive regulation eroded profit margins in property and liability lines, the managements of many property and liability insurers viewed entry into the life insurance business as a means of increasing their profit, and of offsetting the cyclical nature of property and liability insurance earnings. One study found that 24 property and liability insurance groups entered the life insurance business in 1957 and 1958, and 28 additional groups followed in 1964 and 1965.[8] By 1973 all of the top 100 property and liability insurers had formed or acquired life insurance affiliates.

Developments in Life Insurance

Several other developments in life insurance marketing which were taking place during the post World War II period also influenced the movement of life insurance companies into the property and liability insurance field.

Three of the nation's largest life insurers and many smaller ones were heavily dependent on industrial life insurance and other life insurance sold by the debit system. Industrial life insurance, which was introduced into the United States in 1875, was designed to make available to low income people a small amount of life insurance with premiums payable in small amounts, collected weekly at the home of the insured. The premium payment method was, and is, convenient for persons with low income and little skill in budgeting. This premium collection system is very expensive, however.

Several factors combined in the post-war period to erode the market share of industrial life insurers in major parts of the country. First, rising incomes and greater financial sophistication, combined with the lower cost of ordinary life insurance, and the easy availability of monthly debit ordinary, caused large segments of the industrial insurance market to move up to ordinary insurance.

Second, frequent increases in coverage under the social security program reduced the need for the very small amounts of insurance usually purchased through the industrial insurance system. Finally, group life insurance, purchased through and frequently paid for by employers, expanded rapidly. In 1940 group insurance accounted for only 13 percent of all life insurance in force, while industrial insurance accounted for 18 percent. By 1971 group insurance accounted for 39 percent of all life insurance in force, while industrial insurance accounted for only 3 percent.[9] An increasing amount of monthly debit ordinary insurance offset part, but by no means all, of the loss of the industrial market.

[8] Joseph Earnest Johnson, *The Movement of Property-Liability Insurer Groups Into Life Insurance,* unpublished doctoral dissertation submitted to Georgia State University, 1971, pp. 19, 21.

[9] *Life Insurance Fact Book 1972* (New York, Institute of Life Insurance, 1972), p. 25.

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It should also be noted that, in many cases, the insurers who lost the industrial business were writing the group business. However, this fact did not eliminate all of the problems arising from the decline in industrial life insurance. First, the profit on group life insurance usually was lower than the profit on industrial and ordinary insurance. Second, the insurers which had been engaged heavily in debit marketing had invested many millions of dollars in building large forces of debit agents. The erosion of the debit system threatened to make uneconomic the continued maintenance of this marketing force.

Political and Economic Developments

Many of the major life insurers also write large amounts of health insurance, both group and individual. In 1971 all insurance companies combined wrote $22 billion of health insurance premiums. Blue Cross, Blue Shield and similar organizations wrote an additional $10 billion.[10] Life insurers alone wrote $13 billion of health insurance premiums in 1971.[11] As the nation moved toward universal health insurance the future of much of this business seemed doubtful. While some of the national health insurance proposals would permit the continued participation of private insurers, others would transfer virtually all medical expense coverage to the government.

Even more pressing, though possibly less severe, is the pending development of prepaid group medical care plans, sometimes called health maintenance organizations or HMOs. With labor unions pressing for more HMOs, and with the federal government investing large sums of money in their development, it seems likely that these institutions will be major factors in the medical care system in the very near future. Many insurers are helping to finance and organize HMOs in the hope that they can participate in the development by furnishing management assistance, marketing services and reinsurance.[12] The permanence of the service arrangements seems questionable, and the insurers must still consider themselves threatened with the loss of much of their health insurance business. No-fault automobile insurance laws also may reduce the health insurance premiums, and transfer some of that premium income to property and liability insurers.

The Conglomerate Movement

Changes in business organization also contributed to the movement of life insurers into property and liability insurance. Prominent among them were the development of the conglomerate form of organization and the

[10] *1972-73 Source Book of Health Insurance Data*, (New York, Health Insurance Institute, 1973), p. 5.

[11] *Life Insurance Fact Book 1972*, (New York, Institute of Life Insurance, 1972), p. 7.

[12] Arch B. Edwards and William L. Horton, "Health Maintenance Organizations: The Strategic Issue Facing Insurance Companies," *Best's Review*, Life/Health Insurance Edition, May, 1973, p. 24.

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rediscovery of synergy with its magic formula of two plus two equals five. In fact, two plus two sometimes exceeded five if the accountant performing the addition possessed a sufficiently fertile imagination.

The conglomerate movement offered ambitious financiers a means of building extremely large enterprises without running afoul of traditional antitrust policies, because the companies grew by acquiring small shares of many markets rather than a large share of a single market. The bull stock market and investor infatuation with the conglomerates made it easy for them to grow through acquiring smaller corporations by exchanging the overvalued conglomerate stock for the stocks of the smaller firms.

The conglomerate movement affected insurance marketing in at least two ways. First, several conglomerates acquired control of insurers, especially property and liability insurers, in order to use their liquid assets and cash flow to support other acquisitions. This development was greatly encouraged, if not started, by an analysis of the property and liability industry published by an investment banking firm in August, 1967.[13] Property and liability insurers were easy prey for the conglomerates because the insurer stocks were then selling at less than their net asset value, while the conglomerate stocks were selling at very high prices. Insurers which did not want to be taken over by conglomerates found it desirable to establish their own conglomerates through holding companies. Through diversification and sophisticated financial public relations, they raised prices of their own stocks to the point that they were no longer attractive targets for conglomerate takeover.

Perhaps an even more important effect of the conglomerate movement was the widespread acceptance of the idea that management skill is independent of the line of business. That is, the idea that a good manager can manage one kind of business as well as another. This theory was in marked contrast with the old theory that a manager should start at the bottom of the firm and learn all facets of the business as he climbed to the top. One observer has credited this theory, along with "the psychedelic accountant, and the go-go fund", with responsibility for the great merger movement of the 1960s.[14] The theory of scientific management cut the insurer managers loose from their traditional restriction to their own industry and permitted them to expand into other fields, particularly into other areas of finance.

In the meantime the concept of one-stop financial shopping brought new faces to insurance marketing. This concept seems to have been created by property and liability insurers and their agents as a means of easing the

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[13] Edward Netter, *The Financial Services Holding Company*, (New York: Carter, Berlind, & Weill, Inc., 1967, reproduced in United States Senate, Subcommittee on Antitrust and Monopoly of the Committee on the Judiciary, *The Insurance Industry: Hearings*, part 15 (Washington: U. S. Government Printing Office, 1970), pp. 9573-9591.

[14] Lewis Beman, "What We Learned From the Great Merger Frenzy," *Fortune*, April, 1973, p. 144.

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effects of the low profits and severe competition of the last years of the 1950s and the decade of the 1960s.

Many property and liability insurers formed or acquired mutual fund management firms, premium finance companies, and other financial organizations. They were followed by the banks and one-bank holding companies, which, among other things, wanted to enter the insurance and mutual fund business.[15] The number of one-bank holding companies in the United States grew from 117 in 1954 to 1,116 in 1969. Banks controlled by one-bank holding companies controlled 32 percent of all commercial bank deposits in 1969, as opposed to less than 10 percent in 1954.[16]

Investment brokers also sought to enter the life insurance business to even out the cyclical nature of their business, and to provide a means of supporting their sales people during periods of slow market activity.[17] Most of the brokerage firms merely acted as brokers for established life insurance companies, but at least one large investment brokerage firm has expressed an interest in establishing its own life insurer.[18] The investment brokers, like the property and liability insurers and the one-bank holding companies, want to become financial department stores.[19] It would seem inevitable that life insurers, pressed by new competition and unfavorable political and economic developments, also would seek to diversify.

Life Insurer Responses

In the early years of the movement toward broad financial services organizations, some of the nation's largest life insurers were unable to own property and liability insurer affiliates because of the restrictions of New York law.[20] However, the New York law was amended in 1962 to permit such affiliations.[21] In 1971 the laws of both New York[22] and New Jersey[23] were changed to permit life insurers to engage directly in the reinsurance of aviation risks, without the necessity of establishing a property and liability affiliate.

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[15] See United States Senate, Committee on Banking and Currency, *One-Bank Holding Company Legislation of 1970: Hearings,* 2 volumes, (Washington: U.S. Government Printing Office, 1970).

[16] Charles P. Salley, "1970 Bank Holding Company Amendments: What Is Closely Related to Banking?", *Monthly Review: Federal Reserve Bank of Atlanta,* June, 1971, p. 98.

[17] See "Marketing Life Insurance Through Stock Brokers," *Insurance Stock Review,* August, 1972, pp. 7-9; and Sidney Fish, "$200 Million Life Cover Sold by MSE Members," *Journal of Commerce,* November 29, 1971, p. 2.

[18] "The Month In Brief: Merrill Lynch Eyes Insurance," *Best's Review,* Life/Health Insurance Edition, April, 1973, p. 5.

[19] Frederick Andrews, "Hungry Brokers: Securities Firms Seek to Diversify to Offset Stock Market's Cycles," *The Wall Street Journal,* December 19, 1972, p. 1.

[20] Adelbert G. Stroub, Jr., Ed., *Examination of Insurance Companies,* (New York: New York Insurance Department, 1953), Vol. 2, p. 292.

[21] *1962 Laws of New York,* Chapter 627.

[22] *1971 Laws of New York,* Chapter 977.

[23] *1971 Laws of New Jersey,* Chapter 144.

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The movement of large life insurers into the property and liability insurance field began in 1962 shortly after the New York insurance laws were amended to permit such action. In June of that year the Connecticut General Life Insurance Company purchased control of Aetna Insurance Company, a major agency company. In the same year, the Lincoln National Life Insurance Company, which did not operate in New York and was not affected by New York law, acquired control of American States Insurance Company. In 1968 State Mutual Life Assurance Company of America became the first large mutual life insurer to enter the property and liability field, through its acquisition of the Hanover Insurance Company. None of these acquisitions caused much concern in property and liability insurance circles because the acquired companies continued to operate through their traditional agency marketing channels.

The entry of the largest life insurers into the business of aviation reinsurance caused only slightly more concern, because the added capacity they provided was badly needed to provide the coverage required by the newer jet aircraft. Only a few reinsurers worried about the possibility of price instability resulting from the increased competition by inexperienced insurers.[24]

The real shock to the property and liability industry came with the announcement in 1970 that the Prudential Life Insurance Company would launch a subsidiary company to sell automobile and homeowners insurance through Prudential's 25,000 life insurance agents, a sales force more than double the size of State Farm's 11,000 man sales organization. John Hancock Mutual Life Insurance Company announced its entry into the property and liability business at about the same time. The Hancock has approximately 13,000 agents.

The Prudential Property and Casualty Company began operations in 1971 in Illinois. Prudential has approximately 1,500 agents in Illinois, as compared to approximately 800 for State Farm. John Hancock launched its new operation in Indiana and Ohio. It has approximately 500 agents in those states, compared to approximately 850 for State Farm.[25]

More recently, the Metropolitan Life Insurance Company, which has approximately 24,000 agents, has announced its plans to enter the property and liability insurance business. Marketing is expected to begin in January, 1974.[26] The National Life and Accident Insurance Company, with approximately 7,000 agents in 25 states, has purchased control of Service Casualty

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[24] "Reinsurance Offices Association Annual General Meeting: Mr. J. A. S. Neave's Address," *Reinsurance*, July, 1972, pp. 111-113; and "A Leading Lloyd's Underwriter Speaks His Mind," *Reinsurance*, February, 1973, p. 435, 436.

[25] The number of agents for Prudential and John Hancock were taken from *Best's Insurance Reports: Life and Health*, and from Priscilla S. Meyer, "Mutual Life Insurers Expanding Coverage To Product Liability, Factory Fire, Airline," *The Wall Street Journal*, February 3, 1972. The agency figures for State Farm were taken from *Leader's Digest*, the 1971 annual report of the State Farm Companies, pp. 11, 208, 209.

[26] "Metropolitan Life Planning to Enter Property-Liability," *The Wall Street Journal*, September 22, 1972, p. 2.

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Company, which was formerly a subsidiary of C.I.T. Financial Corporation.[27] Both Metropolitan and National plan to sell property and liability insurance through their life insurance agents.

American General Group has announced that the agents of its Nashville-based life insurance affiliates will sell property and liability insurance for Maryland Casualty Company, another of its affiliates.[28] American National Financial Corporation has formed a property and liability subsidiary, American National Property and Casualty Company, to sell property and casualty lines through the 6,500 man life insurance sales force of American National Insurance Company.[29]

The Equitable Life Assurance Society of the United States has announced that it is seriously considering entry into the property and liability insurance field. If it decides to enter the field, it probably will sell automobile and homeowners insurance to groups, rather than making individual sales through its life insurance agents.[30]

Reasons for Life Insurer Responses

The large life insurers have mentioned several reasons for entering the property and liability insurance field. An officer of Prudential Property and Casualty Insurance Company has suggested three reasons. First, an integrated all-lines management and marketing system is attractive to both the public and agents. Second, Prudential will realize a greater return on its investment by operating a property and liability company than by merely investing its assets in a company operated by others. Third, the large property and liability insurers had entered into competition in the life insurance market.[31] The first reason mentioned above seems to be at least an implication that the need to provide an additional source of income for its life insurance agents was a major factor in Prudential's decision to enter the property and liability insurance field.

Another large mutual life insurer, in an internal memorandum, has listed the following reasons for its plan to enter the property and liability market: (1) to earn a greater income on its investment funds, (2) to protect its employee benefit business against all-lines insurers who can offer a complete package, including automobile and homeowners coverage, (3) to hedge against loss of its group health insurance business to a national health insurance plan, (4) to diversify its product line, and (5) to employ more efficiently its administrative, technical and marketing organizations. This company, like the Equitable, plans to market personal

[27] "The Month in Brief: Two More Life Companies to Enter P/L Field," *Best's Review*, Property/Liability Insurance Edition, September, 1973, p. 6.

[28] Ibid.

[29] "The Month in Brief: American National Enters P/L Field," *Best's Review*, Life/Health Insurance Edition, November, 1972, p. 5.

[30] "Equitable Life Plans Airline Insurance Through Pooling Plan," *The Wall Street Journal*, February 22, 1972, p. 11.

[31] Leroy J. Simon, "Why the 'Rock' Moved Into Property-Liability," *The Journal of Insurance*, July/August, 1973, pp. 21-25.

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lines property and liability insurance on a group or quasi-group basis to its many group life insurance, group health insurance and pension customers.

Operating Results

Very limited information is now available concerning the early operating results for the property and liability affiliates of the Prudential and John Hancock. In 1972 Prudential Property and Casualty Insurance Company reported direct premiums written of $5.367 million, and net premiums written of $61.041 million,[32] indicating reinsurance assumed of approximately $56 million. It reported a loss ratio of 72.2 percent and a combined loss and expense ratio of 108.3 percent. However, the loss ratio for direct business was only 65 percent for automobile insurance and 54 percent for homeowners insurance.[33]

The property and liability business produced by Hancock agents is written by Sentry Insurance and reinsured by Hanseco, Inc., a subsidiary of Hancock. In 1972 Hanseco reported written premiums of $1.353 million, a loss ratio of 106.7 percent, and a combined loss and expense ratio of 178.6 percent.[34]

The Hanseco results would be highly unsatisfactory for a mature property and liability insurer, but are not particularly surprising for the initial operations of a new insurer. It appears that both Prudential and Hancock are at least reasonably satisfied with the operating results. Both have announced expansion of their property and liability operations to additional states.[35]

Reaction of Property-Liability Insurers

The reactions of property and liability insurers to the invasion of their markets by the major life insurers, with few exceptions, have been very mild. One group of property and liability insurance agents has launched an investigation of the development, with the possibility of eventual legal action to deter the large mutual life insurers from entering the property and liability insurance market.[36] The President of Insurance Company of North America has termed the movement of life insurers into property and liability insurance a major threat to the property and liability agency system.[37] However, his statement should be viewed as an attempt to

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[32] 1973 *Argus F.C.&S. Chart,* (Cincinnati: The National Underwriter Company, 1973), pp. 112, 113.

[33] These loss ratios were furnished to the author by Mr. Martin Albaum, Director of Research, Prudential Property and Casualty Insurance Company.

[34] *1973 Argus F.C.&S. Charts,* pp. 152, 153.

[35] "The Month in Brief: Pru, Hancock to Expand Their P/L Markets," *Best's Review, Life/Health Insurance Edition,* June, 1972, p. 5.

[36] "Mutual Life Probe Voted by NAMIA," *Journal of Commerce,* March 23, 1973, p. 2.

[37] "As INA's Mail Plan Defended: New Prudential Entry Scanned," *Journal of Commerce,* September 26, 1972, p. 1A.

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defend new marketing methods introduced by his own company, rather than an attack on the life insurers.

It also should be noted that Insurance Company of North America is one of the major property and liability insurers that entered the life insurance business in the late fifties. Its life insurance affiliate, Life Insurance Company of North America, ended 1972 with $5.75 billion of life insurance in force, placing it, by that measure, fifty-ninth among the nation's 1,800 life insurers.[38] The parent company has invested approximately $50 million in its life subsidiary since 1957.[39]

Conclusion

The entry of large life insurers into the property and liability industry appears to be the result of long term developments in both life and multiple-line insurance marketing, along with social, political and economic changes. Three of the largest life insurers, and several smaller ones have already announced their entry into the property and liability market. Others are expected to follow.

Both the sales and underwriting results for Prudential Property and Casualty Insurance Company have been impressive. Limited information now available indicates that the Hancock has been less successful, both in sales and in underwriting. However, the available information is not adequate to support any firm conclusions.

The effective employment of the many agents of the debit life insurers seems certain to increase competition in the property and liability insurance market, and to accelerate the erosion of the market share of the traditional property and liability agency companies. The group and quasi-group marketing of personal lines property and liability insurance by the large group life insurance underwriters also may furnish new competition for the independent agents. The agent associations are, of course, aware of the potential competition and are acting to try to prevent or meet it.

In any case, current trends seem certain to reduce the traditional separation of life and multiple-line insurance operations in the United States. Perhaps insurance people of all lines will begin to think of the insurance industry as a single industry, and to face its problems with a more united front. If so, the industry may profit in the long run in spite of the current unsettled conditions of the market place.

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[38] "Leading Life Companies in Three Categories," *Best's Review*, Life/Health Insurance Edition, May, 1973, pp. 42, 43.

[39] *INA Corporation 1972 Annual Report*, p. 21.

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