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BANCASSURANCE CONCEPT FROM THE PERSPECTIVE OF MONTENEGRIN MARKET*

Milijana Novovic Buric **, Vladimir Kascelan***, Sasa Vujosevic****

ABSTRACT

Integrated services of financial institutions contribute to the quality and development of financial markets. The collaboration of banks and insurance companies through the bancassurance model, as the distribution channel of insurance products, results in reduction of business risk and costs of market research and achieves better profitability and other mutual benefits which have a positive effect on the performance of the insurance and financial markets. More specifically, the effective implementation of bancassurance provides benefits to banks, insurance companies, and to their customers.

Although bancassurance has development perspective on the Montenegrin market, the paper will prove that adequate education and motivation of employees in the banking sector, as well as the adequate demand for this type of financial services, are necessary for its successful implementation. The purpose of this paper is to show the current trend of banks entering the insurance market in Montenegro and to point out the perspective and development problems of bancassurance in Montenegro.

Keywords: financial services, banks, insurance sales channels, bancassurance, insurance market

JEL: G22

INTRODUCTION

Insurance product distribution through banks is becoming present in the process of deregulation and globalization of the financial market. Bancassurance occurred as a result of the simultaneous goal of insurance companies to reduce sales costs and increase revenues and banks to achieve an additional income and expansion of financial services, where clients were given the opportunity to use services of banks and insurance at the same place. In the situation of global drop in profit, conglomeration, oligopolization, as well as market segmentation by large financial groups, banks are becoming more oriented to the integration with insurance companies, motivated by higher business profitability in the first place, but also by the expansion of the financial service they offer to their clients. In order to reduce transaction costs and strengthen competitive positions, some insurance companies can use and combine different sales channels depending on institutional solutions. Distribution channels through agents, Internet, banks and media are often combined.

Bancassurance has a forty-year-old tradition and the similarity between bank business and insurance business could be best observed in France. At first, bancassurance was mostly realized in the field of sale of life insurance policies (term insurance) in order to secure home loans and other bank loans. Later, the products of simpler technology of property insurance were introduced too (casco insurance, home insurance, travel medical

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insurance etc.), and at the end of the 1980s, the sale of unit-linked policies as well. At the beginning of the 1990s, banks begin more intense over-the-counter sales of life insurance, when the European Union (EU) brings the First Directive on the sale of non-life insurance through bank channels.

Since bancassurance has a high potential in the markets with low insurance penetration and limited choice of distribution channels, which is typical for the developing markets, its successful application can be expected in Montenegro, especially when it comes to simple insurance products compatible with banking services. Also, the amendments and changes of the Law on Insurance of Montenegro from August 2012 created legal conditions for the implementation and development of bancassurance in Montenegro.

Many studies on bancassurance focused on the benefits that can result from the cooperation of banks and insurance companies. Bergendahl (1995) cites several economic reasons why banks sell insurance, while Baumol et al. (1982) do not find benefits for insurance companies from consolidation with banks. Saunders and Walter (1994), Hughes et al. (1999) showed that consolidation of banks and insurance companies reduces business risk and banks achieve higher cost advantage from the sale of insurance products than insurance companies. However, Carow (2001) argues that the prices of bank shares are not significantly changed after bank's integration with the insurance industry. Although many studies have shown that bancassurance is a profitable strategy for a bank as a partner in the business, there is no solely opinion on whether insurance companies gain significant benefit or cost advantage by selling the products through the bancassurance channel (Chank et al., 2011).

Although there are no significant studies dealing with key success factors of

bancassurance, Benoist (2002) proposes three golden rules for its successful implementation. These are: a) bancassurance is successful if the model is adjusted to the context of banks and the insurance companies business, b) it is essential to managing key success factors such as quality, innovation, short time penetration and selling of new products to market, advanced technology and low costs and c) strengthening cooperation with customers.

Researchers have definitely shown that bancassurance provides significant benefits to customers. Bente and Ghilimei(2008) indicate that the reduction of distribution costs leads to a reduction of insurance price. On the other hand, introduction of new products is certainly better adapted to the needs of clients (insurance deposits, loans, etc.) in relation to those products that banks and insurance companies launched independently.

Based on a survey conducted by Price Waterhouse Coopers & Economist Intelligence Unit (Insurance Advocate 2000), it can be concluded that the key success factor of insurance company, which plans to do diversification of its sales through the bancassurance channel, is the ability to develop new innovative insurance products.

The aim of this paper is to show the level of bancassurance development in Montenegro, as well as the key factors that limit or contribute to its further development. The research was done on the territory of Montenegro where 120 people, employed in banks and insurance companies, were surveyed.

1. MODELS AND SPECIFICITIES OF BANCASSURANCE

In a narrow sense, bancassurance represents distribution of insurance products through a bank, while in a broad sense, it can be defined as a model of integration of banking and insurance market in order to connect and control the whole process of emission and

distribution of life and non-life insurance products. Although the relation between banks and insurance companies in a way that banks undertake obligations from insurance and create insurance products is not allowed, different product distribution through these financial institutions is becoming present in the process of deregulation and globalization of financial market. A bank can join the sale of insurance products based on the agreement of distribution with the insurer, through joint venture, but also through the financial conglomerate to which the bank also belongs, but which has evolved either from merger or acquisition, as well as from the establishment of an insurance company or a bank. (Ćurak & Jakovčević, 2007).

Bancassurance based on the agreement of distribution implies the situation in which a bank acts as an intermediary offering products of one or more insurance companies. This type of bancassurance is typical for the sale of simple and standardized products. Within this model, or even especially (Bancassurance, 2008), the model of Strategic Alliance can be extracted, in which banks sell products exclusively for an insurance company. Strategic Alliance is an agreement between banks and insurance companies for the joint use of distribution channel. In this model, the advantage of a bank is the possibility to choose the best insurance company in terms of product quality, image and etc. At the same time, a bank informs the insurance company about its important clients, which both institutions could have benefits from. The shortcoming of the model is a low level of integration between banks and insurance companies. The cooperation

within the framework of strategic alliance does not result in the loss of organizational and functional independence of partners. Cooperation leads to attracting new customers, enabling partners to maintain competitive advantage in the financial market. The main risk of the model is insufficient sale due to a relatively low level of formalized cooperation. Banks certainly gain experience in the field of insurance and for them it can be assumed that this model is a phase that leads towards a strategy of creating their own insurance companies.

According to joint venture model of bancassurance, banks and insurance companies strengthen their cooperation through management coordination, sharing a client database, as well as through the joint development of the products. Specifically, this model achieves the joint ownership of products and customers and long-term cooperation. The essence of joint venture is fund allocations of banks and insurers with the goal of creating a legal and independent organizational entity which has to realize defined business objectives.

The next model of bancassurance includes the offer of different financial services through the integration of institutions, mergers or acquisitions, and very often through a holding company for financial services. In this business model, a holding company owns the insurance company and bank, and it is often called financial conglomerate. The potential benefits of this model are full integration of processes and systems, access to existing bank clients, provision of financial services in one place, as well as the possibility of developing fully integrated financial products.

Table 1.1. Bancassurance models

	Specificities	Benefits	Disadvantages	Representation
Agreement of distribution	Bank as an insurance agent	Simplicity, low start-up costs and no capital investment	Less flexibility of supply, possible conflict of business cultures	Germany, Great Britain, USA and Japan
Joint venture	Join ownership of customers and products. Strategy of bank and insurers consolidation.	Exchange of databases, transfer of knowledge and experience	More complex management in the long term	Italy, Spain, Portugal
Integration model	Acquisition or bank or insurance companies establishment	Integrated business, unique business culture	More investment and higher capital risk	United Kingdom, Ireland, France, Spain, Belgium

Source: Fiordelisi F., Ricci O., (2012): Bancassurance in Europe, Past, Present and Future

In practice, there are various hybrid models of bancassurance, so it is possible to give them a different classification. For example, models can be viewed on the basis of income source of banks participating in the business of bancassurance. Besides the provision, there are also specific profit-sharing agreements signed between bank and insurance company. Bancassurance can also be viewed through the integrative model, the specialist model and the financial planning model (Dumm & Hoyt, 2003). In the integrative model, insurance product distribution is carried out through the existing bank channels and with the help of bank clerks. In the specialist model, insurance products are distributed by product experts who are usually employed in insurance companies or represent them. The financial planning model is a bancassurance model which is characterized by team approach and through which every client is offered a possibility to use an overall package of financial services in order to satisfy individual financial needs. Every model must be compatible with the bank's database of clients

and the strategic goals of the insurance company.

Regardless of the analyzed and applied bancassurance model, it is important to define the joint strategy and standards of evaluation of business cooperation. Realized premium per insurance product is among the most important indicators of insurance sales success through banks, as well as average premium per bank clerk, the number of cancelled insurance contracts, and the income from the commission for every counter officer in the bank.

The combining of bank and insurance services in one financial institution, brings multiple benefits to both institutions. Banks expand their area of operation and they are especially interested in life insurance, while insurance companies can offer their products through banks in the market with lower costs (Novović & Purić, 2011). The acceptance of bancassurance as a sales channel stems from different motives of bank, insurance company or clients. The product diversification method and the source of additional income from

commissions are the key motives of banks, while insurance companies see bancassurance as a way to increase total revenues, improve the penetration into the market itself, and as a better access to the client database. For clients, bancassurance represents a special benefit in terms of reduced prices of high quality products, but also a possibility of more efficient delivery of products, or the so-called home delivery (Ostojić, 2011).

Bancassurance, especially life insurance due to high commissions charged by insurance agents, is a more efficient distribution channel than through agents. Through this product distribution model, insurers have the access to the bank's client database, which gives them the possibility to create products harmonized with the needs and possibilities of clients. Further, the market segment which is not available in other distribution channels is here available for insurers, enabling the increase in sale, i.e. the increase in the revenue from the insurance premium.

With distribution of insurance products, banks improve their profitability. Close relationship between the bank and the client contributes to the increase in profitability based on bancassurance business, and the reputation banks enjoy among a significant number of financial services users, which is stimulating for the purchase of insurance products offered at bank counters. Banks also realize the access to potential buyers thanks to widespread bank branches and owning large databases for the assessment of clients'

needs and possibilities. It is estimated that bancassurance makes up 20-30% of the total revenues of leading European banks in this business (Ćurak, 2007).

The advantages of bancassurance from the aspect of banks are reflected in avoiding dismissals of the employed due to the development of information technologies. Bancassurance expands the activities of the bank, gradually building them into financial supermarkets satisfying those clients who prefer realizing all or a larger part of financial services in one institution.

2. BANCASSURANCE IN DEVELOPED EUROPEAN MARKET

According to different economic, social, political and cultural environment of certain countries, the experiences worldwide in the field of development and usage of bancassurance are different. Analyzing the European market, it can be observed that banks are a significant distribution channel of life and pension insurance. More specifically, a sale of life insurance through banks is present in Australia, South America, Central and Eastern Europe.

The following table shows the representation of selling insurance products through bancassurance.

Table 2.1. Bancassurance, sales of insurance products in Europe and the Anglo - Saxon markets

	Eastern Europe	Central Europe	Western Europe	Anglo-Saxon markets
Countries	Lithuania, Croatia, Bulgaria, Turkey	Poland, The Czech Republic, Slovakia, Slovenia	Austria, Belgium, The Netherlands, Italy, France, Ireland, Spain, Portugal	Great Britain, Denmark
Dominant type of offer	Simplified low price offer of life insurance	Simplified low price offer of personal insurance	Simplified low price offer of life and non-life insurance	Total offer of life and non-life insurance

Source: Ernst & Young (2010), Bancassurance: a winning formula

Bancassurance accounted for over 70% of the total sales in Turkey, Italy and Spain. In these countries, the second important sales channels were agents who generated over 10% of the insurance premium. Bancassurance was not the dominant sales channel in Slovakia, the Netherlands, Ireland and Bulgaria. In Slovakia and Ireland the sale was most generated by insurance companies (37% and 59%), while in the Netherlands and Bulgaria by agents (74% and 39.3%).

Portugal. Brokers dominate in the UK, Belgium and Bulgaria, while direct sales in the Netherlands, Finland and Croatia.

According to the data from Figure 3, domination of bancassurance regarding the sale of life insurance in the countries of Western Europe compared to other insurance sales channels can be observed. In Portugal, Turkey and Italy, about 70% of the total life insurance premium in 2012 was realized through bancassurance, while it was least represented in Germany and Sweden in the same year. In East European countries

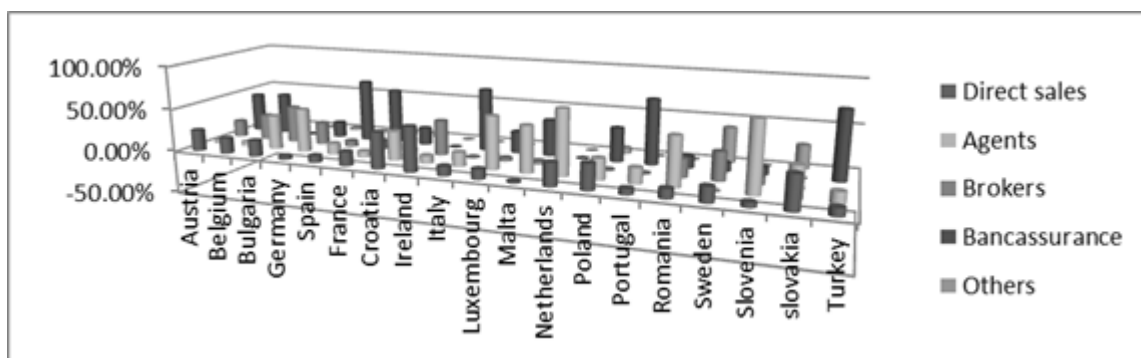


Figure 2.1. Distribution channels in selected European countries in 2012

Source: European Insurance, Statistics no. 50

Distribution of non-life insurance through banks is less represented in Europe, where agents and direct sales channel are dominant. Agents are the biggest suppliers of non-life insurance products in Germany, Italy and

according to the dynamics of development of life insurance, bancassurance as a sales channel did not have a significant share in the total sale of life insurance. The share of sold policies of life insurance through banks in 2012 amounted to 13.6% in Romania and 20% in Croatia. Like in non-life insurance,

agents and brokers played an important role in the distribution of life insurance products in East European countries.¹

The best results of sale of non-life insurance through banks were achieved in Turkey, Portugal (more than 14%). These are certainly the countries where bancassurance is the most significant sales channel for life insurance as well. Figure 2 shows that the premium of non-life insurance was not collected through banks in Slovakia, the Netherlands, Malta, Ireland and Bulgaria. Figure 3 shows that bancassurance accounted for more than 70% of life insurance premiums in Portugal, Italy, Turkey and Spain, more than 60% in France and more than 40% in Austria, Belgium and Malta.

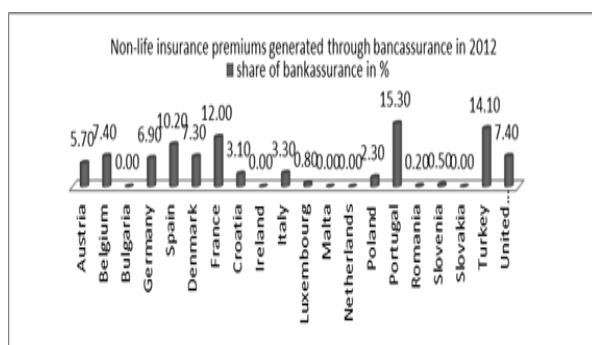


Figure 2.2. Non-life insurance premiums generated through bancassurance in selected EU countries in 2012

Source: *European Insurance in Figures, Statistics no. 50*

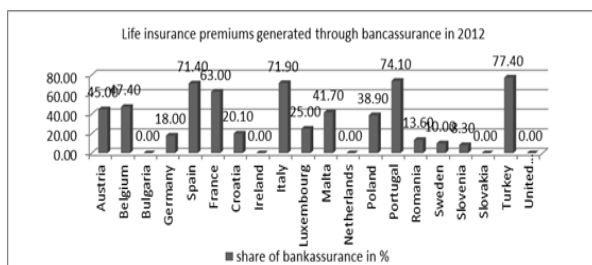


Figure 2.3. Life insurance premiums generated through bancassurance in selected EU countries in 2012.

Source: *European Insurance in Figures, Statistics no. 50*

If we analyze Croatia and Slovenia, as the countries of the former Yugoslavia and now members of the EU, we can notice that the share of sold policies of life insurance through banks was about 20% in Croatia and 8.3% in Slovenia, while the percentage for non-life insurance was 3.1% and 0.5%. Analyzing countries in the region, Slovenia and Croatia have most success in bancassurance. In Serbia, bancassurance has been applied since 2006, in Bosnia since 2009, while in Montenegro since 2012.

3. BANCASSURANCE IN MONTENEGRO

The amendments and changes of the Law on Insurance of Montenegro from August 2012 created legal conditions for the implementation and development of bancassurance in Montenegro. The conditions for a bank to act as an agent in insurance are defined by the Insurance Supervision Agency of Montenegro (ANO), which brought the Rulebook on Terms of Granting Approval to Banks to Act as Insurance Agents in January 2013. Bancassurance can be carried out by banks which have an operation license issued by the Central Bank of Montenegro (CBCG) and the approval of ANO, i.e. agency activities in banks can be carried out only by persons employed in the bank, who own a license to act as agents in insurance.

A bank in Montenegro, which wants to act as an agent in insurance, must in its business premises visibly mark the place where the business is carried out and display the name of insurance company which it represents. Also, work place must have adequate computer equipment and software support for the agency business in insurance. On the bank's premises where the agency business is carried, a printed list of all insurance companies with whom the bank has an agency agreement, must be displayed in alphabetical order, including the types of insurance offered in the bank. The bank acting as an agent in insurance can distribute promotional material

only for insurance companies with whom it has an agency agreement. For this job, the bank cannot realize additional revenues aside from the commission revenues.²

The role of banks as agents in insurance is very modest in Montenegro, since only four banks have received work permissions so far (Societe Generale Montenegro, Atlas Bank, Hypo Alpe Adria Bank and Hipotekrana Bank). All banks were licensed in 2014, when they began to work. During 2015, the registration of two new banks can be expected. The gross written premium generated by the banks amounted to €130,000, which is 0.19% of the total market gross premiums in 2014. Banks concluded 971 insurance policies, 426 life insurance policies and 545 non- life insurance policies in 2014.³

Banks did not have special interest to represent insurance companies until the expansion of term insurance which is used as collateral for consumer loans in Montenegro. Recognizing the benefits that bancassurance gives, both through operating revenues and income realized on the basis of provision, banks have launched the process of integration with insurers. The most sold product through bancassurance in Montenegro is a term insurance, which serves as collateral, primarily for consumer and cash loans, and then for mortgage and housing loans. Products of property insurance, used as a security instrument when buying property on credit, are also sold through bancassurance in Montenegro.

Experience has shown that the integration of banks and insurance companies results in reduction of business risk, strengthens the market position and achieves better business results. Analyzing Montenegrin financial market, a need for integrating banking and insurance products is noticed in the field of credit insurance, life insurance sales through bank counters, for providing certain benefits to existing bank customers when taking

insurance, as well as for providing benefits to consumers of insurance in certain banks, which use bank's services. Montenegrin banks that are licensed for insurance agents mainly offer term insurance and property insurance as the security for loans. Hypo Alpe Adria Bank is the first bank in Montenegro which started to offer insurance products to their customers. Out of all loan packages, the most important are: ⁴

1. Cash loans for employees- include job loss insurance and disability insurance over 50%.
2. Cash loans for retirees- include accidental death insurance and death insurance due to illness
3. Housing and Mortgage Loans - include term insurance, or beneficiary of the loan must be insured for the time of its repayment.

Hypo Alpe Adria Bank offers contents insurance (as a separate policy or related to a credit), as well as casco and travel insurance. Also, it is important to stress that all items of leasing contracts must be insured.

In order to analyze the potential of bancassurance in Montenegro, a survey which included employees of the insurance sector and banking was conducted. Out of a total of 150 questionnaires sent, 30 were invalid, so we analyzed the responses of 120 participants. The survey covered 64% of respondents aged 25-40 and 36% of those aged 40-60 year. Out of those surveyed, 72% have higher education and 28% secondary education, while 60% of the respondents were male and 40% female.

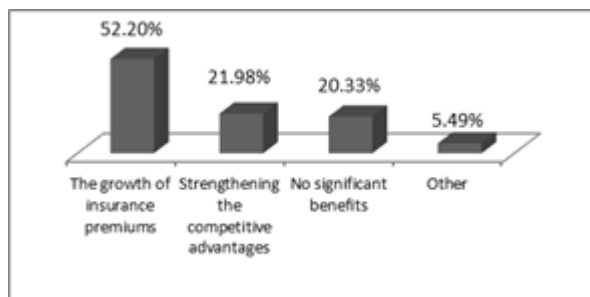


Figure 3.1. Bancassurance benefits for banks

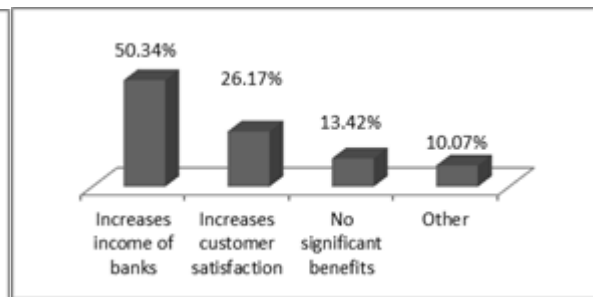


Figure 3.2. Bancassurance benefits for insurers

Figures 3.1. and 3.2. show the most important benefits of bancassurance for banks and insurance companies. The attitude of over 50% of the respondents was that the most important advantage of bancassurance is the growth of the commission fee income (for banks), and the growth of the insurance premium (for insurers). The opinion of 13.4% of the respondents is that bancassurance does not provide significant benefits to banks while 20.3% of the respondents believe that bancassurance does not give particular benefit to insurance companies. Specifically, the survey results suggest that bancassurance provides significant benefits to banks in relation to the insurance companies.

Limiting factors of bancassurance development from the aspect of banks and insurance companies are shown in Figures 3.3. and 3.4.

The respondents (54.24% of them) consider that the poor purchasing power of citizens is a key economic factor that slows the growth of bancassurance. The lack of interest of clients to buy insurance through banks also negatively affects the development of bancassurance in the opinion of 26.55% of the respondents while distrust to financial institutions influences the further prospects bancassurance (19.21%). It should also be noted that bancassurance has prospects of further development in Montenegro regarding

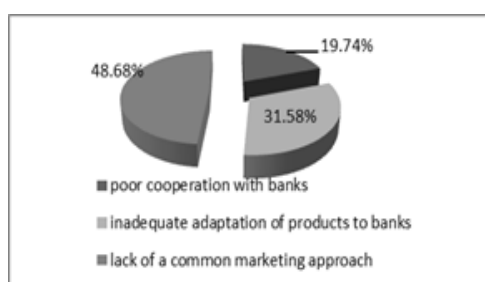


Figure 3.3. Limiting factors –banks

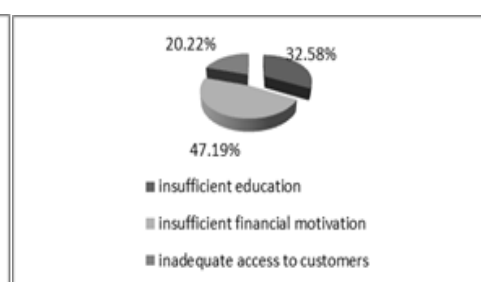


Figure 3.4. Limiting factors – insurers

the opinion of more than 60% of the respondents.

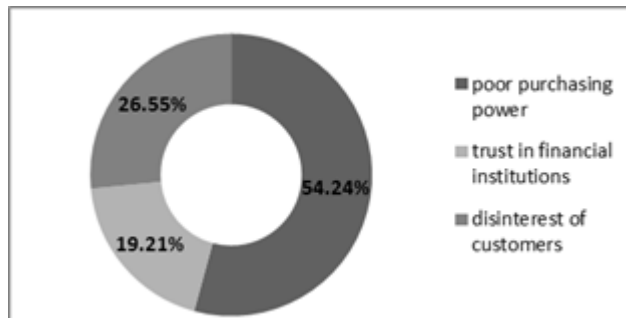


Figure 3.5. Other limited development factors

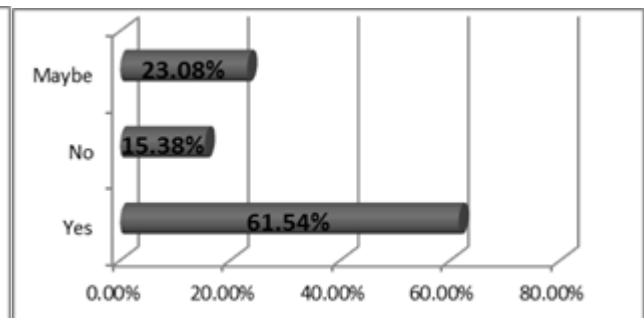


Figure 3.6. Perspective of bancassurance

Bancassurance has a potential in the Montenegrin market especially regarding simple products, compatible with the services of the bank, such as life insurance, for example. The fact is that it cannot be expected from Montenegrin citizens to go to banks in order to buy an insurance product. Therefore, it seems more realistic to observe the prospects of bancassurance in Montenegro through connected purchase, i.e. a loan and insurance, deposit and insurance etc. It can be understood if there is a professional relation between the personal banker and the client, when all financial needs and possibilities which can be realized in the same bank are pointed to the client.

In order to implement the specified, it is necessary to have adequate education of bankers about the importance and characteristics of insurance products that are offered. In Montenegro, bankers who offer insurance products have to be licensed by the Insurance Supervision Agency. The question is whether the acquired knowledge (with the aim of getting the licence) is sufficient for the successful insurance sales. Bankers also have to be motivated to sell insurance products.

The integration of insurance products into bank products means an easy way of selling, due to the fact that clients accept to conclude insurance contracts more easily together with another financial product, especially when it comes to a loan arrangement (lower interest rate if life insurance is concluded too, etc.)

(Šker, 2012). Through approved loans, clients can also be offered different insurance products, such as fire insurance (home loan), motor vehicle liability insurance and casco insurance (car loans), travel and medical insurance (payment cards), etc. For the Montenegrin insurance market, bancassurance is certainly very important because the growth of the insurance premium can be expected, especially taking into account the fact that banks have a better rating among Montenegrin citizens than insurance companies, and that buying insurance in a bank lowers the pressure exerted on citizens in telephone selling and through agents and brokers.

Besides the mentioned advantages, banks and insurance companies are facing the certain problems. In order to successfully introduce bancassurance, it is necessary to adapt information systems, for example programs for sale of insurance products, but also to enable training of bank employees due to insufficient knowledge of the specifics of insurance products. Costs of education of employees represent one of the limiting factors for selling modern and more complex insurance products through banks. In contrast to intermediaries and other representatives, bank employees do not receive a commission for every product sold, which is not a stimulating affect to sales of insurance products. Also, due to the possibility of greater channelling savings into the insurance sectors of not the banking sectors, the bank may have

a passive approach to the sales of insurance products. Reputational risk is also present in bancassurance. If customers are dissatisfied with the method of sum insured payment or the actual amount of the compensation, mistrust or leaving the bank may appear, which negatively affects the rating of the bank.

Analyzing the achieved results in the first year of bancassurance in Montenegro, as well as the tendency of already integrated banks and insurance companies to further promote this distribution channel, a penetration of other Montenegrin banks to insurance market could be expected.

Conclusion

Successful application of bancassurance in Montenegro in the following period can be expected if both banks and insurance companies recognize multiple advantages of this sales channel. Personal bankers are expected to play an important role in the promotion and development of bancassurance in Montenegro. They are supposed to be motivated by their managers to carry out these operations. In order to provide the prospects for bancassurance in Montenegro, compared to other sales channels, it is necessary to set up a joint strategy of presentation of simple insurance products in the financial market. Banks and insurance companies should jointly work on the planning of sale and marketing of insurance products, in order to provide a successful sale service. A continued education of the personnel is also necessary in banks, which would certainly improve the sale of insurance products.

Bancassurance enables the expansion of insurance company's portfolio with the reduction of product distribution costs compared to traditional sales channels. For the development of bancassurance, it is necessary to adjust insurance products to the needs which are coherent to the needs of bank

clients, and further to identify and educate professional staff who would be entrusted with the insurance service distribution. Precisely, a bank officer has an access to the information about client's financial capabilities, they get to know their wishes and needs, and according to this, the client can be advised about the choice of insurance services in a more quality way, which is certainly a benefit for the client and it saves time and costs compared to individual conclusion of an insurance contract.

From the aspect of globalization of financial markets, banks and insurance companies have to be observed as two inseparable sectors whose perspective primarily depends on the key factors which determine development of the financial market (economic growth and development, liquidity of the economy, purchasing power of citizens, etc.). In addition to a greater number of insurance services and accessibility, dispersion of operational risk and profitability of banks, bancassurance will contribute to the development of the Montenegrin financial market, as well as to the savings growth and competitiveness of the market economy.

¹ European Insurance in Figures, Statistics no. 50

² Pravilnik o bližim uslovima za obavljanje poslova zastupanja u osiguranju u bankama, Agencija za nadzor osiguranja Crne Gore, član 5.

³ Report on Insurance Market in Montenegro for 2014, Insurance Supervision Agency

⁴ www.hypo-alpe-adria.co.me

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