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Alternative Distribution Channels in India

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1. Introduction to Distribution

1.1.Definition of Distribution channel:

A set of interdependent organizations involved in the process of making a product or service available for use or consumption by the consumer. The objective of the distribution is to create place utility, the value of having the products where the customer wants them, when they want them. Distribution has two aspects: logistics and strategy.

Channels of Distribution are what has always traditionally been called "Place" in the 4 P's model of Marketing. Distribution Channels provide the utility of *place*; of having products *where* the customer wants *when* the customer wants them. The terms *Place* and *Channels of Distribution* are synonymous

1.2.Construction of purchase decision in Insurance

Insurance Industry must view customer needs in a holistic manner, considering the market as a whole .The Industry must target overall financial management of the population. Consumer education should be appropriately structured. Industry must take into account consumer differences and should have system in place to deal with different levels of sophistication of the customer. The Industry should be aware that customers' demographic characteristics affect their expectations and needs.

The rational model of consumer behavior assumes that individuals will follow behavior based on rational economic analysis to buy any thing. But the evidence in practice does always not support such rational assumptions: individuals often make their decisions on *non-rational* grounds. They use rule of thumb measures, their cognitive biases affect their perceptions, and their decisions are based on habit, or on what people they know are doing.

1.3.Distribution in Insurance:

Distribution in Life Insurance requires the intermediaries to have prerequisite qualification, adequate product knowledge and communication skills. The intermediaries are required to assess risk for the Insurer and also serve the Consumer till the final settlement is made.

1.4.Market situation up to privatization

The Agency channel was the only channel catering to the needs of the market. It was generally felt that there were demand side as well as supply side gaps in the Agency channel. The Life Insurance Intermediary did not enjoy a professional image and was found inadequate and not keeping with the expectations. Finally, IRDA came out with new Regulations with effect from 14.07.2000.The Regulations introduced Composite Agency enabling the Agents to do both Life and Non-Life Business. Corporate Agency and Broker channels were opened up.

2. Need for alternative distribution channels

2.1. Financial Liberalization

The liberalization of national financial and capital markets; coupled with the globalization of national economies has catalyzed financial innovation and spurred the growth of cross- border capital movements. The regulatory authorities in many countries have altered rules governing financial intermediation to allow a broader range of institutions to provide financial services and thus new classes of non-bank financial institutions have emerged. The Insurance (amendment) Bill, 2002 passed on 23.09.2002 provides for setting up of Cooperatives exclusively for carrying on Insurance business. The cooperatives would be subject to some paid up capital requiremens, deposits with RBI and other regulations concerning accounts and audit.

2.2. Cost advantages

The existing two-tier structure needed a relook and use of technology with agency channel was poor and inadequate. Besides, the levels of service were poor not consistent with the costs. To maximize reach in the market place, many insurers are aiming to derive channel advantage because each channel has unique strengths. For e.g., a direct sales force is usually optimal for complex, high cost transactions where face-to-face interaction is expected and required. Brokers and Corporate Agents can dramatically expand market reach through local access and penetration. The Internet can be used to get the message out to untold millions, at an extremely low cost.

The companies that choose and cleverly integrate the right mix of channels can build go-to-market systems that respond optimally to each of the requirements of the products and markets. They can, for example, use expensive sales force representatives only to acquire and grow the most important key accounts. They can then use brokers to reach dispersed groups of smaller customers and to provide local sales support. They can use call centers to close simple sales, generate sales leads for other channels and follow up on direct mail campaigns. They can use the Internet to reach customers who prefer to serve themselves and want to save money. These efforts add up to a huge competitive advantage in terms of revenue growth, market reach, customer loyally and higher productivity. Experience shows better averages in terms of policy size, first premium per policy and first premium per Rs.1000 sum assured.

2.3. Advances in Information & Computer technologies:

The integration of voice and data enabled entry of interactive voice response system (IVRS). The policyholder can manage his policies through his facility. The website, though initially started as a spin of, became interactive enabling the policyholders to know product information, calculate the premium quotes, know the premium position and various other benefits and redress grievances. The touch screen kiosks have been introduced to create awareness of the products and for servicing. The metro area networks and the wide area networks facilitated payment of premium anywhere and provided access to policy information anywhere in the country. As a result of the above initiatives the customer has become ever more informed, demanding and intervening in the purchase decision-making. The market became highly segmented and warranted multiple channels to exploit it.

2.4. Multiplicity of channels and insurance penetration

(i) " One size fits all" service model does not work any longer. This realization in the minds of the Government and the Consumers shall surely help improve the Life Insurance penetration.

(ii) The numbers tell the story: The latest Tillinghast-Towers perrrin survey of Insurance CEOs reveals that

- Distribution effectiveness and productivity is seen as the number one strategic issue facing the industry.
- Technology is the number one "weapon of choice" for tackling distribution challenges.

Other results are:

- Captive agents premium share dropped 7% from 1989 to 1999.
- Top producers who leave for independent agencies today do so 50-60% sooner than a decade ago.
- Change in the distribution system is one aspect of Regulation and Development of Insurance Industry in India. The new relationships are in the nature of Joint ventures rather than traditional relationship that usually exist between Insurance Intermediaries & Insurers.

2.5.Effectiveness of new distribution channels

Though intended for Banking, the following steps suggested by Shri Vepa Kamesam, Dy Governor, RBI at 25th Bank Economists Conference 2003 held on 12.12.03 are relevant for Insurance Industry.

(i) Understand customers' current channel transaction behavior and their underlying attitude.

(ii) Use sophisticated experimental customer research to assess the economic impact of tactics designed to change that behavior.

(iii) Develop an integrated channel integration plan which blends, economic and non-economic incentives are targeted at the right customers.
(iv) Design channels to emphasize personalized interaction.

2.6. Valuation of Distribution channels – current and alternatives.

It is of academic internet to know from a paper published by society of Actuaries on Actuarial Appraisal value in connection with acquisitions of Life Insurance firms,. It is argued that the value of new business is designed the measure and make a provision for the company's ability to produce new business, as well as take into account any franchise or brand value. The value is calculated using risk discount rates. Here distinction is made between installed distribution capacity and alternative distribution channels. It is observed that determining the value of alternative distribution channels is a delicate balance. While a seller may provide significant opportunities in the form of an existing client base, installed distribution, capacity or name recognition, buyers will not want to pay for value they feel they create with their intellectual and technical capital. Presented well, this sort of exercise can unlock significant value on behalf of the seller.

2.7.Issues of managing multiple Channels:

Distribution can remove the company further away from the end consumer whose needs and requirements are to be understood by the Insurance Company. Therefore, all the following issues from design to alignment with the company will have to be taken care of.

- Channel design - Using service output demands
- Investment and strategic direction
- Optimizing your channel structure to meet end-users' demands
- Identifying and managing conflict between channels
- Integration of channels and communication between channels
- Problems with one channel should be capable of being solved thro'other
- Different brands products and different brand strategies needed for different channels.
- Company to have programs, policies, procedures in place to serve policyholders coming from different channels.

3. Regulation

3.1. Eligibility:

3.1.1. Eligibility for agents:

- The eligibility was made 12th Standard for all places with population of 5000 and 10th standard for all other places.
- Training of 100 hours (with a relaxation for the qualified people and 150 hours in the case of composite agents who can do life as well as general business) was mandated as a prerequisite for issue of License.
- Training of 25 hours practical training has also been introduced for renewal of license for all new agents.

3.1.2. Corporate agents:

- Definition of corporate agent includes a firm, a company founded under the Companies Act 1956, Banking company as defined under the said act or a cooperative society including a cooperative bank registered under cooperative societies act of 1912, NBFC registered with RBI, Panchayat or a local authority or NGO or a micro lending finance organization under cooperative society Act or any Board or Institution recognized by either central or state Government.
- Specified person or the corporate insurance executive to have the same qualifications applicable to the individual agent and undergo the requisite training.

3.1.3. Brokers:

Minimum two employees of the broker who can be a proprietor, firm, corporate should have the basic eligibility qualifications like Associateship exam of Insurance Institute of India or equivalent.

3.2. Market conduct norms

It is for the first time that a code of conduct for the Agents was prescribed by the Regulator. The regulations recognized that agent is acting on behalf of the insurance company and not the policyholder as has been argued in many legal cases hither to. The Regulation recognized that selling should be need based. Now the agent is under duty to disclose all possible choices for the given premium and help the prospect to choose appropriate plan. He should also disclose his commission to the prospect and all material information to the insurer. The conduct norms are the same for Corporate insurance Executives, Specified person and Corporate Agents. The conduct norms for Brokers have been given on similar lines.

3.3. Restrictive provisions

The agent should not induce the prospects to submit wrong information and vomit any material information. He should not offer different rates advantages, terms and conditions other than offered by the insurer.

4. The history so far

The statistics of Alternative Distribution channels of LIC suggest that corporate agencies including banks are garnering 82% and the rest 18% is coming from Brokers. The international experience shows that Bancassurance is able to get major chunk as the time passes by as can be observed from the following table.

Country	Share	Top Players
France	56%	Credit Agricole,Caisses d'espargne,BNP
Germany	4%	Deutsche
Italy	45%	Roma Vitae, Assiba, Mediolanum Commercial, Union Vita
Netherlands	20%	ING,Fortis,Rabobank
Spain	73%	BSCH,LaCaixa,BBVA,Seguros,Caja Madrid
UK	9%	Lloyds Bank,Barclays Bank,Royal Bank of Scotland

(Source: Business Standard 'Banking Annual' November 2002)

Even the statistics of Private insurers suggest similar trend as under

Company	Share of Corporate Agents including Banks	Key banks tied up with
ICICI Prudential	28%	ICICI Bank, Federal Bank, South Indian bank, Bank of India, Lord Krishna Bank
HDFC Std. Life	14%	HDFC Bank, Union Bank of India, HDFC Ltd, Indian Bank
Birla Sun life	24%	Citibank, Deutsche Bank, IDBI Bank, BNP Paribas, Catholic Syrian Bank, Development Credit Bank, Bank of Rajasthan and Bank Muscat
SBI	17%	State Bank of India, Associate banks of SBI, 20 Regional rural banks
Allianz Bajaj Life	20%	Standard Chartered Bank, Syndicate Bank

LIC tied up with Corporation Bank, Central Bank of India ,IOB, UCO Bank, Bank of Punjab, Oriental Bank of Commerce and fourteen cooperative Banks. Over time bancassurance may get at least 20% share.

5. Thinking of e-commerce

5.1.The information technology act-enabler

The Information Technology Act was passed in 2000 to facilitate e-commerce. The Act comprises of three significant aspects:

- Legal recognition of electronic records and communications - contractual framework, evidentiary aspects, digital signatures as the method of authentication, rules for determining time and place of dispatch and receipt of electronic records.
- Regulation of Certification Authorities ("CAs") - appointment of a Controller of CAs, grant of licenses to CAs, duties vis-à-vis subscribers of digital signature certificates, recognition of foreign CAs.
- Cyber contraventions - civil and criminal violations, penalties, establishment of the adjudicating Authority and the Cyber Regulatory Appellate Tribunal, etc.

If the product is simple and sufficient consumer awareness of Life Insurance products exists in the market, the products can be offered through the net with significant cost savings.

5.2. Early movers

Birla Sun Life Insurance Company Limited (BSLI) launched its e-commerce portal to enable purchase of an insurance policy through its website. This is the first offering of its kind by a life insurance company in India to offer the purchase of life insurance on the Internet. A scientifically designed process termed as the “3 Step Process” has been created to assist the customer in the purchase process. The first step in this process helps the customer understand the life insurance requirements, identify the right plan and explain the features of the recommended plan. The next step is the application process where the policy illustration is created and the application form is completed. The final stage is the payment page from where the customer can buy the policy online using credit or debit card. After the customer pays the premium, a BSLI Insurance Officer will meet with the customer within 48 hours to collect the age proof and get the signature on the application form and the policy illustration. In the first phase, the Birla Sun Life Flexi

Secure Life Retirement Plan (without life cover) and Birla Sun Life Single Premium Bond are being made available for online purchase.

6. Conclusion:

Customers still rely heavily on Individual Agency channel. Alternative distribution channels have given competitive edge for the Insurers. It is apparent that multiple distribution channels will help an insurance company to offer a range of contact points to the customer, thereby increasing the chances of success.

The Individual Agent including Corporate Agent, though explains all options, is tied and has to sell the policies of the company he is representing. Brokers are in major cities and the concept is yet to take off. With these channels the costs may not come down but the customization may go up. It is also to be noted that the customization of the product has not reached individual level but only segment level.

Along with these distribution channels come various challenges. Effective management of channel conflict, and curtailing the costs of distribution will be of utmost importance. The importance not only remains on how many channels a company currently has, but on how those channels work and interact with each other in a cost effective manner giving a single view of the Organization and Unified experience to the customer.

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