

IEA THE FUTURE OF LIFE ASSURANCE

How can the industry deliver what customers really need and want?

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Narrative

Title slide

Good morning ladies and gentlemen. I am delighted to be here this morning and I look forward to some lively debate later on. Before that, I've been asked to speak briefly about how can the industry deliver what customers really need and want. But part of the problem is in the title...

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... it assumes that customer needs and customer wants are one and the same. But the needs and wants of customers are not aligned. This list is by no means exhaustive, but it gives a flavour of what we know to be true. In our culture of celebrity, people want their jam today, not jam tomorrow. They want to believe that their lives will be sunshine every day, whereas we know they need to plan for those rainy days.

They want longer leisure time, yet they need a longer working life to afford any leisure at all. They want to believe that the State will support them – after all, they've paid their taxes! But we know the demographics. We know that the State can't afford anything like what they want, and therefore financial independence is really what they need. And we know that people want financial security – never to have any money worries – but what they need is good, dependable financial advice, because without it, they will not take the right decisions at the right time.

The challenge is that people tend to base their financial decisions on the here-and-now rather than on their future needs. This leads to a culture of spend now, save later. But when the saving bit comes round, there tends to be nothing left. The culture needs to be one of save now, spend later.

I know these are ballpark figures but about half of UK adults don't have any life or income protection, and about a third have no retirement savings beyond the state provision, even though about 80% of pre-retired people don't believe the state pension will give them the standard of living they hope for. We can argue the statistics but no-one questions the general truth that people need to be encouraged to plan for their retirement years.



That's why the latest budget decision to curtail tax relief was so disappointing. It sends out completely the wrong message to pension savers. Tax relief on contributions was a way of the Government saying to everyone, and I mean everyone, irrespective of earnings, that 'saving for your pension is a good thing and we will encourage it'. Now that contract has been broken, and if it can be broken for one segment of savers now, it can be broken for others sometime later. It also adds cost and complexity to pensions. All round, it was a poor decision that will hinder progress towards restoring the save now, spend later culture.

So this is the dilemma. We know what people need to do, but we also know that they don't want to do it.

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I think this quote from President Eisenhower sums it up well. His challenge then is our challenge now. "How to get people to do what I want them to do and to get them to do it because they want to do it." I believe that we as an industry have to show greater leadership as to how we can help people break the cycle of their current circumstances determining their financial decisions.

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But Eisenhower also said, "You don't lead by hitting people over the head – that's assault!" Frankly, many feel that our industry has done just that – hit them over the head. Let us just take a moment to see things through the eyes of our customers.

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The very people who financial services exists to serve are, right now, feeling a combination of heartache, lost, confused, angry, let-down, resentful, miserable, and a host of other feelings on top. They've seen the value of their money fall, whether it be invested in savings accounts, in their homes, in investment vehicles or in pension arrangements. Many now realise that the level of expertise behind their decision to opt for default funds is not what they thought it was. In Boardrooms they have seen greed applauded and failure rewarded, and to make matters worse, they then saw their money used to bail out those responsible. Their confidence in financial services is at rock bottom. And it's not their fault. We need to change. We need to restore our reputation.

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I believe we need to look backwards as well as forwards, or to quote the film title, we need to go back to the future. I received a seminar invitation recently and the first words of the email designed to grab my attention were these; "how to look ahead without looking back". I'm sorry, but I don't agree. As a famous philosopher once said, "Those who cannot remember the past are condemned to repeat it".



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Our industry took its eye off the ball in recent years. The Embedded Value accounting system didn't help with its over emphasis on new business and new business profits. The industry became mesmerised by new business, writing it at too high a cost. Acquisition costs were unsustainably high. Product complexities were designed and concealed commission, and poor sales behaviour was condoned rather than stamped out. Our hunger for ever increasing new business numbers was insatiable. Just like people at large, our short-term wants overrode our long-term needs. We all did it!

Banks too transformed themselves from strong, stable, safe, solid deposit taking and lending institutions into high-risk, easy-credit, sales-orientated organisations. And the rest, as they say, is history.

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If there is a silver lining to all of this, it is exploding the myth that a debt-based culture is the way to live. Having quoted a US President from the past, let me quote the one who, to a large extent, will determine our future. Barack Obama just a couple of months ago said, "An economy built on reckless speculation, inflated home prices and maxed-out credit cards does not create lasting wealth. It creates the illusion of prosperity and it endangers us all." The illusion of prosperity has now been well and truly exposed as a wolf in sheep's clothing, and not before time. It does not deliver what it promises. One message people need to hear loud and clear is that things will never return to how they were before this crisis. We are entering a new financial era.

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However, part of the new era should include aspects of a much older one. I know these rules of conduct for employees – 1872 do the rounds from time to time, but nothing has changed in the last 137 years to make rule Number 6 obsolete. "Every employee should lay aside from each pay day a goodly sum of his earnings for his benefit during his declining years so that he will not become a burden to society." It always was good advice to plan for your retirement years, and it always will be. And that's amazing considering how times have changed since 1872. The very next rule, for example, says that any employee who smokes Spanish cigars, drinks liquor or gets shaved in a barber shop will give good reason to suspect his worth, intentions, integrity and honesty! I don't think that's still office policy at Friends Provident but I'm going back to check!

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These things may make us smile, but the hard reality is that the financial services industry is viewed as an industry of questionable 'worth, intentions, integrity and honesty'. Yet I believe passionately that our industry is a worthy one, daily paying more than £200 million in pensions and life assurance claims. It has been my privilege on several occasions to deliver the cheque personally to policyholders, and therefore I know, first-hand, that our industry is able to help real people through real anxieties, but that's not how we are seen.



I read in our latest Corporate Responsibility brochure that there's research showing that more than half of those surveyed believe most financial services firms will mislead customers if they can make more profit by doing so. That's how much of an uphill struggle we face.

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Working in financial services has to be recognised again as an honourable profession. It's my privilege currently be the President of the Chartered Insurance Institute and you may know that the theme I chose for my Presidential year is 'Bringing Professionalism to Life". We need to go back to the future and restore professionalism. This is fundamental to restoring consumer confidence. This must be the industry's public and private face again. Put bluntly, we must attract the right people, dissuade the wrong people and punish the crooks.

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We must restore customer relationships and offer simple products and simple processes. Our relationships with customers must be mutually valued. The 'man from the Pru', for example, was seen as a trusted friend of the family. He would track those key family events and guide the family's financial decisions, providing convenient access to straightforward, affordable products. That model of course is no longer affordable or appropriate, but we have to find workable ways of achieving the same outcome. Our products are still too complex. Some need to be but others don't. I believe there is an appetite to re-introduce simple, easy-to-understand, easy-to-buy products. We need transparent products that do what is expected.

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Although not universal by any means, certain enlightened employers in days gone by shared the responsibility for the financial wellbeing of their employees. Don't forget that those office rules of 1872 were from the employer, not the life office. I'm not suggesting employers should take on this responsibility, but I do believe that we should restore workplace opportunities. Many employers would be happy to accommodate initiatives from us to use the workplace as a means of helping their employees manage their money better and guiding them at appropriate times towards decisions that are sound and sensible.

It may sound like I'm advocating a return to a bygone era, and in part I am, but this must be coupled with a determination to leverage every kind of modern medium and advancement in communications and behavioural science, to engage with customers in ways that work for them.

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In looking ahead I think there is a real opportunity to communicate in ways that customers use.

Last year, the CII did some work to examine the financial behaviour of 18 to 34 year olds, referring to them as the IPOD generation – Insecure, Pressured, Over-taxed and Debt-ridden.



What I found striking was that this generation possessed the highest potential for appreciating the value of financial advice, yet didn't benefit from it. Their preferred way of communicating and purchasing doesn't fit with how our industry does it. We need to bridge the gap between what we do and what customers prefer. Whether it means selling through social networking websites or some other vehicle that they use and we don't. It's our responsibility to reach them, not their responsibility to reach us. We live in an age when an unknown lady can sing a song on a TV programme and, a week later, over 100 million people have seen it on You Tube and it has become the most popular topic on Twitter! That's communication!

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We also have to be sure that our process designs reflect the ways that customers behave. Two examples, both related to selecting investment funds: Firstly, this financial crisis has made people realise that investing in default funds, as most people do, does not mean that, behind the scenes, there is a financial expert looking after their individual interests. It's no wonder these people now feel let down. Knowing this must make us think what we do about it. There is a good deal of innovative thinking out there about the design of default funds, or the development of target dated funds, that we must draw on, so that opting for a default position represents a sound investment decision.

Secondly, science tells us that the more fund options you offer customers – previously thought to be a good thing – the more likely customers are to be confused and opt for the default, which has led us to restructure how we present our funds to our customers. There is an enormous array of scientific research into how people behave, and we have to find ways of integrating behavioural science and innovative thinking into process design to help customers make good decisions at a good time. But even better would be to reduce the number of decisions required.

Take company pensions as an example: A long-serving member of staff at Friends Provident had to make no decisions at all regarding his or her pension. Membership of the pension scheme was not optional but an accepted condition of employment. The contribution rate and the benefits were linked to salary, so as salaries rose, so did the savings and the benefits. The retirement age was fixed, and there was a formula that kicked in if the person wanted to retire early or late.

Compare that to today. Employees have to decide when and if to join the defined contribution scheme, how much to contribute, taking account of employer matching opportunities, which funds to invest in, when and whether to switch, what impact the recession is having on their pension pots and what to do about it, as well as when to take the benefits. There was a lot to be said for compulsory membership and, without it, we have to be prepared to do a lot more hand-holding of employees than we do currently.

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Let's look at a quick example of integrating behavioural finance, which has proved that employees are unlikely to increase their pension contributions if it reduces their take-home pay, but they are willing to increase their contributions if the increase coincides with a pay rise that more than



covers the increase. In FP we call this the 'plan for tomorrow' scheme, and this graph illustrates the difference it can make. Very broadly, everything about John and Paul is the same except that John never increases his contributions whereas Paul increases his contributions by 1% each time his pay rises, up to a ceiling of 10%. I'm not expecting you to remember these details, but rather to accept that it's a very normal set of circumstances, yet the difference it makes at retirement is immense, with Paul's fund value being virtually twice as much as John's. It's knowing the behaviours that enable us to help the Pauls and Paulas of this world to make good decisions.

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Looking ahead, our industry must also react to opportunities more quickly as they emerge, to help people when they need it. For example, the credit crunch has magnified the need for protection. Because bad things are happening to more people, more often, people realise that it could happen to them, and are asking themselves: "what if it did?" It's precisely these kind of worries that our industry can shoulder for people. I think the opportunity for promoting the benefits of protection cover is with us right now, especially as I understand that protection cover is probably the cheapest it has been for 20 years. [By the way, I happen to have some application forms with me if you're interested!]

Another good example is the need to design more flexible products for those in the decumulation period of their lives, a period that is not served well by our industry at the moment. This is an opportunity now, and needs to be grasped.

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We must also recognise what hasn't changed. The fundamentals that shaped our industry remain intact. People are still getting married, raising families, taking risks, falling sick, buying houses, losing jobs, needing pensions, and so on. Our industry was needed before the crisis and will go on being needed long after it and, in that sense it is an industry with a long-term future.

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Looking further ahead, 2012 will be a landmark year for several reasons. We must use the run-up to 2012 wisely. One is the implementation of changes resulting from the Retail Distribution Review, which I know that John is going to touch on, so I won't expand other than to say that this is a step change we must get right. We now have a good sense of the direction of travel, but we must use these intervening years to ensure that the changes eventually implemented effectively deliver the original objectives of a step change in professionalism and widening consumer access to financial services. I am a passionate supporter of the financial adviser community. Anything that raises standards of advice still further has to be a good thing, but we must be careful that we don't drive good advisers out of our industry in the process. We must get that balance right.

2012 also sees the introduction of personal accounts, which again is a gold-plated opportunity for our industry to add value, but which could be squandered, depending on the final decisions made. We do have to ensure that all that is good about current pension provision remains intact.



The focus must be in levelling up not down! I believe the current proposals give employers too much opportunity to take short-term decisions that might improve their profits but at the expense of the long-term needs of their employees. I also believe that the government's current stance on meanstesting must mellow. It would truly be a scandal if thousands of workers find out at retirement that they would have been better off had they kept their pension contributions in their pocket.

And what about life cover? People need it, yet it doesn't currently feature in the Government's proposals for personal accounts. Personal accounts give us an opportunity to extend life cover cost effectively. We could do well to look at the Australian model – it's always helpful to listen to Australians! Down-under, employers pay a dollar a week per person for life cover; a cheap way of providing life cover on a falling scale, starting at 100,000 dollars for younger ages and scaling down to 20,000 dollars as the employee gets older. Why not take the opportunity to incorporate something similar here?

Auto-enrolment is another opportunity. If the Government believes it to be a good thing, as we do, then why wait until 2012 to introduce it? As the economy recovers auto enrolment to qualifying company plans could be introduced in advance. What better way to prove its worth. These are huge challenges and they need our focus. We mustn't let the current crisis distract us.

And finally, of course, 2012 gives us the Olympic Games. Important, not only because it should enhance the feel good factor, but also because it will mean that Australia will be restored to its rightful place in the medals table....just above Great Britain!

Thank you.

