Developments in Korea's Bancassurance Life Insurance Market

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The life insurance markets in Korea and Japan share many similarities. Bancassurance, or the sale of life insurance products by banks, was deregulated at around the same time in both countries. Due to the affinity for saving-type products in Korea's life insurance market, bank assurance has performed well from the start. However, recognizing its downside for consumers and life insurers, regulators have pushed back the deregulation schedule.

1. Introduction

When the currency crisis forced Korea to seek an IMF bailout in 1997, life insurance companies were among the casualties. The government injected massive public funds to revitalize banks, life insurers and other financial institutions, and in the process their composition changed drastically. Of the 33 life insurance companies in the life insurance market, 14 went bankrupt by 2003. During this period, Japan's life insurers were also under great duress, with seven going bankrupt, but the situation in Korea was even worse. Korea implemented a sweeping revitalization policy, including significant changes to the supervisory regime for life insurers. On the sales front, bancassurance (Korea adopted the European expression for the sale of insurance products by banks) was deregulated at about the same time as in Japan.

This paper examines the status of bancassurance in Korea's life insurance market, a market which shares many similarities with Japan. In doing so, we hope to find implications for the future of Japan's life insurance market.

2. Market Comparison—Japan & Korea

(1) Similarities

The life insurance markets in Japan and Korea are structurally similar. Both have high penetration rates. By premium income, Korea ranks seventh in the world (Japan is second). But in terms of market penetration rate as measured by the ratio of premiums to GDP, Korea outranks the U.S. (first in premiums) and France (fourth in premiums).

Figure 1 Ratio of Premiums to GDP (%)

Rank (total premiums)		% GDP
1	U.S.	4.2%
2	Japan	8.3%
3	U.K.	8.9%
4	France	6.4%
5	Germany	3.1%
6	Italy	4.9%
7	Korea	6.8%

Source: Swiss Re-Insurance Company, *Sigma* No. 2 (2005).

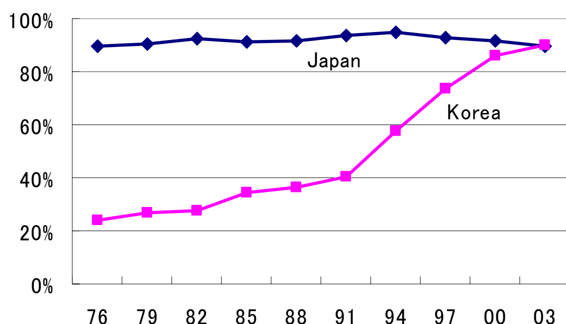
Moreover, Korea has the world's highest household penetration rate in life insurance. According to a 2003 survey, Korea's household penetration rate was 89.9%, slightly higher than Japan's 89.6% rate. In Japan, the household penetration rate drifted downward in the 1990s following the asset bubble's collapse. But Korea's penetration rate rose consistently through the

1990s despite the currency crisis. As a nation, Korea has obviously fully accepted life insurance.

Another similarity with Japan is that the high penetration rate was achieved through a mostly female sales force. While the number of agents has decreased in recent years, they remain the primary sales channel for life insurance.

As of 2006, there are 22 life insurance companies. The market share of foreign life insurers has risen in recent years. This trend is also similar to Japan's market.

Figure 2 Household Penetration Rates



Sources: Korea Life Insurance Association, Life Insurance Business in Korea; Life insurance Culture Center, Japan Institute of Life Insurance, Nationwide Survey on Life Insurance.

Korea's life insurers can be classified into three groups—the big three (Samsung Life, Kyobo Life, and Korea Life), the other nine domestic firms, and foreign firms. From fiscal 2003 to 2004, the big three lost market share to foreign and other domestic firms. The growth of foreign firms has been particularly pronounced.

Figure 3 Premium Income & Market Share

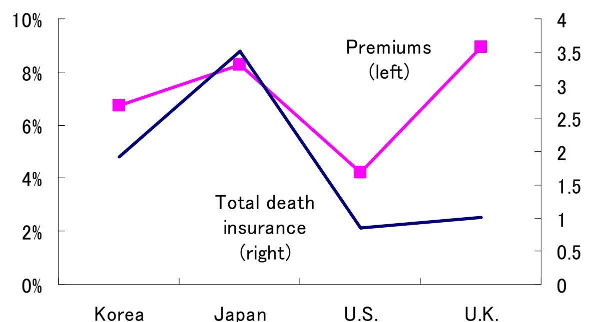
	2003		2004	
	Premium income	Share	Premium income	Share
12 domestic firms	43.6	86.4%	44.9	83.5%
Big three	36.3	72.0%	36.8	68.5%
Others	7.3	14.4%	8	15.0%
11 foreign firms	6.8	13.6%	8.8	16.5%
Total	50.4	100.0%	53.8	100.0%

Notes: Premium income is in trillion won. In fiscal 2005, one firm withdrew, leaving 22 firms.

(2) Differences

The biggest difference is in death protection (Figure 4). Measured against GDP, Korea's total death protection is twice as high as that of the U.S. and U.K., but only one-half that of Japan. This is because Japan's life insurance market has consistently sought growth in protection, while Korea's market resembles the West, where life insurance is used as a form of savings.

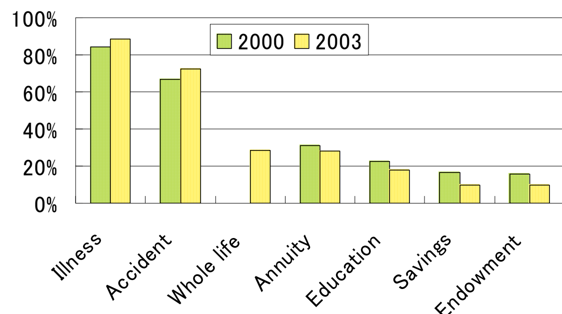
Figure 4 Premiums & Death Protection (as ratio to GDP)



Note: For the U.S. and U.K., insurance amount is for individuals.
Sources: Swiss Re-Insurance Company, *Sigma* No. 2 (2005); insurance associations of each country.

This situation is also reflected in the survey of penetration rates mentioned earlier. By product type, Korea boasts high penetration rates for sickness and hospitalization insurance, and accident insurance. Whole life insurance, which in Japan is the leading type of insurance, has a penetration of almost zero at 0.1% in the 2000 survey.

Figure 5 Penetration Rate by Product

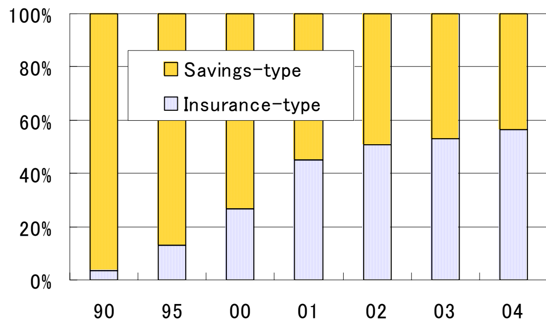


Source: KLIA, *Life Insurance Business in Korea.*

Until the mid 1990s, savings-type products formed the core of Korea's life insurance market. These are products whose benefits before death

exceed premiums paid in. Only recently has attention shifted to death protection. The weight of insurance-type products has grown in recent years.

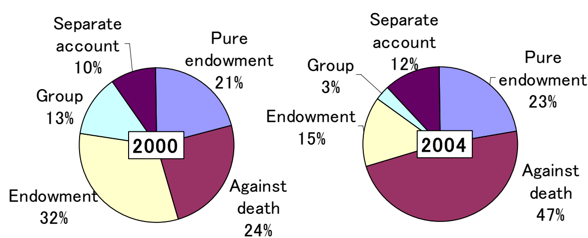
Figure 6 Composition of Premium Income



Source: KLIA, *Life Insurance Business in Korea*.

A more detailed breakdown by product type shows that death protection (whole life, fixed-term, illness, accident, etc.) has grown significantly as a share of premium income. Since death insurance products have a long contract period, they tend to stabilize earnings for life insurers. This factor, along with the economic recovery, help explain the improved earnings stability of life insurers in Korea.

Figure 7 Composition of Premium Income



Source: KLIA, *Life Insurance Business in Korea*.

The new emphasis on products that insure against death was triggered by foreign life insurers, who have targeted wealthy customers and trained male insurance agents to sell whole life insurance products. Their success has prompted domestic life insurers to follow suite.

3. Bancassurance in Korea

Japan began the first phase of deregulation for bancassurance in April 2001. The second phase began in October 2002 for annuities, and the third phase in December 2005 for lump-sum life insurance and endowment insurance policies shorter than ten years. Barring unforeseen problems, full deregulation will be achieved in December 2007.

Meanwhile, Korea has introduced bank-assurance in the manner described below. Significantly, its approach contains regulations not found in Japan, including a minimum limit on the number of insurers collaborating with financial institutions, and a ban on unfair transactions between financial institutions and insurance companies.

(1) Implementation Schedule

Korea started deregulating bancassurance later than Japan. The first phase, which began on August 30, 2003, authorized the sale of credit life insurance and savings-type insurance by financial institutions. In April 2005, third-sector products without maturity repayment (illness, accident, and long-term care insurance) were deregulated. Like Japan's three-phase approach, Korea's approach takes into account the strong sales capability of financial institutions and possibility of unfair competition (as specified in Article 91 of Korea's Insurance Business Law).

Figure 8 Schedule Revision

Initial		Revised	
Aug. 2003	Individual savings-type products ・annuities ・education insurance ・endowment insurance ・credit life insurance	Aug. 2003	Individual savings-type products ・annuities ・education insurance ・endowment insurance ・credit life insurance
April 2005	Individual insurance-type products	April 2005	Third-sector products (no maturity repayment)
April 2007	All life insurance products (including group annuities)	Oct. 2006	Third-sector products (maturity repayment)
		April 2008	Insurance-type products ・ordinary life insurance ・severe illness insurance

Source: KLIA

However, the deregulation schedule—which originally consisted of three phases to be completed by April 2007—has been changed. The deregulation of insurance-type products for

individuals, originally slated for April 2005, was confined to third-sector insurance products without maturity repayment. Third-sector products with maturity repayment will be deregulated in October 2006, and all other insurance-type products, including whole life insurance and products containing insurance for severe illness, in April 2008. Automobile accident insurance for individuals will also be delayed until April 2008. No completion date has been set for full deregulation.

(2) Operating Rules

① Applicable financial institutions

Banks, securities companies, mutual savings banks, and credit card companies are authorized to sell insurance. Entities that already offer services similar to bancassurance, such as the National Agricultural Cooperative Federation and Korea Post, are not included.

② Distribution channels

Financial institutions can offer bancassurance services in three ways: (1) as agents or brokers of insurance companies, (2) by acquiring an insurance company, or (3) by establishing an insurance company as a subsidiary.

③ Partnerships

Large financial institutions with at least two trillion won in assets (approximately 200 billion yen) cannot become exclusive agents of a specific insurance company. In addition, product sales of any one insurance company must not exceed 25% of total insurance sales.[1] As a result, large financial institutions must collaborate with at least four insurance companies. This upper limit had been 49% until it was reduced to 25% in April 2005.

These restrictions aim to prevent large financial institutions from forming exclusive ties with specific insurance companies and thereby monopolize the market. They also aim to offer smaller insurance companies the chance to form alliances with financial institutions. The restrictions do not apply to financial institutions with less than two trillion yen in assets.

④ Sales location

Insurance sales are allowed only at branch offices of financial institutions, and the insurance sales counter must be set up separately from the banking counter. Door-to-door and telephone marketing are prohibited. However, Internet marketing to an unspecified and large number of customers is allowed.

⑤ Sales agents per location

Each sales location can have up to two sales agents (this restriction applies until March 2008).

Sales agents are prohibited from performing other functions such as leasing. In addition, other employees not assigned to sales are prohibited from selling insurance or making referrals.

If a financial institution hires former insurance company sales agents, they are not counted as sales agents under the following conditions: (1) they have at least two years of insurance sales experience, (2) at least six months has passed since leaving the insurance company, and (3) the new employment period is at least one year long.

⑥ Responsibility to consumers

Financial institutions are prohibited from offering loans that require recipients to buy insurance.

In addition, before selling insurance, financial institutions must explain what they can and cannot do as an insurance agency (for example, they must explain that they are acting as the sales agent, and that the insurance risk is borne by the insurance company).

Financial institutions must also inform

[1] If a financial institution owns at least a 15% stake in an insurance company, the sales limit is 33% of total insurance sales.

consumers sufficiently to make insurance purchasing decisions, and receive confirmation from customers that this has been done.

⑦ Unfair financial transactions

Financial institutions are strictly supervised so as not to abuse their dominant position over insurance companies. In an examination of bancassurance, the Financial Supervisory Service found cases of unfair behavior wherein negligent financial institutions (e.g., those who sold insurance without adequate explanation) shifted the responsibility to insurance companies. Regulations have been established to prevent such unfair transactions between financial institutions and insurance companies.

Bancassurance contracts between financial institutions and insurance companies must have a duration of at least three years. In addition, the FSS issues a notice to financial institutions found engaging in unfair transactions such as: (1) applying pressure on the insurance company to invest in or deposit funds at the financial institution; (2) demanding that the insurance company share bancassurance expenses or deploy staff; (3) demanding excessive commissions or unreasonable allocations of insurance company profits; (4) demanding premium discounts for group insurance in which the financial institution is enrolled.

The supervision of sales commissions is particularly strict. The concern here is that smaller insurers and foreign insurers, in seeking larger market share, may sacrifice profitability by offering high commissions to financial institutions or guaranteeing high interest rates on savings-type products. The measure prevents them from offering excessive commissions to financial institutions.

(3) Bancassurance Performance

As of October 2005, 19 of the 22 life insurers had set up bancassurance channels. Measured by initial premiums, an indicator of new contract sales, bancassurance has consistently performed well, capturing a 51.6% share in the inaugural period from September 2003 to March 2004, 46.7% in fiscal 2004, and 49.0% from April to October 2005.[2]

Figure 9 Bancassurance Market Share

9/2003 ～ 3/2004	FY 2004	4 ～ 9/2005
51.6%	46.7%	49.0%

Source: KLIA.

The market share is even larger when we focus on sales of individual savings-type insurance. According to the KLIA, the bancassurance market share from September 2003 to November 2004 (initial premiums basis) comprised 44.5% of all life insurance products, and 66.2% of individual savings-type products.

Figure 10 Bancassurance Market Share (Sep. 2003 ～ Nov. 2004)

	All products	Individual savings products	Banc-assurance
Initial premiums (bancassurance share)	90.3 bil. won (44.5%)	60.7 bil. won 66.2%)	40.2 bil. won
Total premiums (bancassurance share)	651.5 bil. won (7.5%)	278.3 bil. won (17.7%)	49.2 bil. won

Source: KLIA.

Bancassurance has thus exceeded initial predictions calling for a 15 to 20% market share by 2012.

According to a study by the FSS, when third-sector products without maturity repayment were deregulated in the April-June 2005 quarter, 110 financial institutions were engaged in bancassurance (17 banks, 12 securities firms, and 72 mutual savings banks).

Furthermore, despite the deregulation of third-sector products, an overwhelming 99.9% of sales still consisted of individual savings-type

[2] However, we note that since initial premiums do not distinguish between monthly and annual payments, it includes lump-sum products, which comprise a large part of bancassurance, and thus tend to inflate the market share.

products, which were deregulated in the first phase. A large part of this consisted of lump-sum individual annuities, which resembles the case in Japan.

4. Issues

The FSS has conducted several examinations into bancassurance, and found instances of improper sales to consumers and unfair demands being put on insurers. Attributing these improprieties to the market's explosive growth, the FSS decided to revise the deregulation schedule.

In a month-long investigation in October 2004, the FSS examined the head offices of eight major banks, their 66 branch offices, and 11 insurance companies. In addition, they surveyed 3,100 SMEs who had bought insurance from banks. Suspicious banks were identified and further examined. In February 2005, all eight banks were found to have violations and penalized.

The main violations were to require customers to buy insurance as a loan condition, allowing insurance sales agents to make loans, allowing loan employees to sell insurance, and selling insurance without adequate explanation or verifying the customer's identity.

5. Conclusion

The explosive growth of bancassurance in Korea can be attributed in part to familiarity with savings-type products in the life insurance market. Banks are already the primary sales channel for individual annuities in Japan, and financial institutions in other countries have done well selling savings-type products as well.

On the other hand, Korea's financial institutions have not been assertive in third-sector products, with almost no successful cases of banks selling insurance-type products. In the future, Korea's life insurers will need to improve channel management and sell more savings-type products through the bancassurance channel, while selling more whole life insurance products through their own sales network. This will require better training of the sales network for insurance-type products.

In Korea, the style of financial supervision fuses together a European wariness of conglomerates and an Asian emphasis on harmony and protecting small and medium insurers from the abuses of financial institutions. Since banks in Japan also exercise strong dominance over customers, Japanese supervisors should also take into consideration the relationship between financial institutions and insurance companies.