

# Finance & Insurance Sector



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## Industry Overview

The banking system in the US includes combined annual revenues of around \$630 billion generated from approximately 7,000 commercial banks, 1,200 savings banks, and 8,000 credit unions. Large commercial banks include Bank of America, JPMorgan Chase, Wells Fargo and Citibank. Navy Federal Credit Union and ING Direct and are considered to be the largest credit union and savings bank in the US today. The industry is concentrated with the 50 largest institutions constituting more than 60 percent of the market. Commercial banks account for around 81 percent of industry revenue while savings banks account for around 13 percent; and credit unions about 6 percent.

The insurance sector in the US includes around 130,000 insurance agency and broker offices. These offices generate annual revenues of approximately \$85 billion. Large companies include Marsh & McLennan, Arthur J. Gallagher, and Aon. The industry continues to be highly fragmented with the largest 50 firms only constituting around 20 percent of the total Market despite the prominence of large companies in the commercial segment.

## Competitive Landscape

Demand for banking services is closely tied to economic activity and the level of interest

rates. The profitability of individual banks depends on marketing, operational efficiency and rigor risk management policies. Some segments of the industry rely on large economies of scale exist in, which has resulted in some industry consolidation. Smaller banks are typically able to compete in their niche segment by improving customer service or knowledge of the local market. The industry is capital-intensive and highly automated.

Demand for the insurance sector is closely related to consumer income and the commercial activity volume. The profitability of individual agencies depends on effective use of marketing channels. Large agencies have advantages in name recognition, association with more insurers, and the ability to craft more detailed insurance packages. Small agencies can compete successfully by specializing in a product, industry, or market.

## Business Challenges

### *Concentration of Real Estate Loans*

Banks earn a majority of their fees from real estate loans. They hold large portfolios of real estate loans and securities and as the demand for real estate credit decreases, fee income for banks also decreases.



### ***Exposure to Interest Rate Changes***

Due to the fact that many banks make money by lending funds at higher interest rates than they have to pay to acquire funds, bank profits are heavily sensitive to changes in interest rates. When the cost of funds increases, bankers may not be able to increase the interest rates at the same proportion on their outstanding loans.

### ***Stricter Regulation***

State and federal regulators have broadened their powers over bank operations. This included but is not limited to the types of loans and investments banks can make, the amount of interest banks can charge, the amount of capital kept in reserves and a variety of other matters. The current global financial crisis prompted a re-examination of financial regulation and a movement toward tighter regulatory control.

### ***Revenue Depends on Economic Conditions***

The revenue of many insurance agencies is dependent upon economic conditions, especially in property and casualty insurance, because the volume of insurance-related transactions fluctuates. A slower economy generally means fewer new homes built and sold, fewer cars bought, and fewer insurance products bought.

### ***Competition from Direct Sales***

Even though the majority of insurance transactions involve an agent or broker, experts anticipate that less of these transactions will involve an agent or broker because more consumers are beginning to purchase insurance through direct sources. Insurers can easily sell auto and term life insurance, which constitutes the largest volume of insurance business, over the Internet without an insurance agent.

### ***Poor Public Image***

Gaining consumer trust is the single biggest challenge for any insurance agent, especially for independent agents with limited support

from a large company's brand or reputation. The reputation of agents is harmed even further if they represent insurers with financial problems.

## Trends

### ***Industry Consolidation***

Between 2000 and 2008, the number of US commercial banks and savings institutions dropped by 15 and 23 percent, respectively. This is also true for the insurance industry with agencies and insurance carriers, responding to the wider insurance needs of business customers. While the overall number of independent agencies has dropped, the average agency size in terms of revenue has grown.

### ***Renewed Focus on Risk Management***

Excessive risk-taking, primarily related to mortgages and mortgage-backed securities, has led to widespread revenue losses across the US banking industry. There has been a big push from industry leaders for banks to reflect more prudent risk management policies.

### ***Expansion into Non-Bank Financial Services***

US Banks are now able to provide new services to consumers and businesses, including insurance, stock brokerage, and investment management. Demand for such services will increase rapidly as the number of retirement aged Americans increases by more than 50 percent between 2000 and 2020.

### ***Consumers Research Policies Online***

Consumers use the internet to comparison shop, but most still prefer to ask a person questions and close the deal with an agent. Although online insurance sales amount to billions of dollars annually, they are still a small percentage of overall insurance revenue.

### ***Consulting Services***

The increased complexity of financial and risk management gives insurance agents an opportunity to expand their role as an advisors, especially within the commercial segment. For example, there is an increase if insurance agents that providing risk management solutions to small and mid-sized clients who often can't afford a risk manager on their payroll. Insurance agents are using consulting to build stronger relationships, retain existing clients, and attract new ones.