Boomer benefits

David Macchia is the CEO of Boston-based strategic marketing consultant Wealth2k and is widely credited with the marketing vision that turned the indexed annuity industry into a $30 billion a year business in the US. Macchia says structured products will define the future of retirement security in the US. The Structured Products Association's *Negin Janati* asked him how the industry can get out in front of tens of millions of baby boomers as they hit retirement age

> Structured Products Association: You recently stated that the US structured products industry is poised for the type of explosive growth experienced by equity indexed annuities in recent years. What's the rationale for your prediction?

David Macchia: To be clear, I believe that the growth potential for the structured products industry outpaces by a wide margin what we saw occur with equity-indexed annuities. It's all about the importance of the value proposition that can be delivered via structured products to the retail consumer. As financial advisors and consumers begin to realise that importance of properly managing the transition to retirement, they will seek out products that are able to deliver equity-linked growth potential combined with safety of principal.

Over the period that begins, roughly, 10 years before retirement and extends through to 10 years after retirement, it's vital that retirement assets are supported by principal protection. Otherwise, normal market downturns could cause a lifelong reduction in income-generation capacity, if not total portfolio ruin. Is there any risk more important for a retiree to manage? So when I say that there's explosive growth potential for the US structured products industry, it's in the context of this need to manage retirement risk which is shares by millions.

SPA: How do you envisage structured products becoming the dominant investment vehicle for baby boomers and the so-called 'lifecycle' market that's so sought-after by the financial services industry?

DM: This is the key question for the structured products industry. I'd start by looking at the equity-indexed annuity business as a model of what not to mimic. When equity-indexed annuities debuted in 1995 they were relatively simple contracts that provided excellent value to the consumer. In the years that followed, we saw a rare example of what I'd term 'dis-innovation', and as succeeding generations of the product were introduced the complexity increased and the value provided to consumers fell. That's a formula for limited growth, regulatory intervention, hostile press coverage and rejection by a large part of the adviser population.

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So while many in the equity-indexed annuity industry felt good about the product reaching $25 billion in sales, I saw it differently and asked: "Why hasn't this product reached sales levels that are multiples of that given the attractiveness of its inherent value proposition?" The truth is, it never became a mainline product and it won't become one unless and until it's cleaned up and can be embraced by the advisers who have traditionally shunned it.

SPA: You're approaching the challenges of the industry as an accomplished marketing professional outside the structured products arena. What does the industry need to do to reach its full potential?

DM: Here's what I feel is most important: communicate the value of structured products clearly and compliantly, avoid undue complexity and maintain excellent consumer value. If the industry can rise to meet these three challenges it will reach sales levels that potentially dwarf other industries that are aiming their offerings at the same customer base, including the insurance industry, I might add.

The introduction of structured products into the retail marketplace is first and foremost a communication challenge on a mighty scale. Retail investors will have to be supported by educationally focused communications that impart clarity and confidence among consumers, advisors – and regulators. The education of regulators is a big issue.

When products become overly complex, it's difficult or even impossible for consumers to understand them. Without understanding, consumers will not have confidence in the products.

When I entered the insurance business in 1977 it didn't take me long to realise that it was truly difficult for people to understand the products. This continues to this day – call it a lack of transparency. It's what the structured products industry needs to avoid. Here's why: throughout the accumulation phase, consumers regularly purchased products based on their faith in their advisers rater than on a clear understanding of the products. I believe that this will change during the distribution phase, and that consumers will demand confidence in the products as well as the advisers. The reason is that the economic stakes in the distribution phase are just too high for any other result. If the structured products industry wants to reach its full potential it will see confidence as it's first and most important deliverable.

SPA: You've become passionate about the potential of structured products over just a short period of time. How did you first hear of structured products and what convinced you the industry is positioned for its long-anticipated tipping point?

DM: I first became aware of structured products through one of Wealth2k's clients, Fixed Income Securities. We were hired by FIS to create some consumer educational presentations on several structured products. In order to create these presentations we really needed to learn how they work and what value they offer.

When I think about the tipping point being realised it's due to a number of factors: the multi-trillion-dollar scale of the financial need, the nature of the competition facing the structured products industry, and the intense marketing communications challenge, which I believe the structured industry is more likely to execute on properly.

SPA: What role does technology play in the industry's efforts to achieve its full potential?

DM: Technology will be important in communicating the value of structured products and in making it easy for consumers to purchase them.

Mass communications and technology are two sides of the same coin; our society has begun to transition from one which acquired information through reading to one which acquires information through watching. Digital delivery of the value of structured products will make it possible for mass market consumers to understand their value in a needs-based context. This is critical to success.

I should also point out that there are no shortage of complexities which must be managed in terms of using digital delivery across multiple channels of distribution, each comprised of distributors which may have their own disclosure requirements and business rules to contend with. In my commercial life, I've spend a great deal of time on this challenge in order to create a web-based communications network designed to handle these complex business requirements.

SPA: How would you compare the structured products business to other, more well-established industries such as the mutual fund and insurance worlds?

DM: Some of my friends in the insurance industry may bristle when I say this, but I think it's possible that the structured products industry may end up serving as the saviour of the insurance industry, for a couple of reasons.

One could argue that the insurance industry should be the business that's naturally positioned for success in boomer retirement given its experience and ability to underwrite mortality and morbidity risk. But when you think about the present size of the annuity industry, for instance, you see that its total asset base is a bit over $2 trillion. This implies a huge capacity constraint that I don't hear being discussed in the insurance industry.

It's the non-profit organisation that I serve as a director – the Retirement Income Industry Association – that has identified this capacity limitation as a problem given that we're looking at tens of trillions of dollars of boomer retirement assets which must be longevitised.

So one can draw a straight line to both the need for new types of structured products designed to meet the market need in terms of the money volume, as well as to strategic alliances between some insurance companies and some providers of structured products. It's through these alliances that I can see some insurance carriers reaping a golden harvest of new business in the future. ■