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The Dangers of Reviewable Products?

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Reassuringly refreshing



Agenda



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- Need for Critical Illness Insurance
- Driver of Trends in Critical Illness Insurance
- Types of Reviewable Business
- Fairness and the Mother Test
- Anti-selective lapsation
- Learning from other markets on reviewable business

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Need for Critical Illness Insurance



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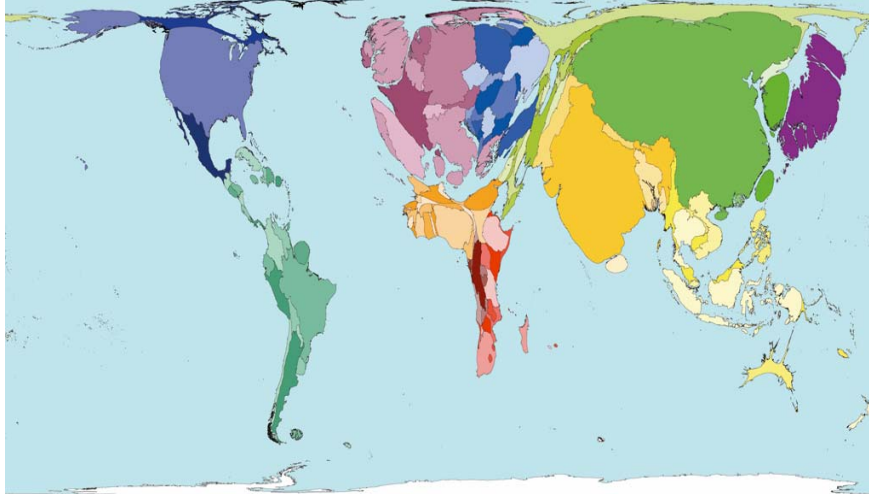
**Asian companies could sell much more CI !
Average sums assured are low to cover all these
needs!**

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Need for Cancer Cover



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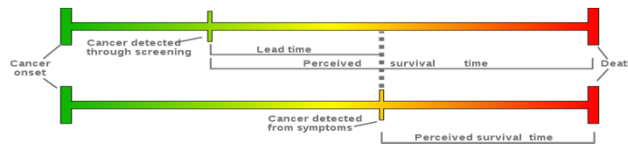
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Round up of future trends for CI



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- MORE and CHEAPER and BETTER screening in the future
- More people will survive cancers with minimum impacts on their health



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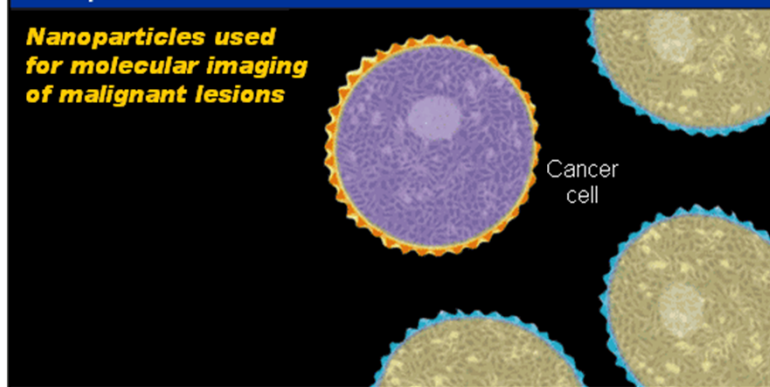
Nanotechnology in cancer detection



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Nanoparticles

Nanoparticles used for molecular imaging of malignant lesions



Source: NCI Alliance for Nanotechnology in Cancer

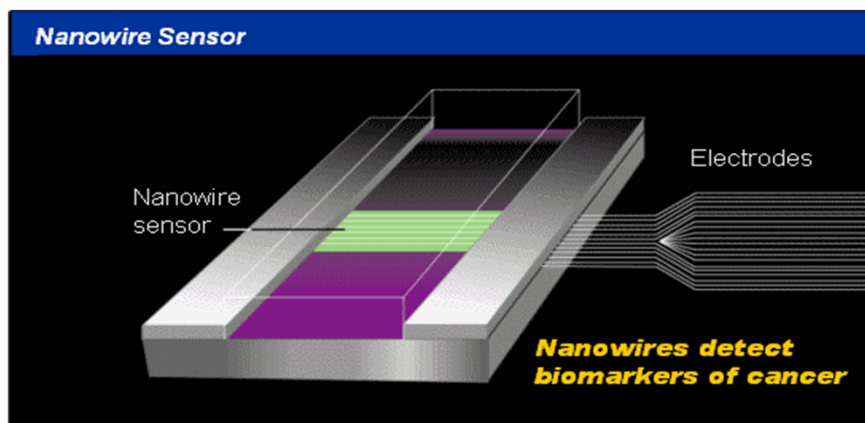
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Nanotechnology in cancer detection



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Nanowire Sensor



Source: NCI Alliance for Nanotechnology in Cancer

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Types of reviewable products

- Level premium
- Yearly Renewable Term
- Renewable after 5 or 10 years
- Premium rebates
- Participating

Each type of product brings its challenges



Reviewable products = less risk??

- You can increase rates if experience is bad
- Requires less margins in the pricing
= cheaper rates = more sales
- Often require less capital (except under Solvency II !)

What can possibly be wrong?



Are reviewable rates fair?

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- Safeguard the consumer's interests
- Be clear and transparent

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The Mother Test

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Learning from other markets – CI cover and brand damage in the UK



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- CI cover in the middle and late 90s did not have future deteriorations priced into reviewable rates
- CI experience worsened (generally due to troponins and heart attacks and earlier detection and IBNR)
- Premiums went up by around 25-30%
- Customers complaints went up!
 - Never understood premiums could change
 - Never expected a review since there was no review in 3+ years
 - Reinsurers and insurers both suffered brand damage
- Lessons learnt
 - The ABI Best Practice
 - Guaranteed is Guaranteed
 - Insurers ask reinsurers more questions now!

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Learning from other markets – CI cover and brand damage in the UK (ctd)



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- Other knock-on effects:
 - FSA required insurers to review down rates of other reviewable products where experience had improved (eg mortality)
 - Fall in trust for insurance companies
 - Some insurers kept premiums unchanged and accepted lower margins from the worse experience
 - Retrospective offer of guarantee to the customer post review increase
 - Increased use of reinsurance on inforce business or move to capped or guaranteed reinsurance rates



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Learning from other markets – unit-linked WoL in Ireland



- Customer given choice of mix of savings and protection element at outset
- Premiums are fixed for 5 years but reviewed on any deviation in experience
- Investment return was initially priced at an optimistic level (and not disclosed to the customer)
- Funds had a heavy exposure to real estate
- Property and equity prices fell
- Increases of 1000% at renewal were not uncommon
- Huge anti-selective lapses followed
- Many companies offered the option of a switch to a non-linked WoL product
- Significant press coverage and brand damage to most Irish insurers



Learning from other markets – Single Premium Reviewable LTC



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- Don't do it!
- Sold in the UK in the early 90s
- 10 year reviewable Single Premium Plans
- What can rates be reviewed for?
 - Experience?
 - Interest rates?
 - Changes in reserving regulations?
 - Reinsurance?
 - Nothing was defined at outset!
- No communication in 10 years before review
- Option was given to reduce benefits or top up premium: about 20% chose to top up

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The DANGERS of getting it wrong



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Ensuring Fairness to Customers

- Customer dissatisfaction => trust broken, take out dissatisfaction on entire relationship
- Agent/distributor backlash => new business sales fall on all products
- Reputational risk => affects your brand & potentially other parts of your business (non-life, bank, ...)
- Regulator oversight => questions, approvals, ...

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Customers like certainty and guarantees



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- In markets where both reviewable and guaranteed terms are offered, hardly anyone buys reviewable business
- This includes markets such as Korea, Japan and the UK (95% of CI in the UK is guaranteed)
- Guaranteed rates are strongly preferred by customers in other forms of insurance e.g. motor where no claims discount protection is frequently bought
- Trust is an issue for insurance companies

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Anti-selective lapsation



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- Lapses increase => loss of embedded value
- Lapses are selective => experience worsens
- Most acute in products which have a step up in premiums e.g. YRT or 5 year renewable

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Learning from other markets – Korean hospital cash



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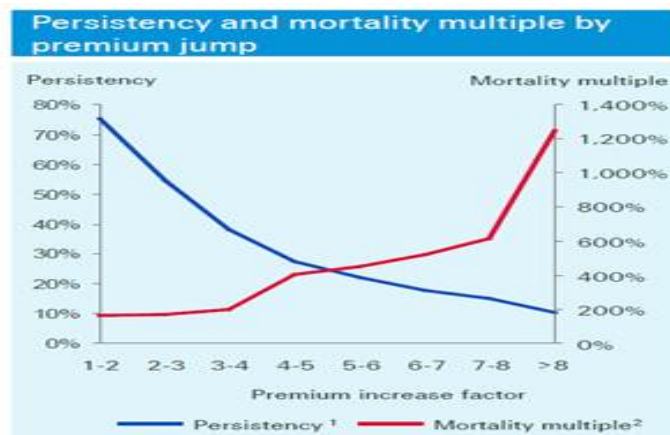
- Korean Hospital Cash business
 - whenever premiums go up by more than 15-25% anti-selective lapses ensue
 - Issues with consumers switching to other companies and switching to different products to meet their protection needs e.g. introduction of reimbursement plans
 - reviews have to go through the regulator which can prevent use of some important rating factors which could prevent anti-selective lapsation

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Learning from other markets – US post level term



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Source: Swiss Re Investor Presentation

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Learning from other markets – Australian Income Protection



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- Almost all the products sold are YRT & inflation linked
 - Premiums already go up by 13% a year
- Very common for new benefits, features and prices to apply to the existing in force portfolio
- Lapses typically 12-15% per annum
- Experience has worsened during the GFC, albeit bit later than expected
- Prices are rising & now lapses are rising
- Many companies reporting lapse and experience losses

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Some recent reporting from Australia



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AMP (Australia's biggest life insurer)

- AMP's Wealth Protection earnings compressed by poor lapse/claims experience
- While AMP insurance margins remain above market average, Wealth Protection's FY 12 results impacted by higher lapses and claims costs leading to experience losses of A\$49m¹ in FY 12
 - Lapse losses A\$29m (2H 12 A\$20m; 1H 12 \$A9m) – claims losses A\$15m (2H 12 A\$29m; 1H 12 \$A14m gain)
- AMP has strengthened assumptions for lapses and income protection claims (AMP Life), impacting both EV and VNB and the expected mix between profit margins and experience results in FY 13²
 - Strengthening lapse assumptions was the major driver of the impact on E V

NAB Wealth (Australia's 2nd biggest life insurer)

March 2013 v March 2012

Cash earnings before IoRE of \$48 million for the March
2013 half year decreased by \$45 million or 48.4% when compared to the March 2012 half year. This was largely due to higher insurance claims, an increase in lapses and changes in the profile of the retail insurance book, partially offset by growth in average inforce premiums.

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Impact on all stakeholders Guaranteed v Reviewable



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Adviser	Insurance company	Customer
Higher commission	Higher risk as no ability to change rates	Initially more expensive
Fewer complaints due to premium increases	Less potential for brand damage	Certainty of cover at given price
Easier to explain to customer	No future admin hassle at review	Simple to understand
	Differentiation from competitors	

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Conclusion



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- Guaranteed is Guaranteed
- Guaranteed rates have the potential to:
 - Grow the market
 - Improve one's Brand
 - Reduce risk
- Reviewable has to be explained
- Reviewable is not risk free
- Guarantees should be offered where they can be; there is still a place for non-guaranteed rates
- Consider offering both reviewable and guaranteed

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How much do guaranteed CI rates cost?



YOUR QUOTE RESULTS

£60
APPLY BY 31 OCTOBER

Quote type requested	Your cover amount	Your premium
Guaranteed	£100,000	£47.65
Standard	£100,000	£42.19

Your total monthly premium is £47.65*

Your total monthly premium is £42.19*

Guaranteed is only 13% more expensive for 25 yr term!