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# Alas, Poor Traded Endowment Policy Market. We Knew You

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# Editor's Letter
# Volume 2, Issue 6, June 2023

The first secondary consumer life market came courtesy of the United Kingdom, when auctioneers H E Foster & Cranfield started auctioning pure life risk policies in 1843. Due to tax changes, however, that market is now essentially defunct. *Greg Winterton* spoke to **Roger Lawrence**, Managing Director at **WL Consulting**, and **Alec Taylor**, Marketing and Relationship Director at **SL Investment Management**, to get their thoughts on the market generally in *Alas, Poor Traded Endowment Policy Market. We Knew You.*

As artificial intelligence (AI) becomes more high profile, insurance practitioners are taking note of not only the potential for the technology, but also the potential for AI bias. *Aaron Woolner* spoke to **Karl Ricanek**, CEO at **Lapetus Solutions**, and **Keith Raymond**, Principal North America Analyst at **Celent**, to get their views on the challenge in *US Life Insurers Look for Solutions to AI Bias Issue*.

The Office of the Montana State Auditor recently issued an advisory regarding the practice of inducing termination of death benefits through time-limited enhanced cash surrender value offers. *Jeffrey Davis* spoke to **Nat Shapo**, Partner at **Katten Muchin Rosenman**, to get his thoughts on this development in *Montana is Latest State to Warn Life Insurers About Enhanced Cash Surrender Value Offers.*

The rising interest rate environment is impacting certain transactions in the life ILS market but some of the nuances in the space means that a temporary pullback shouldn't be too severe. *Greg Winterton* spoke to **Adam Robinson**, Head of Life and Chief Underwriting Officer at **Securis Investments**, to get his thoughts on what's going on here in *Dealflow Down in Life ILS But Moats Remain.*

Much of the deal activity in the life settlement industry's secondary market revolves around higher face value policies, but increasingly, smaller face value policies are becoming of interest to investors in the space. **Anna Bailey**, Managing Partner at **Chestnut Capital Management**, explains some of the benefits that smaller face value policies can bring to a portfolio in *Increased Activity In Smaller Face Value Life Settlements A Welcome Development*, our first commentary article this month.

It's incredibly difficult to measure the size of the life ILS market in terms of assets under management held by investment funds. There's little publicly available data, and naturally, many asset managers won't provide information unless they're required to. So, for this month's poll, we wanted to see what our readers thought in *What Is Your Best Estimate of the Size of the Life ILS Market in Assets Under Management?*

Mortality trends impact all silos of the life risk industry, and **Mike Fasano**, Senior Underwriting Consultant at **Fasano Associates**, offers his analysis in *Mortality & Life Expectancy Trends*, our second commentary piece for June.

Technology advances are driving improved processes in all industries and markets, and the longevity markets are no different. *Greg Winterton* spoke to **Mark Venn**, Director at **ClearLife**, to learn more about his firm and how technology is impacting longevity investors in this month's *Q&A*.

Reasons abound why seniors in the United States might seek to sell their whole life insurance policy, but interesting new trends are driving supply. *Greg Winterton* spoke to **Aaron Giroux**, CEO at **LifeRoc Capital**, to find out what they are in *New Drivers of Life Settlement Transactions Emerge to Provide Industry With Added Fuel for Growth.*

I hope you enjoy the latest issue of Life Risk News!

**Chris Wells**
Managing Editor
**Life Risk News**

# Alas, Poor Traded Endowment Policy Market. We Knew You

Author:
**Greg Winterton**
Senior
Contributing Editor
**Life Risk News**

In 1983, the UK government introduced the mortgage interest relief at source (MIRAS) program, which was designed to encourage homeownership in the country by offering borrowers tax relief on interest payments on their mortgage. Albeit circuitously, this policy paved the way for what followed; the Traded Endowment Policy (TEP) market, where individual policyowners could sell their policy on the secondary market to a third-party investor. Thus, the first substantial secondary life market was born.

The sale of mortgage endowments in the UK eventually became something of a consumer – and therefore political – hot topic, however, as it became clear that the promises offered by manufacturers of mortgage endowments - that the endowment would grow sufficiently large so as to pay off an interest-only mortgage - would not be able to be kept.

> “Activity in the early 1990s was light but it accelerated quickly. We were advertising in newspapers, and in the trade press – remember, this is before the internet – and we were fielding an ever-increasing volume of calls a day from consumers looking to liquidate. We were acting as a market maker – buying policies onto our books direct from consumers, then selling onto individual investors via our stock list.”

So, consumers wanted rid. Enter the TEP market; after a slow start, things began to move.

“Activity in the early 1990s was light but it accelerated quickly,” said Alec Taylor, Marketing and Relationship Director at SL Investment Management. “We were advertising in newspapers, and in the trade press – remember, this is before the internet – and we were fielding an ever-increasing volume of calls a day from consumers looking to liquidate. We were acting as a market maker – buying policies onto our books direct from consumers, then selling onto individual investors via our stock list.”

The market ballooned in the mid-1990s, by which time, TEP investment funds listed on the London Stock Exchange had become a popular way for investors to invest in pooled TEP product. These were closed-ended, 12 or so-year duration vehicles, and by the end of the decade, deals were plentiful as the market was in full expansion mode. The number of trading firms increased from three or four to 20 or more, making the size of the market significant.

“In 1999, there was around £400m of deals done in the market, and market penetration was probably around 40% by 2000/2001,” said Roger Lawrence, Managing Director of actuarial firm WL Consulting.

But the writing was already on the wall. As early as 1988 – just five years after the introduction of MIRAS – the option for married couples to pool their allowances was removed. British Chancellor of the Exchequer Norman Lamont cut the tax relief to 20% in 1993 and Gordon Brown abolished MIRAS entirely in 2000, by which time endowment mortgages had already ceased to make economic sense.

Similar to the laying down of fine wine, whereby today’s production finally emerges from the cellars many years later, the fuel for a secondary market for TEPs depended on new policy sales continuing to provide tradeable material in the future. The effect of the tax changes meant that new policy sales ceased and though there were still plenty of policies to trade – the typical policy term being 25 years - the end of the market became visible.

For those in the market at the time, they essentially had a quarter of a century runway until they needed to find something else to do. And in the early part of the 2000s, they were still busy, this time, battling one of the most significant economic shocks of the century.

“The bursting of the dot-com bubble really hurt open-ended TEP funds in particular,” said Taylor. “The hit that the underlying insurance companies took on their investments – through their With Profit funds - meant that the value of those policies, and consequently, the TEP funds that owned them, became significantly lower.”

The beginning of the end for the TEP market was juxtaposed with the birth of the US life settlement market.

Whilst the 1911 Supreme Court ruling in Grigsby vs Russell paved the way for the industry, the market in its current form has been around since the early 2000s. Taylor's firm – called Surrenda-Link at the time – pivoted to life settlements in the noughties, and it's been something of a cathartic experience.

**"It worked. The market delivered value to the public and to investors for 25 years. But the regulatory mood is against providing alternatives, so, to all intents and purposes, it's sadly now come to an end."**

"It made sense to pivot. There are – were – many similarities between the two markets, and although the TEP market was still expanding at the time, everyone knew it would eventually enter run-off. The life settlement space is now almost our exclusive focus, and it's a market that's growing, and robust. When you work in a market that has such a long run-off as we had in the UK, you have plenty of time to get over it, but life settlements has been our core business for many years now," said Taylor.

The TEP market in the UK actually dates way back to 1843, when auctioneers H E Foster & Cranfield started auctioning pure life risk policies, pre-dating the Grigsby vs Russell case in the US that was the pre-cursor to the life settlement market. But now, it's essentially a footnote in capital markets history. The market has, more or less, returned to the very niche cottage industry that it was when it began 180 years ago.

Most With Profits funds are closed and in run off; whilst there are still opportunities for small investors to buy into a developing share of these funds' surpluses through appropriate vehicles, this is no longer a serious market that would attract institutional scale investors.

This isn't to say that new secondary life markets might not evolve in the future. In the UK, as part of pension freedom regulatory changes introduced by the Treasury, a secondary annuity market was touted, that would have allowed consumers to realise liquidity out of their fixed annuity contracts, accelerating what would have been future payments. The plan was ultimately scrapped in 2016, but other markets may also arrive as governments and consumers look to find new ways to fund increased longevity and long-term care.

Still, given that With Profits savings are out of fashion, what is left is highly regulated and risk-averse regulators have very little apparent appetite to bring the mortgage endowment market back at scale.

"It worked. The market delivered value to the public and to investors for 25 years," said Lawrence. "But the regulatory mood is against providing alternatives, so, to all intents and purposes, it's sadly now come to an end."

# US Life Insurers Look for Solutions to AI Bias Issue

Author:
**Aaron Woolner**
Contributing Editor
**Life Risk News**

As artificial intelligence (AI) becomes more high profile, insurance practitioners are taking note of the potential for the technology, but also the potential for AI bias.

Insurance regulators have been concerned about the dangers posed by AI for some time. In January 2019 the New York Department of Financial Service (NYDFS) put out a circular on the: 'Use of External Consumer Data and Information Sources in Underwriting for Life Insurance'.

The circular was issued following a departmental investigation which highlighted two major problems with insurers using AI to collate external data sources for their underwriting process: the potential for unlawful discrimination, and a lack of consumer transparency.

Pointing to two existing laws which prohibited insurers from discriminating against customers the NYDFS said: "Based on its investigation, the Department has determined that insurers' use of external data sources in underwriting has the strong potential to mask the forms of discrimination prohibited by these laws."

> **"As artificial intelligence (AI) becomes more high profile, insurance practitioners are taking note of the potential for the technology, but also the potential for AI bias."**

It is not just New York State which is looking to regulate insurers' use of AI, in 2022 the Connecticut Insurance Department, and its California equivalent, inked bulletins on AI and racial bias, while the US National Association of Insurance Commissioners (NAIC) has formed a working group on Big Data and Artificial Intelligence.

The NAIC task force has yet to release any findings but individual states are already taking the initiative. In 2021 the Colorado legislature passed a law requiring that insurers establish a framework to ensure that industry's use of AI is not discriminatory. In February this year a draft framework was issued, which critically moved beyond a principles-based supervisory approach.

It is easy to see why regulators are concerned about the potential for AI powered large language models (LLMs), such as ChatGPT, to inculcate ethnic, and other biases, into insurers' policies if they are used to synthesise the huge amounts of historical data the industry holds.

The litigation risk posed by AI became real in December 2022 when US life and P&C insurer State Farm, found itself on the wrong end of a data-based class action lawsuit, which alleges that Black American householders' claims were subject to greater scrutiny than their White peers — in other words exactly what the NYDFS had warned about three years earlier.

The heart of the problem is the disparity in data held by US life insurers on different ethnic groups and differences in the types of policies they were sold in the past which makes aggregating the data via LLMs problematic.

Karl Ricanek, CEO of Lapetus Solutions, which provides AI products such as facial recognition software to the insurance sector, says these disparities will inevitably result in biased results if AI is used to analyse it.

"If an insurer's data underrepresents the number of African Americans, or Hispanics, then the primary data will invariably overshadow it. Unless firms take specific action to augment their existing data the results won't be accurate. And then the question is, how do you get that data? And how are they utilising that data?"

Ricanek says one solution would be for insurers to pool their existing statistics in order to gain a more holistic output from LLMs. There are precedents, both globally, and in the US, for this type of action. Since 2005, ORIC International has been providing pooled and anonymised data to help insurers manage their operational risk exposure, while the Lapetus CEO points to the US's MIB (previously known as the Medical Information Bureau) which operates on a similar model.

The MIB is a pooled resource which enables US life insurers to cross-check life insurance applications to detect potential fraud, and Ricanek says that a corresponding approach could help ameliorate the issue of AI-linked discrimination.

Adding the caveat that this is not a perfect solution, the CEO says that with each carrier serving a slightly different demographic pooling data will result in a more accurate picture.

"Each insurer has a population that their products resonate with so if you pull all this data together then it's possible to capture the largest swathe of policyholders. If you want to understand how to really use this technology, you have to involve different data points from all the subpopulations."

Ricanek's comments are in line with Keith Raymond, Principal North America Analyst at Celent, who says the issue is not AI technology itself, but instead putting in place the correct guidelines to manage it.

**"Insurers are already using AI. It's just a matter of: 'This is the new shiny toy', and 'What are the implications of using it?'. Do we have to put additional guardrails in place? Because the whole issue about ethics and bias in AI has been around for a long time; it's nothing new. Instead the question is does this add a level of risk that requires additional governance structures?"**

Raymond points to the already extensive use of chatbots by insurers' customer services departments as an example of the technology prevalence in the industry, and he says that the issue now is how to manage AI.

"Insurers are already using AI. It's just a matter of: 'This is the new shiny toy', and 'What are the implications of using it?'. Do we have to put additional guardrails in place? Because the whole issue about ethics and bias in AI has been around for a long time; it's nothing new. Instead the question is does this add a level of risk that requires additional governance structures?"

According to Raymond, insurers need to develop the enterprise data architecture that will enable them to overcome the issue of bias inherent in their data sets and enable them to gain value from using LLMs.

"An insurer may have over a dozen policy administration systems that it wants to bring data from into an AI model. So having the right enterprise data architecture is a key component of success in moving forward with AI utilisation."

The analyst says developing this kind of data architecture is a long term process and therefore there is no second mover advantage from insurers waiting to see how other firms tackle this issue. Instead he says that developing a successful data management system, which overcomes the bias issues associated with LLMs could provide significant business advantages.

"If an insurer already has the architecture in place, it will be easier to build an AI based LLM model using legacy data, making it possible to identify trends and risk patterns which can impact how future products are designed."

# Montana is Latest State to Warn Life Insurers About Enhanced Cash Surrender Value Offers

Author:
**Jeffrey Davis**
Contributing Editor
**Life Risk News**

The Office of the Montana State Auditor has issued an advisory regarding the practice of inducing termination of death benefits through time-limited enhanced cash surrender value offers.

Montana's advisory, issued by Commissioner Troy Downing and titled "Inducing Termination of Death Benefits Through Endorsements Offering Time-Limited Enhanced Cash Surrender Values Not Available at Policy Issuance," highlights concerns over the potential violation of the Montana Insurance Code by a select number of life insurers.

The issue revolves around the emergence of enhanced cash surrender value offers (ECSVOs) made to policyholders via endorsements not initially contemplated at the policy's issuance. These limited-time offers, made by entities not licensed as a life settlement company, frequently exceed the policy's cash surrender value by a substantial amount, with the explicit aim of encouraging policyholders to surrender their policies and relinquish the associated death benefits intended for their beneficiaries.

**"LISA members have to follow those rules, beginning with getting licensed, and every transaction has a substantial regulatory overlay on top of the licensing requirements, and none of those are being followed with these offers."**

As previously reported by Life Risk News, life insurance companies have been offering ECSVOs since around 2018. To date, insurance commissioners in nine states have issued guidance and advisories on the topic of ECSVOs.

The subsequent course of action involves urging state insurance departments to issue directives to life insurance companies, instructing them to cease issuing ECSVOs and to withdraw any previously made offers.

Nat Shapo, a Partner at Chicago law firm Katten Muchin Rosenman and whose clients include the Life Insurance Settlement Association (LISA), pointed to the ways states regulate the industry to protect consumers from the risk involved.

"LISA members have to follow those rules, beginning with getting licensed, and every transaction has a substantial regulatory overlay on top of the licensing requirements, and none of those are being followed with these offers," Shapo told Life Risk News.

"The concern is this is mimicking regulated life settlements -- without the consumer protection regulations for life settlements. It also evades life settlement laws and it's inconsistent with life insurance laws like unfair discrimination and standard non-forfeiture law," Shapo said.

"Once you get past the legal issues, it seems odd that life insurers would be in the business of terminating life insurance," he said.

Life Risk News contacted the American Council of Life Insurers, the Washington, D.C.-based lobbying and trade group for the life insurance industry, for their perspective on the Montana advisory. While ACLI advocates on behalf of 280 member companies across the U.S., Whit Cornman, Director of Media Relations, declined an opportunity to provide ACLI's perspective for this story.

In addition to Montana, eight other states have taken action regarding ECSVO offers: Louisiana, Indiana, Maryland, Oklahoma, Oregon, Pennsylvania and Virginia and Washington.

The Montana Commissioner's office said it conducted a comprehensive review of these offers and concluded they are non-compliant with several provisions of the Montana Insurance Code. Downing's office wrote that "of particular concern" is the issue of unfair discrimination, as outlined by state law. The code expressly prohibits any form of discriminatory treatment between individuals of the same class and with equal life expectancy, encompassing benefits payable and other contract terms and conditions.

To illustrate the concern, Commissioner Downing provided examples of actual limited-time offers reviewed by the Office of the Montana State Auditor. These included instances where surrender value increases ranged from $58,192 to $199,846 over 60 days, $4,756 to $14,682 over four and a half months, $19,037 to $360,601 over three months, and even an offer of $561,000 over just 15 days, where the original surrender value was $0.

Downing's advisory noted: "A striking case of unfair discrimination arises when comparing two policyholders who purchase identical policies on the same day, pay equal premiums over a 20-year period, but experience vastly different outcomes."

In one scenario described in the Montana advisory, a policyholder surrenders their policy and receives $19,037. In another, the policyholder accepts an enhanced offer the following day, resulting in a staggering $360,601. This discrepancy represents an almost 1,900% disparity in benefits received for the same premium payments, constituting a clear violation of the Montana Insurance Code, the advisory stated.

> **"Policyholders should exercise caution and seek professional advice when evaluating any future offers they receive, empowering them to make informed decisions regarding the surrender of their policies."**

Commissioner Downing clarified that while the Office of the Montana State Auditor does not presently intend to take enforcement actions against insurers who made enhanced cash surrender value offers prior to May 5, 2023, these endorsements and offers are unequivocally in violation of state law.

In light of this advisory, Commissioner Downing says he urges all licensed life insurers, including those who have previously filed enhanced cash surrender value endorsements, to refrain from making further offers of this nature. Failure to comply with the advisory may result in regulatory action and disciplinary measures in accordance with Montana law.

The ramifications of this advisory extend beyond the borders of Montana, as the National Council of Insurance Legislators (NCOIL) had previously called upon state regulators to review similar filings for compliance with their respective laws. It is possible that more states will follow suit to ensure policyholders are protected from potential unfair practices.

"Policyholders should exercise caution and seek professional advice when evaluating any future offers they receive, empowering them to make informed decisions regarding the surrender of their policies," the Montana advisory concluded.

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# Dealflow Down in Life ILS But Moats Remain

Author:
**Greg Winterton**
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**Life Risk News**

A significant percentage of deal activity in the life ILS market consists of 'value in force' (VIF) transactions; the life ILS fund lends money to life insurance companies, with the collateral being the premium payments of a block of policies.

One impact of the higher interest rate environment on both sides of the Atlantic is that deal activity in the VIF space is, currently, subdued when compared to previous years when lower interest rate regimes were more normal. The reason is clear; higher risk-free rates trickle down into the alternative financing market.

"Counterparties have much higher costs of financing now. If they have 15 years' worth of cash flows, and the market securitises at risk free + 700 basis points, it's more expensive for them to do that now than, say, two years ago," said Adam Robinson, Head of Life and Chief Underwriting Officer at Securis Investment Partners.

> **"Counterparties have much higher costs of financing now. If they have 15 years' worth of cash flows, and the market securitises at risk free + 700 basis points, it's more expensive for them to do that now than, say, two years ago."**

The loans made by life ILS funds tend to be multi-year in nature, like many in the broader private debt market. But for those insurance companies looking for shorter term financing options, accessing capital is not a great deal easier.

"A lot of counterparties have been looking for shorter term revolving facilities, however with the inversion of the yield curve, these have become more expensive for them as well," added Robinson.

Accessing the debt markets is harder now for all businesses, public or private. In the general private debt market, banks are pulling back, as are various alternative credit providers; even the private equity sponsor-backed space is seeing a slowdown. But one of the idiosyncrasies of the life ILS space is that insurance counterparties seeking financing solutions don't have many other places to turn.

"Banks are typically not in the space. Private credit funds could potentially enter the life ILS market, but they largely wouldn't be able to absorb actuarial risks. The Life ILS market absorbs lapse and mortality risk into the structure of the deals done in the space. If lapse rates and mortality rates increase, the life ILS vehicle suffers in the sense that returns are lower, but life ILS doesn't typically go after the balance sheet of the counterparty, so the market provides an obvious risk bearing structure for insurance companies," said Robinson.

Roadblocks to deal activity aren't limited purely to the cost of capital for the life ILS counterparty. Changes in mortality data are making modelling mortality risk more difficult. And understanding the true rate of lapsed policies in the market is similarly difficult.

"Higher inflation, like you see in the UK, is impacting the life ILS space. Consumers will no longer pay for some products that they don't consider necessities, and so some insurance products will be impacted here," said Robinson. "And during Covid, some insurers offered premium repayment holidays, so technically, the policies didn't lapse. But are these policies really still active or are they going to lapse when the holiday ends? All of these considerations are affecting the pricing of risk in the space."

Time will tell whether the current, elevated – at least, elevated when compared to the post-Global Financial Crisis period – interest rate regime persists in the medium term. But the supply of deals in the life ILS space isn't purely a function of the prevailing macroeconomic environment.

Historically, deals in the life ILS market have been conducted bilaterally between parties, meaning that connections and networks have had a significant impact on a portfolio manager's ability to source and complete transactions. But now, brokers are moving into the space, which could increase the supply of risk if they can work with the insurers and reinsurers to bring more products to market. Additionally, the market in Asia is largely untapped, with the vast majority of life ILS activity coming in the US, Canada, and Western and Northern Europe.

Additionally, other trades in the market are picking up steam.

"Appetite from insurers with regards to protection is starting to pick up," said Robinson. "A number of them are starting to engage in conversations around this, because an advantage of life ILS when compared to a reinsurer is that they're not a competitor, so there's little to no intellectual property risk for an insurance company when showing a block of business to a life ILS fund."

"Appetite from insurers with regards to protection is starting to pick up. "A number of them are starting to engage in conversations around this, because an advantage of life ILS when compared to a reinsurer is that they're not a competitor, so there's little to no intellectual property risk for an insurance company when showing a block of business to a life ILS fund."

An irony of the life ILS market, which is the same in all private credit markets, is that investors are pausing or reducing their allocations to the space, given the relative attractiveness of more liquid debt markets that are now, for the first time in a long time, providing a respectable yield (albeit still a negative real yield, when factoring in inflation). But despite the pull back in life ILS activity, the deals that are getting done are charging a higher interest rate, which means higher returns than before, a boon to those investors that have allocations in the space.

Activity in the life ILS space is set to be mixed in the foreseeable future; at least, in the VIF space, as the insurers wait for interest rates to start coming down. But when compared to the broader private credit market, the moat around the space should insulate it from too much of a pullback in the short term.

"As I mentioned, life ILS counterparties have fewer places to turn than other companies for their financing needs. Activity is lower, but only marginally so, and so the outlook for activity remains solid," said Robinson.

# Mortality & Life Expectancy Trends

Author:
**Mike Fasano**
Senior Underwriting Consultant
**Fasano Associates**

> "Life expectancy continued to improve, in part due to reduced cancer mortality, from 76.5 years in 2000 to 78.9 years in 2015; but then we back tracked to a life expectancy of 76.4 years in 2022, leaving 21st century performance flat thus far."

In this paper I will discuss mortality and life expectancy trends in the 20th and 21st centuries, developments that offer the potential to extend life expectancy, and funding constraints that may limit that potential.

**20th Century:**

US life expectancy (at birth) increased steadily in the 20th century, from 48.2 years in 1900 to 76.5 years in 2000.

- Mortality improvements in the first part of the 20th century were influenced by a reduction in childhood mortality and infectious diseases due to better sanitation and safer drinking water.
- Mid-century improvements resulted from further decline in infectious disease associated with widespread use of antibiotics and vaccines, with benefits spread evenly across ages.
- Late century improvements were associated with a reduction in cardiovascular mortality due to medical technology that resulted in better diagnostics (echocardiograms, cardiac MRIs, etc.) and treatments such as bypass surgery, cardiac angiography and the like, as well as blood pressure and cholesterol drugs. These improvements disproportionately benefited those over age 65.

**21st Century:**

Life expectancy continued to improve, in part due to reduced cancer mortality, from 76.5 years in 2000 to 78.9 years in 2015; but then we back tracked to a life expectancy of 76.4 years in 2022, leaving 21st century performance flat thus far. The recent decline in life expectancy was due primarily to COVID-19 related deaths, but also due to drug related accidental deaths. COVID-19 deaths are trending down now, with a significant impact on total US deaths.

Provisional mortality data published by the National Center for Health Statistics (NCHS) reveal a decline in total U.S. deaths from 3,464,231 in 2021 to 3,273,705 in 2022, a reduction of 190,526, or 5.5%. This drop correlates strongly with the decline in COVID-19 related deaths from 462,193 in 2021 to 244,986 in 2022, a reduction of 217,207. Details on the four major causes of death are as follows:

| 2021 Deaths | | 2022 Deaths | |
|---|---|---|---|
| **Causes** | **Deaths** | **Causes** | **Deaths** |
| Heart Disease | 695,547/20.1% | Heart Disease | 699,659/21.4% |
| Cancer | 605,213/17.5% | Cancer | 607,790/18.6% |
| Covid-19 | 416,893/12.0% | Accidents | 218,064/ 6.7% |
| Accidents | 224,935/ 6.5% | Covid-19 | 186,702/ 5.7% |
| All Other | 1,521,643/43.9% | All Other | 1,561,491/47.7% |
| **Total** | **3,464,231/100%** | **Total** | **3,273,705/100%** |

"Ours is an aging population with the percentage of ≥ 65-year-olds is projected to increase from 15.2% of population in 2016 to 20.6% in 2030, while the percentage of 18 to 64-year-olds decreases from 62.0% to 58.1%. This will generate greater retirement and medical expenses with a smaller workforce to fund them."

Predicting the future is always dicey, but I think it is reasonable to assume some further reduction in COVID-19 mortality and, hopefully, drug related deaths as well. If so, an increase in U.S. life expectancy of up to two years in the next three to five years would be possible. The question is whether we have the potential to increase life expectancy beyond that.

**Potential Future Improvements:**

There remains significant potential for continued improvement in cancer mortality through nano cytology driven early detection, genetic profiling, and targeted therapies that attack increased signaling for cell growth, evasion of cell death and increased blood vessel formation associated with cancer growth. Eliminating all cancer deaths would add three to four years to life expectancy at birth – theoretically possible, but I think unlikely in our lifetimes. If we achieved half of this potential, life expectancy could possibly increase by 1.5 to 2 years.

Regenerative medicine offers potential, including (a) miniaturized, implantable and wearable devices that can alter electrical signals to stimulate nerve regeneration, (b) injectable biomaterials that can trigger desired cell responses, and (c) organ/tissue transplants. Research suggests potential for spinal cord regeneration, as well as treatment of neurocognitive disorders like ALS and dementia, and possibly even cures for diseases like diabetes. While these developments offer clear potential for morbidity improvement, the longevity potential is likely to be gradual over a time and not as dramatic as treatments that would significantly impact cardiovascular or cancer death rates.

Epigenetics; PAI-1 levels; diabetic medications: DNA methylation has identified plasma PAI-1 levels as a significant independent predictor of lifespan. A small cohort of an Indiana Amish community with a genetic mutation associated with lower PAI-1 levels lived about 10% longer than the rest. Medication to lower PAI-1 level is in trial phase now and could offer longevity benefits, as could medications reducing insulin resistance, such as Metformin.

Biologic Age; Hayflick Limit: Biologic age remains in the range of 120 years and is the ultimate cap on longevity. The Hayflick Limit has shown that cells divide freely to a predetermined number of divisions and then enter senescence, which correlates with aging. Cancer cells produce an enzyme that preserves the telomere cap at the end of DNA strands and thereby allows unlimited cell division. Biologic age could theoretically be extended IF we could replicate the cancer enzyme in other cells, but this is not likely to happen in our lifetime.

Ethnic Demographics: For a number of reasons, Hispanic life expectancy in the US is shorter than average, while Asian life expectancy is longer. The Hispanic percentage of population is projected to increase from 17.8% in 2016 to 27.5% in 2060, which will dampen LE extension, offset in part by an expected increase in Asian percentage from 5.7% to 9.1%.

**Funding Constraints:**

Ours is an aging population with the percentage of ≥ 65-year-olds is projected to increase from 15.2% of population in 2016 to 20.6% in 2030, while the percentage of 18 to 64-year-olds decreases from 62.0% to 58.1%. This will generate greater retirement and medical expenses with a smaller workforce to fund them. U.S. versus Russia and China tensions will keep defense spending at high levels. At the same time, with federal debt to GDP in the range of 120%, at Second World War levels, the debt service burden will be a significant drain on budgetary resources, while our borrowing potential will be constrained. The microchip revolution was the Industrial Revolution of our generation, but it has run much of its course, with no likely equivalent in the foreseeable future to generate substantial productivity increases. All things considered, it is hard to believe that there will be significant public funding available over the next decade for breakthrough longevity research to extend life expectancy.

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# June 2023 Poll Results

# What Is Your Best Estimate of the Size of the Life ILS Market in Assets Under Management?

Author:
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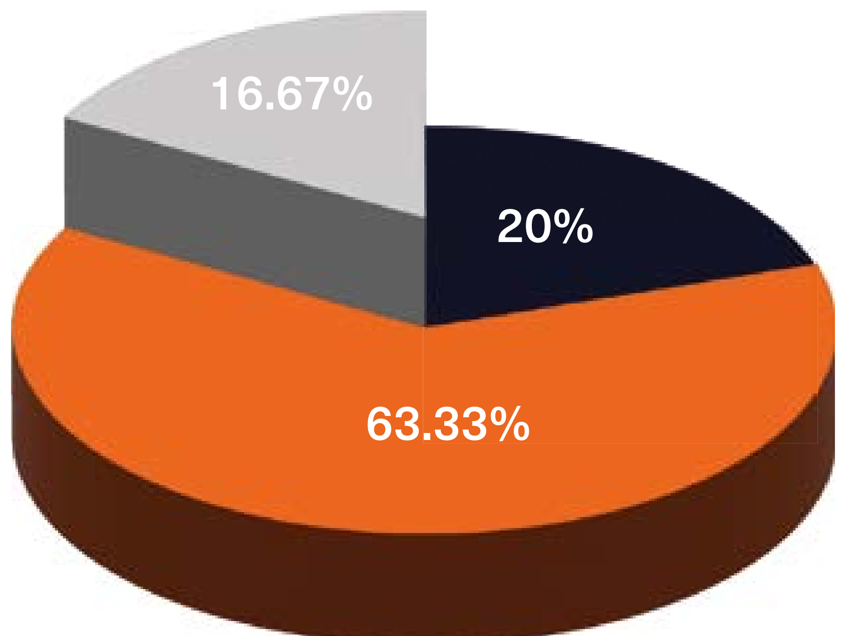
**Life Risk News**

It's incredibly difficult to measure the size of the life ILS market in terms of assets under management held by investment funds. There's little publicly available data, and naturally, many asset managers won't provide information unless they're forced to.

So, we wanted to ask our readers what they thought, with a little bit of educated guessing on our part. We offered three options: below $10bn, between $10 and $25bn, and over $25bn.

The middle option won out in the end, and fairly convincingly; almost two-thirds of our readers think that the market is between $10 and $25bn in AUM. It's not possible to verify if they are right, of course, but if they are, that's a healthy size by many definitions. It'll be interesting to see if sentiment changes over time as the life risk space continues to try and find new ways to involve the capital markets.



# Increased Activity In Smaller Face Value Life Settlements A Welcome Development

Author:
**Anna Bailey**
Managing Partner
**Chestnut Capital Management**

Investors in the life settlement industry's secondary market work with a provider to source policies; indeed, most states that have a regulatory regime for the asset class require a life settlement provider to be involved in the transaction. Those providers in turn source their policies either through the 'direct to consumer' channel – so, advertising on television, radio, in newspapers, or online – or through brokers who sell an insured's life insurance policy on their behalf.

A characteristic of the policies that the brokers work with is that they tend to be higher face value, and for good reason: the broker's costs to source medical records, pay for life expectancy reports and have the insured and beneficiaries sign off on documents necessary to bring the policy to market are similar regardless of whether they're working with a $100,000 policy or a $1 million policy.

That means that deal flow in the smaller face value end of the market from brokers has been slower. But the increase in secondary market deal flow from the direct-to-consumer channel generally in recent years has brought with it a notable increase in the volume of smaller face value policies available to life settlement investors.

Smaller face value policies offer a range of benefits to both fund managers and end investors alike. The first benefit is the classic 'free lunch' – namely, diversification. Best practices in life settlements portfolio construction sees the investor diversify by gender, by age, by carrier exposure, by life expectancy, by impairments, and by state, for legal risk reasons. Many funds in our market are closed ended, so a finite amount of capital goes further from a diversification perspective by investing in smaller face policies, as more policies make it into the portfolio. Instead of buying five large face policies with high-cost premiums, one could arguably purchase 25 polices with the same amount of capital with lower premiums and a diverse pool.

> "The increase in secondary market deal flow from the direct-to-consumer channel generally in recent years has brought with it a notable increase in the volume of smaller face value policies available to life settlement investors."

The second benefit is in being able to execute the job we are supposed to do. Portfolio managers are paid to (wisely) deploy their client's capital. The life settlement industry's tertiary market already provides a mechanism to allocate larger amounts of money, but in the secondary market, there is less activity in the smaller face end, so there's less likelihood of delayed deployment.

The third benefit is access to a part of the market which is growing. 'Baby boomers' are now entering the life settlement market in the sense that many of them are now of an age where they might consider selling their policy. These seniors are more internet savvy than their predecessors – the 'Silent Generation' - and because of this, they have more access to information which in turn means that more of them are familiar with the life settlement option (far too many American Seniors are still unaware of the option that the life settlement industry presents to them) to access liquidity. Again, this trend will fuel increased activity in the direct-to-consumer channel.

Larger face value policies are owned by high-net-worth individuals, the healthy, wealthy, '1%' of the population. The life expectancy profile of these insureds does not always align consistently with the 2015 Valuation Basic Tables used by the life insurance industry for modelling life expectancy because they have a different life expectancy profile; they typically live longer than the 'average' person. But the life expectancy of individuals holding smaller face value policies do align with the 2015 VBT, which, for an investor, means that our exposure to valuation risk is lower.

> “Increased supply of policies in the secondary market is good for our industry, regardless of the policy value size. But the smaller face value end of the market is set to be a more significant contributor to that growth in the coming years.”

Life settlement investors that previously focused heavily or exclusively on larger face value policies are increasingly paying attention to the lower end of the market. The ability to buy more policies with a finite amount of capital not only supports diversification, but volatility and cash flow within the portfolio. Smaller face value policies perform because you can more easily ladder the maturities over the life of a fund which leads to more predictable cash flows from policy maturities. This is a particular benefit to an open-ended fund structure. In larger face, it’s not uncommon to have a quiet six or twelve – even more – months, where no maturities are realised, but the premiums still need to be paid.

Increased supply of policies in the secondary market is good for our industry, regardless of the policy value size. But the smaller face value end of the market is set to be a more significant contributor to that growth in the coming years. Portfolio manager interest is shifting from buying only larger face to actively seeking out good smaller face deals, which brings with it numerous benefits, as outlined above. It’s a benefit to our entire industry – asset managers, service providers, and of course, the end investor - that activity in the smaller face value end of the market is increasing.

# Secondary Life Markets Conference 2023

Date: **September 12th 2023**
Location: **EY, Canary Wharf, London, UK**

Details to be announced visit **elsa-sls.org**

ELSA

# Q&A

**Mark Venn**
Director, ClearLife

Technology advances are driving improved processes in all industries and markets, and the longevity markets are no different. Life Risk News' Greg Winterton spoke to Mark Venn, Director at ClearLife, to learn more about his firm and how technology is impacting longevity investors.

**GW: Mark, yourself and Chris Stuart, ClearLife CTO, worked together at Mizuho before setting up ClearLife. What was the 'eureka' moment that led to the decision to launch your own firm?**

**MV:** If I'm being completely honest, it was probably more hubris than "eureka"! After three years of investing in life settlements – and 14 years in derivatives and principal finance – I decided that I wanted to start a consulting business focussed on life settlements. It was becoming clear at that point (in late 2007) that a significant market correction was around the corner and I felt that the appetite for alternative investments in banks was likely to drop. I thought it really couldn't be too difficult to run my own business (I told you there was hubris involved!) and so made the leap. Chris joining in late 2008 was the key moment that shaped what we wanted to do at ClearLife, as he is expert at converting my wilder flights of fancy into something that can actually be built in a reasonable period of time.

**GW: The life settlement market is famously 'document-intensive' because of the need to analyse medical records of the insured. What are some of the problems that appropriate technology can solve for in this market?**

**MV:** When one thinks of documents, one tends to think of OCR (optical character recognition) and AI (artificial intelligence) follows shortly behind. There is a plethora of firms working on dedicated "smart OCR" for medical records – mostly outside life settlements – and while that is a challenge in and of itself, I think there is much more that can be done with AI outside of medical records. I've lost count of the number of calls and messages we have had from clients who said that interacting with documents is a key challenge and so automating the process of data capture from policy forms, life expectancy reports and other key documents is a natural part of the life settlement purchasing process where technology can make a big difference. I see this as being a step towards AI-driven due diligence, such as being able to identify policies that are likely to have been originated in a non-traditional manner.

Another ongoing challenge is data interchange between market participants. APIs (application programming interfaces) have become mainstream in the past few years and this has enabled us to move from a closed ecosystem (in which everything had to be done within our web environment) to an open platform, in which our clients can pick and choose how and where in the business process they access our services. That mind shift has also changed the way that we at ClearLife think about development and freed up our development team to think more broadly about micro-products rather than one fully integrated platform.

**GW: Still on life settlements - what are some of the notable trends you're seeing generally in this space? Are they short term or structural, and what's the impact of them on the broader market?**

**MV:** There's a structural need to improve origination, by which I mean the flow of unwanted policies from consumers to financial investors. We're seeing an increase in clients looking to source through non-traditional means, such as direct-to-agent and direct-to-consumer channels. We're also starting to see larger aggregators of life insurance (such as registered investment advisors) begin to work on mining their books of business to identify opportunities to switch their customers into cheaper insurance products, creating a pool of potential life settlements. We see this as another area in which technology can provide valuable insight.

**GW: The life-contingent structured settlement market is one that seems to be 'plodding along' in the sense that there are high barriers to entry and so there isn't much in the way of new entrants. Is there enough activity in this space for any new entrants, or is supply quite easily absorbed by the incumbents?**

**MV:** My sense is that it is the latter rather than the former. I've heard several market participants complain about the lack of supply; as a consequence, yield targets in structured settlements are even more inelastic than those in life settlements! Structured settlements have always tended to trade at lower discount rates than life settlements, because of this lack of supply, and the origination process and relatively small size of each settlement make this a labor-intensive process. Most of our clients who are involved in structured settlements tend to hold those positions as an adjunct to much larger life settlements book.

**GW: Lastly, Mark, some say that alternative investment fund managers of all types are infamous for sticking with Microsoft Excel for a variety of tasks, whether that be on the investor relations side or the deal activity side. What's your message to those in the life space that have yet to take the plunge? Why change the habit of a lifetime?**

**MV:** There is no denying that Excel is a great "Swiss Army knife" when it comes to modelling. We use it a lot ourselves for bespoke consulting engagements, such as cashflow waterfall modelling when structuring and arranging loans. However, it lacks a number of features that are critical to core business infrastructure, such as access control, security, auditing and process integration. Often without realising it, people will treat Excel as a database tool and therein lies potential disaster. We have done several migrations with new clients where we have taken Excel workbooks of policy and insured information and moved them into our business management and analytics platform for life settlements. Those migrations frequently expose a number of data errors and inconsistencies. So while there are benefits to using Excel for one-off modelling, long-term data storage and analysis is best served by a dedicated environment supported by auditing, access controls and security.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# New Drivers of Life Settlement Transactions Emerge to Provide Industry With Added Fuel for Growth

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Reasons abound why seniors in the United States might seek to sell their whole life insurance policy to a third-party investor. Two of the most frequently cited are that the insured simply can't afford the premiums anymore - and so selling their policy via a life settlement gets them more cash than the surrender value offered by the insurance company - and the need to be able to fund medical bills or pay off a mortgage.

Many life settlement sales run into five, six, and even seven figures, depending on the policy value. But the more financially savvy American seniors are increasingly seeing life insurance as part of an overall asset allocation model, which in turn is driving more of them to view life insurance as one part of a broader portfolio, something which can be changed depending on the prevailing market environment and their risk appetite.

"Seniors are increasingly undertaking an opportunity cost analysis of maintaining their life insurance policy versus re-deploying that capital to other investment opportunities, such as private investments like real estate," said Aaron Giroux, CEO at Los Angeles, CA-based life settlements provider, LifeRoc Capital. "This is one of the fastest growing reasons that we see people exploring the life settlement option."

> **"Seniors are increasingly undertaking an opportunity cost analysis of maintaining their life insurance policy versus re-deploying that capital to other investment opportunities, such as private investments like real estate."**

Activity generally in the secondary market is seen to be on the up. The Life Insurance Settlement Association (LISA), a Washington, DC-based trade association, unveiled its annual transaction data survey results at its investor conference in May; 3,079 deals were completed by 20 providers in 2022, an improvement on the 2,998 in 2021 – when three additional firms participated in the survey.

Giroux says that he expects that number to push even higher when 2023 is said and done.

"We anticipate that the secondary market will transact around 3,250 deals this year. The general chatter in the industry is that policy submissions are going up."

Not all whole life policies that hit the market get bought, however. Reasons abound for this, including that brokers tend to focus on larger face value policies, restricting supply, and some of the smaller face value policies and younger insureds are perceived as too risky. But this year, those seniors that are managing to realise a sale are considered a safer bet.

"The capital that is in the market at the moment is looking for paper that is less risky – that is, policies with a low probability of survival to maturity. These policies are not really trading at any discount rate," said Giroux.

Whilst brokers remain a significant source of deal flow for life settlement providers, particularly in the medium-higher face value segment of the secondary market, other types of third parties are increasingly getting involved in another boon to those active in the market.

"The direct-to-consumer channel has driven a lot of awareness, but we're also seeing a trend of origination coming through the institutional market. Much of the existing US advisor base is ageing out of the industry, and the newer blood is much less independent and more closely aligned banks, broker dealers, and other institutional players," said Giroux. "Plus, we're seeing sourcing direct from CPAs and attorneys, which is down to the educational efforts that the industry has been involved in."

The industry's tertiary market is experiencing changes in drivers of supply, both structural and cyclical. Macroeconomic factors are also having an impact on the tertiary market; Giroux says that activity in 2022 was higher than in 2021, with one driver being the impact of higher interest rates on portfolios.

"There was some forced selling last year. Some of it is redemption management by open-ended funds and some funds that utilise leverage have had to sell to manage debt and lines of credit. Both of these have brought supply onto the tertiary market last year," he said.

One permanent source of blocks of policies in the market is that of closed-ended funds which are at their end-of-life, so the manager simply sells the remaining policies in the portfolio to liquidate the fund entirely and returns the remaining capital to investors. But an industry that largely operated on a 'buy and hold' strategy is increasingly displaying an interesting change in behaviour.

**"One of the developments that's most impacting the tertiary market is that more and more asset managers are approaching life settlements as an actively managed asset class, like an equity hedge fund would."**

"One of the developments that's most impacting the tertiary market is that more and more asset managers are approaching life settlements as an actively managed asset class, like an equity hedge fund would," said Giroux. "Previously, this was something of a 'set it and forget it' space, but now the core thesis has evolved to the extent that portfolio managers are actively trading in and out of assets during the life of the fund, re-deploying that capital, and not waiting to the end of the fund's life to execute sell side opportunities."

Ultimately, the impact of the macroeconomy on activity in the life settlement market may last a while longer. But for Giroux, what's most notable is that the changes that are having the biggest impact, both in the secondary and tertiary markets, are those which are of a more fundamental nature.

"We need a constant supply of new policies in order for our industry to grow," he said. "I'm mostly encouraged by the developments in the secondary market, like the growth in direct-to-consumer, and the increase in different types of advisors and fiduciaries playing in the space, that should support continued growth in the coming years."

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