Robin & Peter on LIFE SETTLEMENTS

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The State of the Market: Life Expectancies

In the fall of 2008, two of the largest life expectancy companies, 21st Services and AVS, adopted new mortality tables which increased the typical life expectancy by some 20 to 30%. Other life expectancy companies also made smaller adjustments which generally increased their life expectancies as well.

The two most important factors for valuing a policy on the secondary market are the projected premiums to carry the policy and the insured's life expectancy. So, clearly, these adjustments by life expectancy companies have significant implications for life settlements.

To some of us these changes came as no great surprise. Before the fall of 2008, the life expectancies issued by the life expectancy companies appeared to be consistently lower than what life insurers were using. As a result, there was a built-in disparity in the expected value of a policy. An insurance company typically might issue a new policy with an IRR of say 5% on the death benefit at life expectancy. A secondary market life expectancy, some 20 to 30% shorter, might instantly bring the IRR up considerably and make the policy attractive for secondary market investors. One particularly ugly side effect of this disparity was the creation of STOLI (Stranger Originated Life Insurance), which we'll discuss in more detail in a future newsletter.

So - where does this leave us now? What about the traditional life settlement market consisting of policies that were bought years ago for legitimate purposes - policies that today are no longer wanted, needed or affordable? There is no longer an automatic difference between the insurers and the life expectancy companies. The built-in gain is gone. **Generally, to get an offer that exceeds the cash surrender value the insured must have had some decline in health since the policy was issued.**

On the plus side, the change in life expectancies will bring additional capital to the life settlement market. Previously there were some investors that sat on the sidelines wondering how insurers and life expectancy companies could have such different views of mortality. **Having a higher level of consistency in life expectancies is bringing greater confidence in life**

settlements as an asset class.

To quickly estimate the value of your client's policy and whether it could be a viable prospect for a life settlement, we have developed valuation models. These models are based on life expectancy and the carrying cost of the policy and are adjusted periodically to keep up with current market developments, such as the change in life expectancies. This way we can help you to give your clients a range as to what the value of their policy could be and then together you can determine if they want to proceed with the settlement process.

Although life expectancies have increased, many unneeded, unwanted or unaffordable policies still have value over their surrender value. It may not be as much as it was in the past, but if it is more than the surrender value, you will be providing a meaningful and much appreciated service to your clients.

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