State of the Long-term Care Insurance Industry

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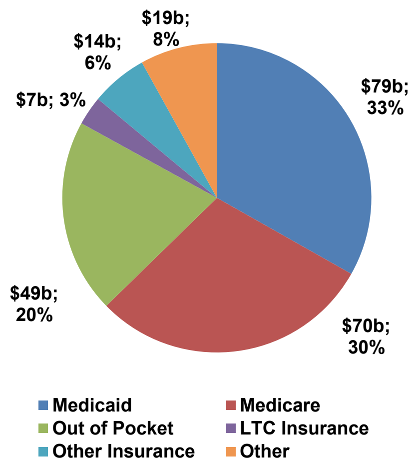
Agenda

- What made LTCi successful in the early days?
- What happened to traditional LTCi?
- Attitudes of a new buyer generation
- Are hybrid products the answer?
- What else can we do?

Funding of LTC Expenses



- **US spending on LTC was $239 billion in 2014**
- **63% was funded by two social programs:**
  - **Medicare: Limited post-acute care**
  - **Medicaid: Once assets are spent down**
- **20% from direct out of pocket spending**
  - **Most represents asset spend-down**
- **Only 3% from private LTC insurance**
  - **7 million insureds out of 86 million age 55+**

Source: National Health Expenditure (NHE) Amounts by Type of Expenditure and Source of Funds: Calendar Years 1965-2014, Centers for Medicare & Medicaid Services

The Need for Private LTC Insurance

- Asset spend-down most common funding scheme
  - Savings are first exhausted or moved via loopholes
  - Migration to public welfare (Medicaid) afterwards
- Strain on social program funding
  - Medicaid's mission is to provide a safety net to the poor
  - Not meant to fund lack of LTC planning for the middle class
- Clear need for individual financial planning / private insurance
  - Demographics result in an unsustainable burden on public resources
  - Preserve assets / legacy funding
  - Higher quality of care when privately funded

Consumer Attitudes

- Biggest fears about retirement[1]:
  - 11%: Will have too much debt
  - 18%: Won't be able to afford daily expenses
  - 23%: Exhaust savings
  - 28%: High medical (LTC) expenses
- Most are aware of Medicaid as a safety net, but worry that it won't allow an acceptable lifestyle

[1]Source: Bankrate.com Money Pulse Survey, Feb. 18, 2015

Consumer Attitudes

- Private financing of LTC is strongly preferred[1]
  - 59% agree that individuals should be responsible
  - 66% agree that owning private LTC insurance would give them peace of mind
  - 51% don't trust the government to run an LTC insurance plan
- Knowledge of LTC costs and risks is relatively low[1]
  - Most greatly underestimate the chance of needing LTC
  - 20% can correctly estimate costs in their state
  - 44% have "other priorities" for money other than LTC insurance

[1]Source: *2014 Survey of Long-Term Care Awareness and Planning*, U.S. Dept. of HHS

Unique Distribution Challenges

- Example of a product that is “sold not bought”
- Lack of awareness of risk and gaps in coverage
- Unfamiliar product features
- Expensive
- Broad distribution channels did not push
  - Lack of understanding of product; discomfort selling
  - Already successful selling other products

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How the Industry Responded

- We answered this challenge with specialty distribution
  - Agents that are trained to sell LTC almost exclusively
- Small distribution pockets produced a majority of sales
  - Initial specialists were captive
  - Independent specialists later emerged and dwarfed captives
- Agents were trained to:
  - Patiently sit with customer leads – often several hours
  - Educate customers about risks and complex products
  - Have rational responses to premium amounts
- Specialists often worked with broader distribution to chase leads they encountered (split commissions or referral fees)

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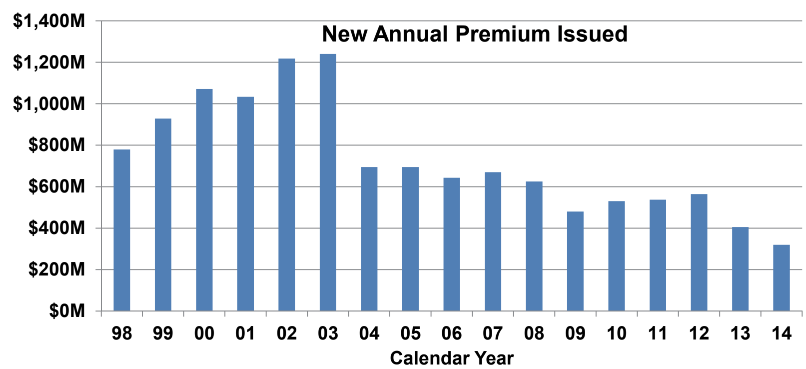
Specialists: Key to Success

- Of the 177 carriers that entered the LTCI market
  - 74 sold less than 1,000 policies
  - Only 56 sold 10,000 or more
- Most carriers did not train or access trained distribution and exited the market early
- Carriers that used specialists saw large sales volumes
- Key to understanding how we succeeded and how we might reenergize the market

Sales Volumes



- Early success!: 20%+ growth during the 1990s
- Short-lived: Sales began to decline in 2001

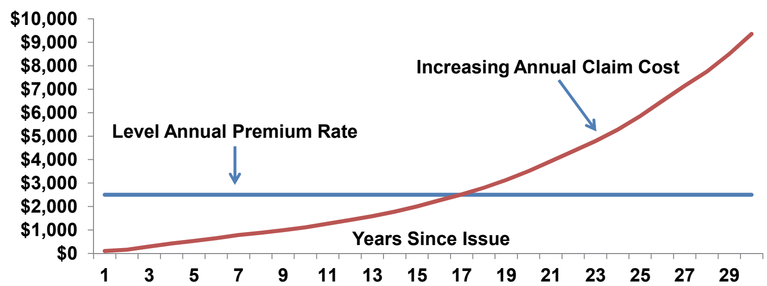
(after netting out 2002-2003 FEP enrollment)

Source 1999 – 2015 *Broker World Surveys*

What Caused the Crash of Traditional LTCI?

Reason 1: LTCI's design makes it a very risky product

- Level premium pre-funds an increasing cost



- Four forces contribute to increasing claim costs:
  - Older people more likely to need long-term care
  - Wear-off of underwriting effect
  - Benefits increase for policies with inflation protection
  - Married people becoming widows and widowers (which have higher costs)

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What Caused the Crash of Traditional LTCI?

Reason 2: Environmental developments

- Very low lapse and mortality rates
  - LTCI's pre-funding nature makes it lapse supported
  - Early pricing assumptions of 4% turned out to be almost zero
  - Mortality rates are lower than annuitant mortality tables
- Unforeseen drop in interest rates
  - LTCI's pre-funding nature makes it very sensitive to interest rates
  - Early assumptions of 5%-8% turned out to be 2%-4%
- Emergence of assisted living facilities ("ALFs")
  - Immaterial care delivery sector when early products were priced
  - Expensive ALF stays are not embedded in early pricing data
  - Almost half of current confinements now occur in ALFs

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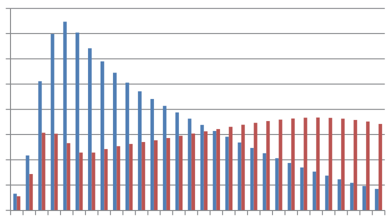
What Caused the Crash of Traditional LTCI?

Reason 2: Environmental developments

Cash flow mismatch causes corrective rate increases to grow over time

Cash Flows By Year Since Product Launch



Rate Increase Required to Offset Future Losses

Deviation	Yr. 5	Yr. 10	Yr. 15	Yr. 20
+10% Claims	7%	11%	18%	27%
-1% Lapse	10%	16%	24%	34%
-1% Interest	8%	14%	20%	27%
All Three	28%	44%	64%	92%

- Regulators resist large rate increases (>25%)
- Often cannot offset losses completely, resulting in reserve corrections
- Creates uncertainty for distribution and potential new customers

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What Caused the Crash of Traditional LTCI?

Reason 3: Carrier exits

2001 Sales

Company	Premium	Share
GE Capital	$243M	23%
Bankers L&C	$83M	8%
John Hancock	$74M	7%
C.N.A.	$61M	6%
UNUM	$55M	5%
Penn Treaty	$47M	5%
Allianz	$42M	4%
IDS	$28M	3%
Fortis	$26M	3%
Life Investors	$26M	3%
Top 10	$684M	66%
Others	$349M	34%
Total	$1,033M	100%

2014 Sales

Company	Premium	Share
Genworth[1]	$90M	28%
Northwestern	$57M	18%
Mutual of Omaha	$32M	10%
John Hancock	$31M	10%
Transamerica[2]	$16M	5%
MedAmerica	$15M	5%
New York Life	$12M	4%
MassMutual	$11M	3%
Bankers L&C	$10M	3%
State Farm	$10M	3%
Top 10	$284M	89%
Others	$36M	11%
Total	$320M	100%

[1]Genworth is a former division of GE Capital
[2]Excluding single premium sales

- 7 out of top 10 carriers writing at LTCI's zenith have exited
- Affects distribution's confidence in industry's commitment to LTCI

Source 2002 and 2015 *Broker World Surveys*

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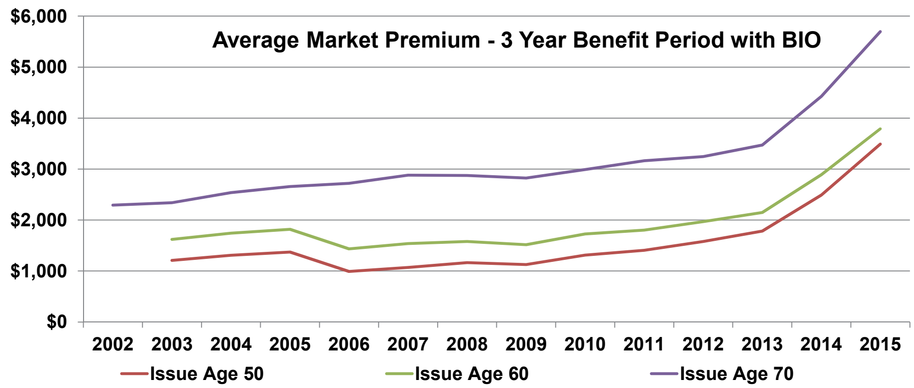
What Caused the Crash of Traditional LTCI?

Reason 4: High new business premium rates

LTCI premiums have climbed above a middle income price point



PA hearing consumer question: “Is LTCI only for the 1%?”

Source: 2002-2015 *Broker World Surveys*

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What Caused the Crash of Traditional LTCI?

- Reason 5: The target market’s generation “turned over”
- We were trying to sell a 30 year-old product to a new crowd

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WWII Generation

- Born 1900-1924
- Also called “G.I.” or “Greatest” Generation
- Endured the Great Depression and won World War II
- Value self-sacrifice
- Average of 2.4 children
- Low divorce rate: 20%
- Saved as much as they could
- Believed in traditional insurance products and trusted their agents
- Currently age 91+

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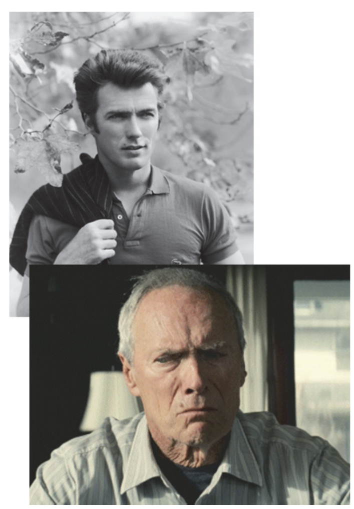
The Silent Generation

- Born 1925-1944
- Born into a time of crisis: Great Depression and WWII
- Younger members grew up in the 50s
- Compliant; honored their elders and loyal to old institutions
- Average of 3.3 children
- Wanted a different childhood for their kids
- Learned how to save from parents
- Currently aged 71-91



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Baby Boomers

- Born 1945-1964
- Also called the "Me" Generation
- Grew up with, but rejected their parents' traditional ways
- Average of 2.0 children
- 40%+ divorce rate
- Redefined retirement
- More likely to view insurance products as investments
- Currently aged 51-71

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Generation X

- Born 1965-1980
- The MTV Generation
- Grew up during prosperous times
- First generation of divorced parents
- First to use PCs
- Average of 2.0 children
- High rate of single parenting
- "Helicopter Parents"
- Out-earned parents, but saved less
- Don't believe that Social Security will be there for them
- Currently aged 35-51

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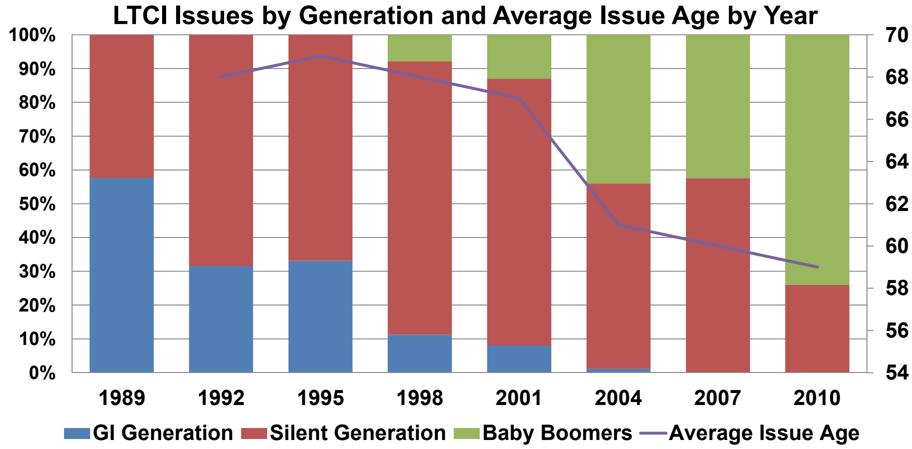
Generation Turnover



Source: 2000-2011 SOA Long Term Care Intercompany Experience Study and AHIP: Who Buys Long-Term Care Insurance in 2010-2011

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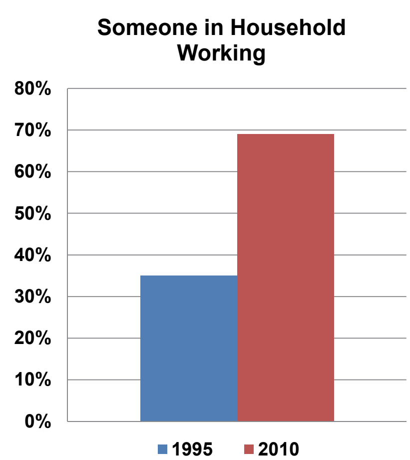
Buyer Statistics



- Lower Issue age in 2010
- Baby Boomers working longer than the Silent Generation

Source: AHIP: Who Buys Long-Term Care Insurance in 2010-2011

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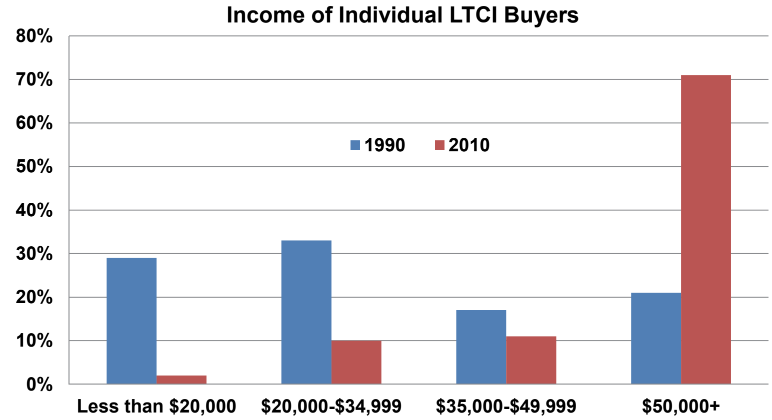
Buyer Statistics



- Inflation partially accounts for shift (71%)
- Rest likely driven by big drop in retiree purchasers

Source: AHIP: Who Buys Long-Term Care Insurance in 2010-2011

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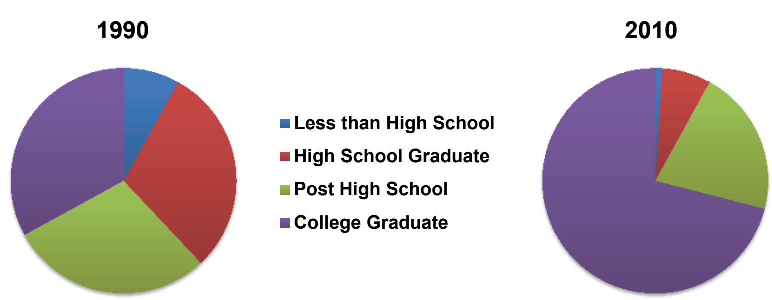
Buyer Statistics

Education Level of Individual LTCI Buyers



Boomers are more likely than Silents to have college degrees

Source: AHIP: Who Buys Long-Term Care Insurance in 2010-2011

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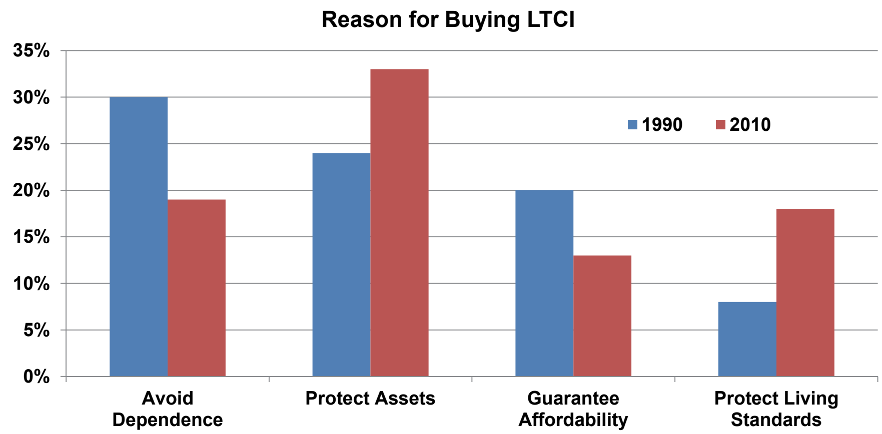
Buyer Statistics



Motivations shifted to preserving assets and lifestyle

Source: AHIP: Who Buys Long-Term Care Insurance in 2010-2011

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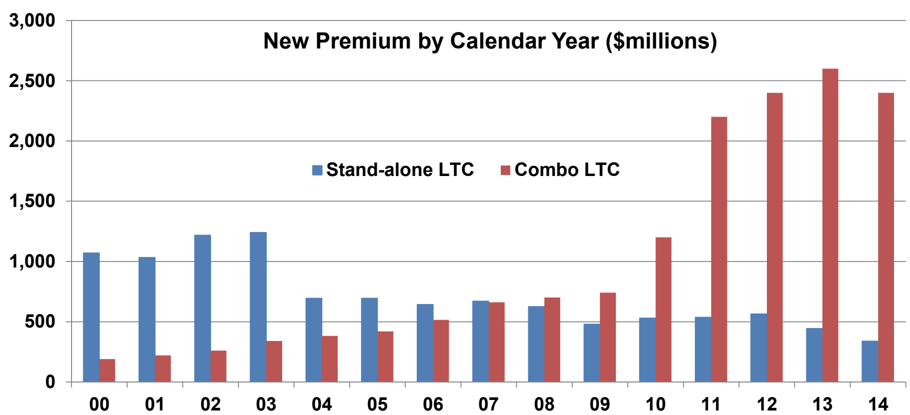
Transition to Hybrid Products



- Shift to hybrids correlates to shift to Boomers as purchasers
- Important to note that much of hybrid premium is single pay

Sources: 2001-2014 *Broker World Surveys* and *LIMRA's Individual Life Combo Products Annual Reviews*

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Hybrid Product Sales

Hybrid products comprised **12%** of new life insurance premium issued in **2014**

100,000 policies and **$2.4 bn** issued in **2014**

Compared to **130,000** policies and **$330m** in the Traditional LTC market

Carriers are entering the hybrid LTC market as opposed to continued exits in the Traditional LTC market

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Hybrid Product Appeal

Customers:

- **Easy to understand: Access to a pot of money (death benefit)**
- **Cost effective: Add-on premiums are generally less than stand-alone**
- **Equity exists in base product's account value**

Carriers:

- **Mitigated risks:**
  - **Exposure limited to life policy net amount at risk**
  - **Insured's equity in base coverage acts like a "co-pay"**
  - **Low mortality offsets life insurance risk**
- **Easy to distribute:**
  - **"Add-on" to the base policy sale; can be sold by broad distribution**

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Are Hybrids the Answer?

Still gaps that can be filled…

Customers:

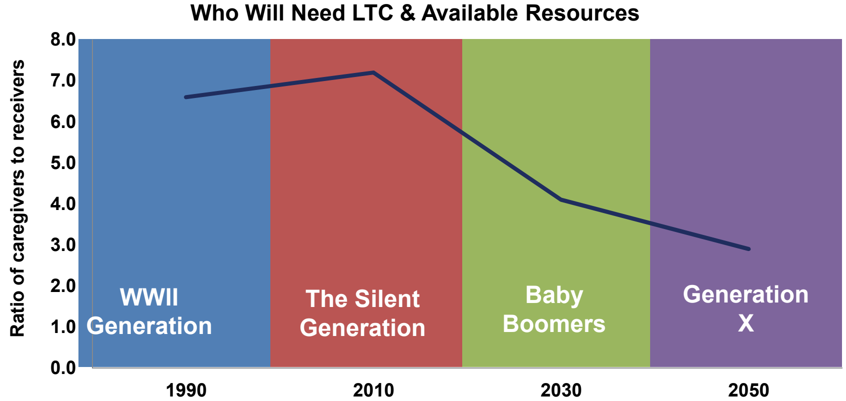
- Not always interested in combining with life insurance
- Simplified purchase
- Modular solutions
- Flexibility of benefits as care delivery evolves

Carriers:

- "Better box" or eliminate long-term environmental risks:
  - Interest rates
  - Declining mortality rates
  - Disability incidence
  - Evolving care delivery

Future Changes in Care Delivery

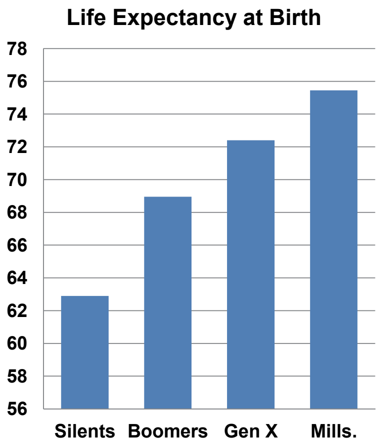
Who Will Need LTC & Available Resources

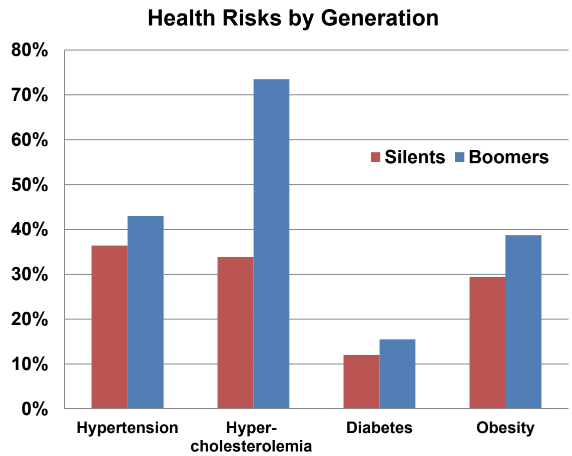


- Generation receiving care will start to flip to Baby Boomers
- Ratio of care givers to care receivers will drop dramatically
- Both will drive changes in care delivery

Source: US Census Bureau 2015 Projection Population

Generational Comparison – Baby Boomers





Boomers will live longer, but are generally less healthy

Source: CDC National Center for Health Statistics and The Journal of the American Medical Association

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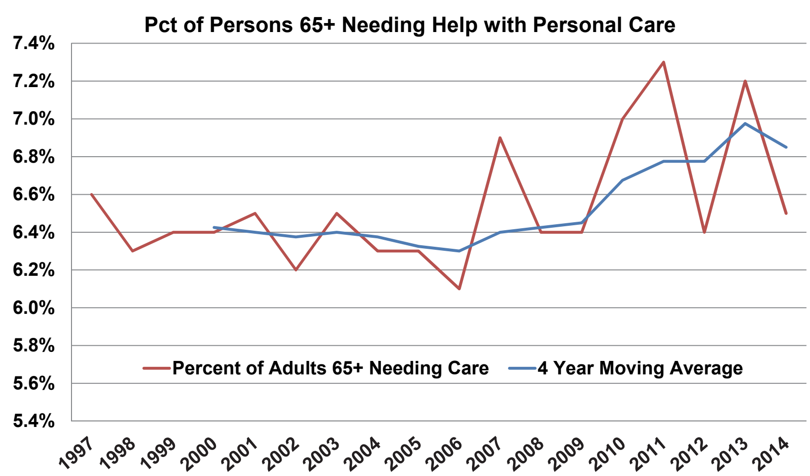
Generational Comparison – Baby Boomers



Source: CDC/NCHS, National Health Interview Survey, 1997–September 2015, Family Core component.

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Current Care Landscape

- Who:
  - Recipients: Silents
  - Informal caregivers: Boomers
  - Formal caregivers: GenXers
- Generational dynamic:
  - Silents accept how things are
  - Do not want to burden children
  - Children are busy and mobile
  - Will endure social isolation
  - Low tech, inefficient health system
- Where:
  - At home
  - Assisted living facilities
  - Nursing homes

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Emerging Care Landscape

- Who:
  - Recipients: Boomers
  - Informal caregivers: GenXers
  - Formal caregivers: Millennials
- Generational dynamic:
  - Boomers will demand change
  - Will not expect help from children
  - Will not tolerate isolation
  - Will want to keep their toys
- Not "Where" but "How":
  - Emerging tech deployed
  - At home via "smart homes"
  - More efficient, less labor intensive
  - Lifestyle preservation "places"
  - Amenities, mobility, social interaction

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What are We Trying to Insure?

A closer look at persons that need care….

- Averages for persons aged 80+
  - Net worth: $275,000 including $135,000 of home equity
  - Annual income: $22,000
- Average annual nursing home cost: $81,000
- Average income shortfall ~ $60,000
- Average time to exhaust assets:
  - Out of cash in about 2 years
  - Burn through home equity in another 2 years
- Many panic and begin Medicaid planning

Isn't this really a lifestyle preservation risk?

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What if We Focus on Lifestyle Preservation?

At the point of needing care…

- Care Annuity (UK version of LTC insurance)
  - Underwritten SPIA issued to newly disabled persons
  - Health conditions result in higher monthly benefit payments than traditional SPIAs
    - 2 year life expectancy for nursing home entrants
    - $120,000 gets you $60,000 per year for life instead of $12,000
  - Removes longevity risk for the annuitant
  - Means that people just need to have enough assets to fund an average stay for persons with similar health conditions
  - Most 80+ year-olds have enough assets to do this

Two U.S. carriers currently sell this product

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What if We Really Changed Our Thinking?

From selling pre-defined benefits to contribution-based products?

- Deferred annuities that are designated to fund Care Annuities
  - Lump sums or periodic deposits
- Simple, modular and flexible for the customer
  - Put in what you can when you can
  - Stop whenever you want; if you don't use it, you keep it
- Elimination of long-term environmental risks for the carrier
  - Only need to price for longevity of cohorts as they become disabled

If we could only change some laws…

- Pre-tax contributions that are not taxed if used for LTC?
- "Term LTC" insurance while account builds up?
- Lever-up account balance if LTC is needed?

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Signs of Hope

- Regulators / legislatures are receptive
  - Increased understanding of legacy block issues
  - Increasing pressure to solve the Medicaid LTC crisis
  - Understand the need for new solutions
  - Asking for industry input: What laws should we change?
- Carriers are evaluating market entry (and re-entry)
  - See an opportunity for an "against the grain" play
  - Want to sell a new value proposition
  - Looking for ways to distribute new product concepts
- Will someone from outside the industry leapfrog us?

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