RETIREMENT & INSURANCE RESOURCES

DUE CARE BULLETIN

November 2012

Update on Analysis of Life & Health Insurer Impairments

Life insurance due care requires an understanding of the factors that impact policy performance and drive product selection.

M Financial Group continues to lead the industry in life insurance due care and client advocacy, providing valuable insight and analysis that delivers significant value to clients.

In March 2010, M Financial Group published a Due Care Bulletin titled "Analysis of Life & Health Insurer Impairments." The bulletin summarized A.M. Best's annual report on impairment rates of U.S. life and health (L&H) insurers.

The impairment report has been updated by A.M. Best with impairments from 2011. The impairment rate for L&H insurers in 2011 was 0.14%, the lowest industry impairment rate since 1962.

The update reinforces the primary conclusions of M Financial's March 2010 bulletin:

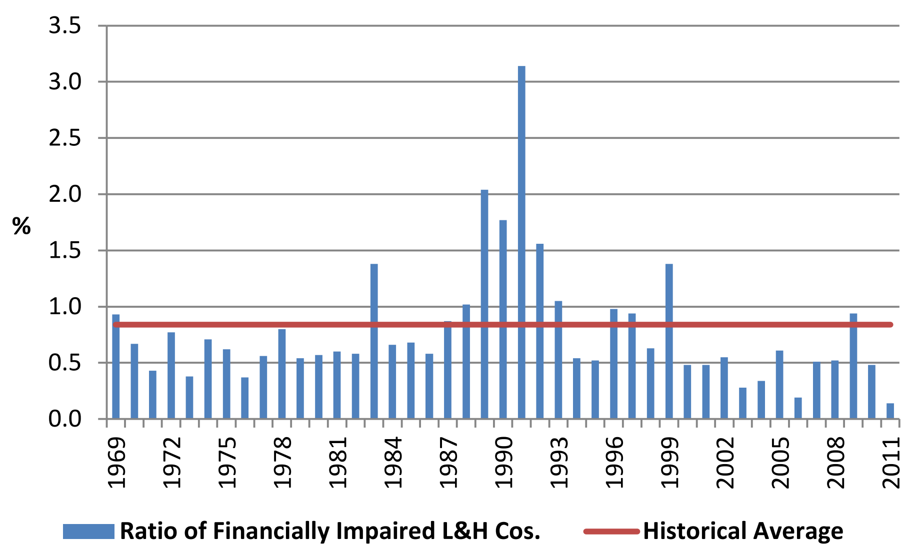
- Most impairments occur with very small insurers (capital and surplus under $20 million)
- Regulatory changes in mid-1990s have helped to reduce impairment rates, which peaked from 1989-1992
- The insurance industry is relatively strong despite recent challenges in the economic environment

In short, as other sectors (most notably the banking industry) continue to be adversely impacted by economic challenges, the life insurance industry continues to effectively serve families and businesses with protection and planning products and services.

History of Life Insurer Impairments

A.M. Best has historically tracked U.S. L&H insurer impairment rates (Figure 1). From 1969 until 2011 the annual rate of financial impairments for L&H companies averaged 0.84%. In 2011, the impairment rate was 0.14%, below the average for the period.

Figure 1. Annual Ratio of Financially Impaired Life & Health Insurance Companies



Source: A.M. Best

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Update on Analysis of Life & Health Insurer Impairments (continued)

Despite the financial crisis which began in 2008, the average annual impairment rate in years following (2008 to 2011 average at 0.52%) was below the historical impairment rate (1969 to 2011 at 0.84%).

According to A.M. Best, 91% of impairments from 1969-2011 occurred at companies with less than $20 million in capital and surplus. The historical impairment rate over the same time period for companies with capital and surplus in excess of $500 million is just 0.4%. By comparison, the smallest M Partner Carrier is Unum Life of America which reported capital and surplus of over $1.7 billion at the end of 2011.

Conclusion

While the life insurance industry does not have a perfect record when it comes to failures, it has historically done an excellent job of handling periods of economic and financial stress. Regulators have adapted capital adequacy and asset quality rules governing life insurers to address risks that previously contributed to the largest life insurer failures. As a result, most failures occur within small companies that lack diversification, transparency, and/or quality management.

As a result of the current economic cycle, nearly all life insurance companies have been negatively impacted. However, the industry remains relatively strong and has weathered the financial crisis well. In October 2012, A.M. Best reiterated its stable rating outlook for the U.S. life insurance industry despite the continued pressure of the low interest rate environment on company earnings. Standard & Poor's reported in its mid-year outlook for the North American life insurance industry that nearly 90% of its financial strength ratings are in the 'A' category or better.

M Financial Group will continue to monitor and evaluate developments relating to the industry as a whole. If you have any questions or comments, please contact any member of the M Product Management team at 800.656.6960.

For More Information

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