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What's Hot in the United States and Canada?

by Karen Terry

The U.S. and Canadian life insurance and annuity markets have their differences. However, when you compare sales trends for the two countries, there are some remarkable similarities in the direction of sales and product performance. This is due in part to the effect of the global economy. Financial markets do not operate in isolation and what happens in the United States and Canada affects the neighboring country's economy, as we have seen with the impact on interest rates in Canada by the recent U.S. sub prime crisis. Financial needs also cross borders. The need for financial security and investment options is the same for consumers, U.S. or Canadian. Finally, Canadian companies have entered the U.S. market and vice versa, and companies watch how products are performing on both sides of the border. Therefore, product concepts that are born in one country often find their way to the other. In this article, I take a closer look at which products are the hot products in the United States and Canada, and what we can expect for future sales for these products.

Super Hot: Universal Life

Universal life (UL) is the hot product in the United States and Canada. In the United States this refers to fixed UL. While fixed and variable universal life products combined represent 56 percent of new annualized premium, the lion's share is currently held by fixed UL, for which sales have been increasing since 1999 (See Figure 1 above). With an impressive 11 percent, 10-year compound annual growth rate, annual fixed UL sales had reached $6 billion dollars by the end of 2007 and represented 41 percent of new annualized premium. UL continues to lead in 2008, although growth has slowed somewhat. It was the only product in the first quarter of this year to experience an increase in sales.

Growth for fixed UL in the United States has been driven in recent years first by the stock market downturn in 2001 when the market decline drove producers and their clients away from the more volatile variable universal life (VUL) products (See Figure 2 below). Variable sales in the United States never recovered from the market decline earlier this decade due to the unwillingness of producers who went through the last market downturn to risk a backlash from their clients again. Some U.S. VUL companies have responded to the market downturn with living benefit and long-term death benefit guarantees. However, the high additional premium necessary to fund the living benefit guarantees has, up until recently, made them a hard sell.

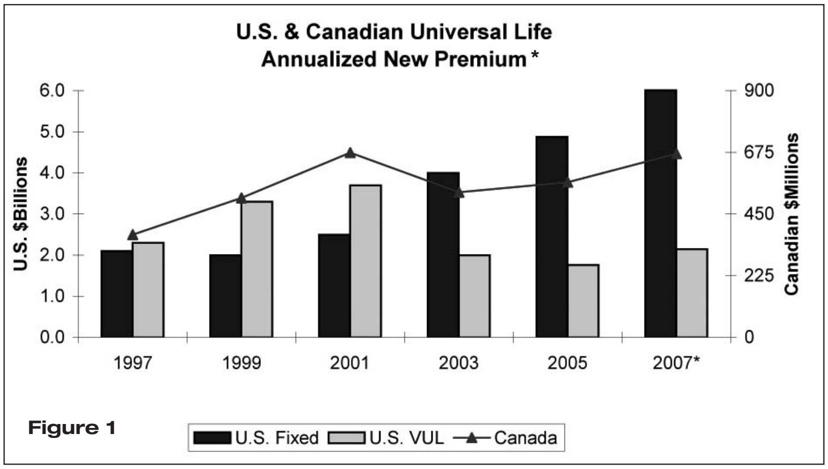

Figure 1

** Preliminary Estimates*

Source: LIMRA International Individual Life Sales Survey and LIMRA Estimates

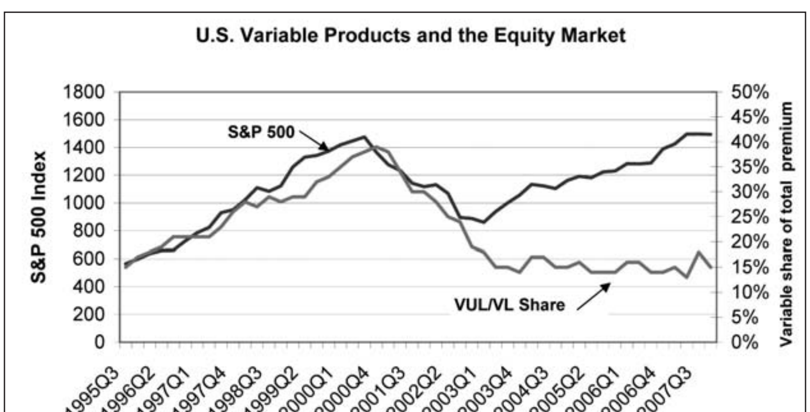

Figure 2

Sources: LIMRA's U.S. Individual Life Insurance Sales, LIMRA estimates, Economy.com

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Fixed UL sales have also been driven to some degree by nontraditional market factors, such as corporate owned life insurance (COLI) and the rise of stranger originated life insurance (STOLI) sales, and by the extremely popular secondary death benefit guarantee UL (DBGUL) products.

DBGUL products have grown swiftly and peaked in 2005 with a 53 percent share of fixed UL premium. However, guaranteed UL sales have slowed recently, in part due to some companies re-pricing their products for older ages in order to reign in STOLI sales. A good portion of the initial DBGUL sales were replacements and some are theorizing that the pool of policyholders who might be replacement candidates is starting to dwindle. STOLI is also starting to appear in the sales of current assumption products as well—shifting some of that high premium growth away from guaranteed products.

Across the border, universal life in Canada is just as popular and also holds the majority share of new premium. Growth has been slightly less spectacular than that of its fixed UL counterpart in the United States, with a 10-year compound annual growth rate of 6 percent. Its growth is close to the 6.4 percent CAGR for U.S. fixed and variable UL combined however. Canadian UL products behave more like VUL in the United States. Although a handful of traditional, current assumption UL products are sold in Canada, the vast majority of UL products allow buyers to invest their premium in indices, some more volatile than others.

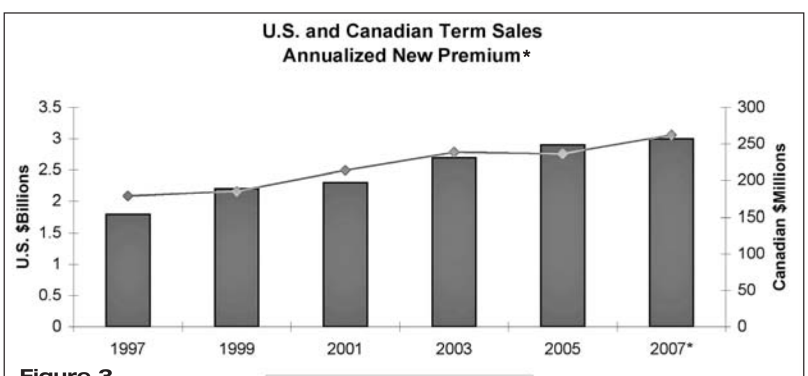

Figure 3

* Preliminary Estimates

Source: LIMRA's Individual Life Sales Survey and LIMRA Estimates

These products are not the same as U.S. equity-indexed products and do not provide the same downside protections. UL sales in Canada experienced the flight to safety seen in the United States for variable products. Unlike U.S. VUL however, UL sales in Canada have recovered, perhaps as a result of less risky indexed investment options.

The future of universal life in both the United States and Canada is dependent on a number of factors—first and foremost the performance of the stock markets and the direction of interest rates. Given the skittishness of the U.S. market, it is not surprising that VUL sales began the year with a decline. A recovery looks unlikely in the near future. Universal life sales in Canada have so far weathered the storm. Time will tell if that will continue.

Sales of UL in the United States will also be impacted by COLI and by the continued presence of STOLI sales, which produce wide swings in premium results. So far, STOLI has not been an issue in Canada and hopefully will not be going forward. Also, as we near the deadline for the new CSO tables in the United States, there may be a fire-sale in VUL as there will be new limits on the amounts people can fund their policy before it loses the favorable tax treatment given to life insurance.

Hot: Level and ROP Term

In terms of policy sales, term insurance is the leading product, representing nearly half of all policies sold in both the United States and Canada. In terms of new premium, term insurance has been a steady performer in both countries. Term sales in the United States have increased each year, with the exception of 2001. At that time, sales decreased after a dramatic increase prior to the introduction of Regulation XXX, which was expected to increase reserving requirements and therefore term prices (See Figure 3, left). Term has also increased steadily in Canada, with a 3.9 percent compound annual growth rate over 10 years. This excludes term to 100 (T-100) products, which functions more like a permanent product in spite of its name.

Specific products have been more successful than term products in general. Guarantees have also been a strong driver of term sales. Twenty-year term is the top seller in the United States at the moment, with a little over one third of new policy sales. Yearly renewable term (YRT), which accounted for one third of new policies a decade ago, now holds a minimal share of the market. Return of Premium (ROP) term has been a hot product in the United States recently as well. Sales of ROP term have helped drive increases in 15- and 30-year term products—with the most dramatic effect on 30-year term. ROP term represents about 10 percent of new premium, and about half of ROP policies are sold with a 30-year guarantee. The additional premium cost has less of an impact over a longer period, making the longer premium guarantees more appealing. This is also a product that is often sold in the mortgage market and the premium guarantee is sold to match the period of the 15-, 20- or 30-year loan.

Premium guarantees are getting longer in Canada as well. Several companies have recently introduced or increased their focus on T-30 products in response to an increase in longer mortgage loans. YRT is non-existent in Canada. The only exception to the success of longer guarantees in Canada is T-100, which again is closer to a whole life product and has been declining in recent years due to profitability issues.

Term will always be a popular product among consumers because of its affordable premiums and simplicity. Sales have slowed in the United States in recent quarters. ROP term, which had contributed to some companies' sales increases, has leveled off. The product's presence in the mortgage market has the potential to hurt growth given the current state of the U.S. housing market. Canadian term products managed a 3 percent increase in the first quarter of the year, benefiting from re-pricing and product introductions. According to a March 2008 article in the Insurance Journal, with long-term debt climbing to all time highs, term sales are expected to increase through 2008 as Canadian consumers look towards estate protection and voluminous loan balances in the event of death.

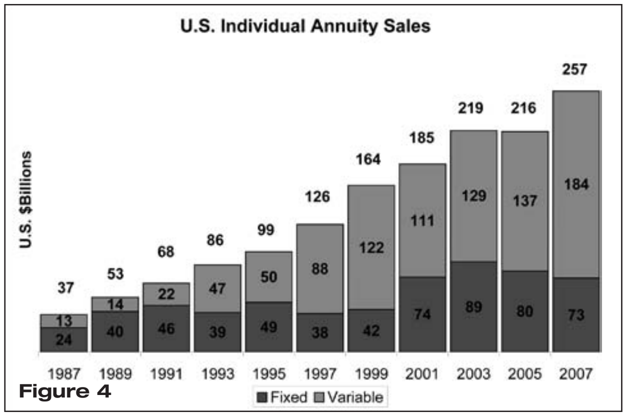

Figure 4

Source: LIMRA International, Individual Annuity Market: Sales and Assets

Individual annuity sales in the United States have grown at an annual rate of 10.2 percent since 1987. ... A similar trend is evident in Canada.

Super Hot: Variable Annuities

Annuities are definitely a hot product in both the United States and Canada. Among the oldest members of the baby boomer generation, ensuring financial security in retirement is a top concern. Individual annuity sales in the United States have grown at an annual rate of 10.2 percent since 1987. In 2007, sales increased by 8 percent and reached a record $257 billion (See Figure 4 above). As in recent years, sales were driven primarily by variable annuities, which grew by 15 percent over the previous year to $184 billion (another record). Fixed annuities in the United States have languished, with some pockets of success in indexed products and qualified plans, primarily in the IRA rollover market.

A similar trend is evident in Canada. Total sales have been increasing rapidly, reaching

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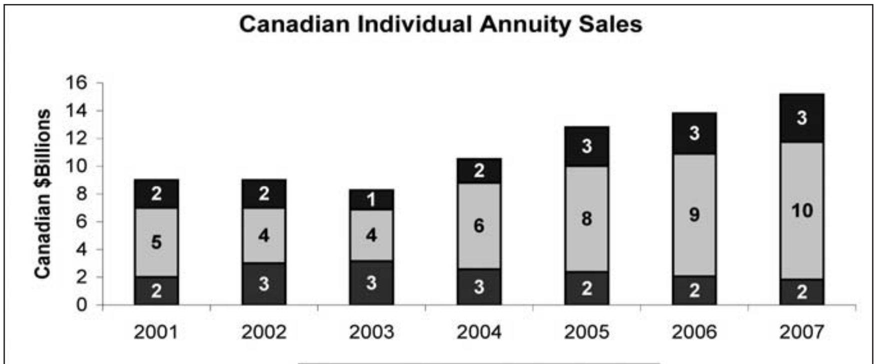

Figure 5

Source: LIMRA International, Individual Annuities In Canada

$15.1 billion in 2007 (See Figure 5 above). As in the United States, annuities with the potential for a higher, variable return have been selling the best in recent years. In Canada, buyers can choose to invest their premiums in a fixed annuity, segregated fund-based annuities, or a combination product which provides both investment options. Segregated funds are tax-advantaged funds with a variable return, but also include a minimal guarantee, in which a percent of the principal is guaranteed upon death or maturity of the contract. Segregated fund-based annuities grew 19 percent in 2007 and have increased 11 percent on average since 2001. Among combination annuities, nearly 90 percent of new premium was invested in the segregated fund options.

One of the reasons for the recent expansion of U.S. variable annuity sales was the introduction and subsequent success of guaranteed living benefit (GLB) riders. Although guaranteed minimum income benefits (GMIBs) had been in existence since the 1990s, the major market downturn in 2000 through 2002 sparked new interest in guarantees and eventually led to the launch of guaranteed minimum accumulation benefits (GMABs) and guaranteed minimum withdrawal benefits (GMWBs). The latter, first marketed in 2002, did not require annuitization and were originally return-of-premium benefits. In 2004, guaranteed lifetime withdrawal benefits (GLWBs) appeared and quickly overtook the GMWB as the most popular GLB.

In a recent LIMRA study—which represents roughly 93 percent of industry sales—the option to elect a guaranteed living benefit was available for 91 percent of newly-issued variable annuities. Of those where the benefit was available, 77 percent of purchasers elected at least one GLB.

Canadian annuity providers and producers are closely watching the recent introduction of GLBs to the Canadian market. To date, anecdotal evidence indicates these benefits are selling very well, although we do not yet have hard data to support this.

U.S. and Canadian annuity sales in the next few years should remain strong as the need for retirement planning will be high. It remains to be seen if variable products will weather the current uncertainty in the economies and stock markets in the respective companies. As of the first quarter of this year, variable sales in the United States were flat for the first time in years, while fixed annuity sales grew by 31 percent. Similarly, in Canada sales were down in the first quarter due to weak sales of segregated fund annuities. If the new GLB riders in Canada continue to take hold, they may mitigate a downturn. U.S. companies are adding to the appeal of some of their GMWB and GMIB riders including more frequent resets and inflation protection.

A Learning Opportunity

So, while U.S. and Canadian products have their differences, there are many similarities in both product types and sales performance. An analysis of each other's products provides a wonderful opportunity for companies in both the United States and Canada to watch and learn from each other's experience. The future looks bright for many of these hot products in their respective home country. It will be interesting to see going forward which product features cross the border and how those that do fare in the other market. □

Karen Terry, FLMI, is Manager of Product Research for LIMRA International. She can be reached at kterry@limra.com.