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FORECASTS FOR THE FUTURE -- THE YEAR 2000

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- What does the future hold for the insurance industry?
- The panelists will engage in a discussion and forecast of the environment in the year 2000. The following aspects will be covered:
  - Demographic trends and outlook
  - Economic outlook
  - Political and regulatory directions
  - Future retirement practices
- Following this forecast, the discussion will center on the implications of this future environment for insurance products.

MR. BARRY S. HALPERN: Mr. Niels Christiansen will lead off with comments on the demographic and social environment in the future and its implications.

MR. NIELS CHRISTIANSEN: There are several major demographic trends I will comment on today, but the one I would like to begin with and center on is the aging of America. Of all the major demographic trends that we are faced with today in the United States and the world, age and the changing distribution of age, especially in the United States, is something that we can both predict fairly accurately and make some inferences based on what has happened in other

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countries who have gone through similar experiences. Much of my work of looking at American society and observing change and trying to answer what that means to the insurance industry is helped by my experience of living in South America for five years, Sweden for five years and working in Switzerland for about four years. Many of the things that have happened in the U.S. have already happened in countries such as Switzerland or Sweden; they have gone through a significant change in the age distribution. The reason that I think age is so important is because age is one of the basic factors that affects our attitudes and our behavior, especially when it comes to economic behavior and what we think about life insurance. The life insurance industry was founded on the need to protect widows and orphans of men who were going to die too early. However, since our population now is living much longer than it used to, the concern over premature death is being replaced by a concern over living too long. The major questions become "How am I going to protect myself and how am I going to support myself as I live to be 70, 80, 90 or 100 years of age?"

I'd like to talk about some history and projections about the percentage of the population over age 65. In 1900 in the U.S. 1 out of every 25 persons was over the age of 65, but by 1980 this was down to 1 of every 9 persons. By the year 2030 the census bureau predicts that 1 out of every 5 Americans is going to be over the age of 65. This is about the same ratio that we have in the state of Florida right now. To give a little perspective, imagine a St. Petersburg, Florida, but a St. Petersburg, Florida that covers the entire country: park benches in the middle of the block, electrified carts replacing automobiles, people driving four-wheeled bicycles. That gives you some idea of what the American landscape is going to look like in the year 2030. As we look at the growth projection, however, it isn't completely a steady growth and this is something very important for us to realize. The great increase doesn't happen all at once. Since 1970 we have been experiencing a steady growth in the over 65 population. The forecast for 1990 is that there will be 32 million, but by the year 2000 it will only increase to about 36 million. We see leveling off around the year 2000. The reason for that is the baby bust of the 1930s during the depression. It then picks up because the baby boomers start to come into the over 65 age group.

I want to direct your attention not to the over 65 population, but rather that segment of the population that is 50 to 65 years of age. Between 1990 and 2000 this is the age group that is going to increase the most rapidly. This age group is not only important because of its increasing size, but it is also very important because of its buying power. Even though it only makes up 14% of our population today, the 50 to 65-year age group controls 34% of our discretionary income in the U.S. It is a relatively small group but it has tremendous buying power. The 50 to 65 year age group is going to go from about 33 million in 1984 to about 56 million in the year 2010. This is the next big change in age distribution that we're going to see in the United States. The main reason for this is the baby boom. We used to talk about population pyramids and back in 1970 we had something that resembled a population pyramid with the baby boom making up the base. However, as this baby boom works its way through the population pyramid, we see that we don't have a pyramid anymore. This has been referred to as a snake swallowing a pig because it is this great big population group that is hard to swallow and provide jobs for and as it works its way up the age distribution you can see that our population pyramid is no longer a pyramid. It is more like a rectangle now. This is called the squaring of the population pyramid. This obviously is going to have a tremendous impact on the number of people who are 50 to 65 years of age and who will become retirees in the beginning of the 21st century.

Because of the importance of the 50 to 65-year age group during the coming years, the American Council of Life Insurance (ACLI) surveyed a national sample of persons 50 to 65 years of age this past year to get an idea of their attitudes and perceived financial needs as they prepare for retirement. We refer to this age group as "prime lifers." Overall, the results of our study indicate that prime lifers are facing their retirement with a lot of confidence and optimism. Most prime lifers feel financially comfortable, and they expect to remain so. Eight in ten say they're satisfied with their family's current financial situation. Likewise, 7 in 10 feel somewhat secure about their financial situation ten years from now.

Behind their widespread optimism, however, lurks a pervasive insecurity about their financial future. A majority is worried that inflation will reduce their standard of living during retirement. About 40% worry about becoming financially dependent on others and about not having enough financial resources to meet their basic expenses. Thirty-six percent worry that they won't have enough money to really enjoy life in retirement.

Another sign of insecurity is that about half the respondents don't believe that the Social Security system will be able to pay them full benefits after they retire. The fear of physical dependency caused by catastrophic illness is the most frequently expressed worry among prime lifers, with 53% worried that catastrophic illness could wipe them out financially. Forty-seven percent worry that a major illness or disability will deplete their savings. Forty-one percent say they worry about whether they will have sufficient funds to cover their medical expenses in retirement.

On top of all this fear lies a gross overestimation of the costs which the government will pay. Prime lifers either don't know or they overestimate how much of their medical expenses are covered by Medicare. When we asked them to estimate the proportion of costs covered by Medicare, only 22% correctly estimated that Medicare will cover less than half of their medical expenses. Fifty-five percent of prime lifers aren't confident that the current extent of Medicare benefits will continue and 2 out of 3 of them believe it is necessary for people over 65 to have health insurance to supplement Medicare.

I'd also like to talk about the need for long-term care. As many of you know, we have a time bomb ticking away in this country in the area of long-term care. Almost all prime lifers, regardless of income, are uninformed or mistaken about the cost of long-term care. Only 12% knew that a month in a nursing home costs over $2,000.

Most prime lifers are also uninformed about Medicare coverage of long-term care. Sixty-four percent had no idea what proportion of long-term care costs are covered by Medicare. Among those who gave an estimate, it was widely believed that Medicare covers a majority of costs for long-term care. In fact, Medicare covers only short-term nursing care for those recuperating from a hospital stay. If the prime lifers feel insecure about meeting pertinent needs, it is with good reason.

I would like to present to you the idea, that in fact these fears about the future of the 50 to 65 generation are going to be what is driving our national political agenda as well as our national social agenda for the next fifteen years. The reason for this is that besides the increase in the over age 65 population we are experiencing right now, the baby boom as it has in the past, is going to be setting our national value priorities both politically and socially. Think back to the last twenty years. They have been doing it already. When the baby boomers were born back in the 1950s, what were our national values centered on? What were the national ideals? It was Ozzie and Harriet in the suburbs raising children. What became our national set of values in the 1960s? What was dominating our national consciousness? It was the baby boomers reaching teenage years. It was the youth rebellion. It was the counterculture. It was the expression of unbridled youth. What became the center of our national consciousness in the 1970s? It was basically the indulgence of young adults, the ME generation, individual freedom, experimentation with drugs, and putting off marriage and family and enjoying young adulthood while they could.

What do we see entering our national values/priorities right now? It's a return to the family, because the baby boomers are starting to have children of their own. What is the #1 television program? "The Cosby Show," alternating with "Family Ties." In the Washingtonian magazine that comes out once a month, about two months ago there was a front page article saying "GOD is back." Why is God back? Because the baby boomers want to take their children back to church to get them a religious education. It is because the baby boomers have reached this stage of life.

As we have witnessed in Europe, once a large number of the population is over 50 years of age the national consciousness becomes inevitably directed toward questions of personal security. In both Sweden (which is a highly socialized country with a national health care system and a national pension system) and Switzerland (which is probably the most capitalistic country in the world) we've seen that when enough people get to be over the age of 65, not only do they start to demand a guarantee of personal security, but they also begin to set the values for the rest of society. The entire society becomes fixated upon the questions of personal security. As the baby boomers reach this point, I believe the same is going to happen to the United States unless we are entirely different from every other European based country.

In fact the generation that is right behind the baby boomers is in a perfect position to be influenced by the baby boom generation. The baby bust is a generation lacking almost completely the youthful idealism that characterized the baby boomers in the late 1960s and early 1970s. A survey of UCLA freshmen in

1971, and again in 1985 asked one question: "What is the most important thing to you in terms of getting a college education?" In 1971 the freshmen said "To serve humanity; to improve the world; to do something for the country." In 1985, what they said was "To guarantee my financial success; to guarantee my financial security."

This latter group went through the value formation stage during the difficult inflationary times of the 1970s, and it is a group which lacks the size to make the impact of youth felt across the country. So, I am convinced that unless something radically different happens in this society than is happening in every other society, the national consciousness is going to be increasingly directed toward personal security.

Thinking of the 3-legged stool that supports personal financial security for individuals (the federal government, the employer, and the individual) we asked our prime lifers who they think has primary responsibility for guaranteeing their financial security in the future? We got back a surprising answer. About 25% of them said a combination of the three. About 30% said the government. About 30% said the individual and only 7% said the employer, through their pension."

I would like you to remember that figure. Because, I think one of the primary questions facing us as a country and industry is, "Who is going to be responsible for financing the personal security of the current 50 to 65-year old generation, and the baby boomers when they reach that age? Is it going to be the federal government? Is it going to be the employer through defined benefit or defined contribution plans? Or, is it going to be the individual, forced more and more to take personal responsibility for his/her own pension, retirement and future financial security?

The next major trend I will discuss is the entry of women into the workforce. Nearly half of all workers today are women, up from 33% only 20 years ago. Besides having a liberating effect on women themselves, women's entrance into the labor force has produced affluent two income families who can afford products like universal life insurance or disability insurance. But greater employment of women has also made divorce economically feasible, and conversely, divorce has forced many women to take full-time employment who otherwise might not want to. So, in short, American household composition has undergone radical change.

The percentage of nonfamily households are on the rise, up from 19% of all households in 1970 to 27% in 1983. Conversely, in 1970, married couples made up 73% of all households; by 1985, this figure had dropped to 58%.

Divorce continues to make its impact felt among married families with children. In 1983, 25% of all children were living in single parent households, most of them maintained by mothers and it is estimated that 45% of today's children will have lived in a divorced family by the age of 18. Currently, one out of every five children is born out of wedlock. All of these factors have weakened the family's ability to function as the real Department of Health and Human Services and makes the government a poor substitute for the family.

The reduced household income which has resulted from slow family formation and divorce has made paying deductibles and co-payments much more threatening to the household budget. It is no wonder that the American middle class seems to embrace HMOs and PPOs, as long as they have some choice and are satisfied with the quality of care they receive.

Another demographic trend is poverty and trends in black income. There have been numerous figures thrown about and considerable discussions on the crucial question of whether blacks have advanced, retreated, or stayed the same economically in the past 15 to 20 years. The truth of the matter is that, according to the U.S. census, the median income for black households was the same in 1984 as in 1967, after taking into account the effects of inflation. In 1984, the median income of black households was $13,500 versus $13,500 in 1967 (in 1984 dollars). However, these figures mask some of the most important income trends to have taken place in the past few decades. A recent study by the Rand Corporation of economic progress among blacks since 1940 concludes that the income gap between whites and blacks is narrowing:

> "The changes over the last forty years were dramatic. . . . America has made considerable strides in reducing Black poverty. . .but [it] remains at unacceptably high levels. However, the real story of the last forty years has been the emergence of the Black middle class, whose income gains have been real and substantial. Finally, a sizable

> number of black men are economically better off than white middle-class America."

The major fact about black income is: black married couples with families have made gains in median income, while black families led by women have fallen behind since 1971. Nonetheless, for blacks and whites alike, being married means keeping ahead of inflation. For many married couples with families, the entry or reentry of mothers into the labor force was a hedge against inflation through the 1970s and early 1980s. Black married couples with families had a median income of $23,418 in 1984, over $2,400 more than in 1971, even after inflation. To me, a major, and surprising finding is that this economic advance among black married couples is greater than the economic advance of white married couples between 1971 and 1984.

It is clear that a major factor holding back black household income is the dramatic increase in black households without a man present; from 28% in 1970 to 43% in 1984. We have witnessed an increase, also, in our white population of female-headed households from 9% in 1970 to 12% in 1984. But the percentage among our black population is obviously of much more significance.

In 1984, nearly 1.9 million black families (30.9%) had incomes below the poverty level of $10,609 for a family of four. For the same year only 9.1% of white families had an income below the poverty level. The poverty rate for families of both races, while slightly higher in the early 1980s than during the 1970s, began to decline in 1983.

Black families comprised of a married couple have made economic advances in the last 15 to 20 years and this is obviously a positive sign for your companies. But by far, the fastest-growing sector of the black population is that of poor single mothers.

The next trend is the increasing affluence in America. By any standard whether it be home ownership, rooms per person, age of home ownership, family income, or disposable income, we as a country have grown richer and enjoy a clearly higher standard of living than we did 25 years ago. Basically, three groups have benefitted from the increased affluence: two income families, the 50-65 age group, and retired Americans.

The group which has shown the greatest economic gain in the last 25 years is our elderly population. The percent of elderly people living below the poverty line has dropped from 25% in 1970 to 14% in 1983. Because they have no dependents, elderly households have a higher per capita income than all people under 50 years of age. Having paid off their mortgages and having lower living expenses, elderly households have the highest per capita discretionary income and the highest household financial assets of any age group. While it is unacceptable that 15% of our older persons live in poverty, it is clear that, as a group, they are living more comfortably than ever. In terms of their potential as consumers, we know that they are already a $4 billion market for Medigap insurance and those who have recently retired have long-term retirement needs before them that make them a very attractive market. Many companies at this time are in various stages of developing long-term care products and other retirement oriented products, and time will judge their success or failure. The growing affluence of this segment of the American population means that individually purchased insurance products have become more of a reality. Disability insurance, supplemental medical insurance, long-term care insurance, individual medical accounts (if they become a reality), annuities, universal life insurance -- all these products have a bright future because of the steady rise in affluence in the U.S. It is important for us to target the dual-income families, the prime lifers and the younger, more affluent retirees with such products. I think that we're just scratching the surface at this point with such products.

The last trend I'd like to talk about is second only to the greying of America in terms of its impact. It is the changing pattern of immigration and the growth of new minorities. Until 1860, we were almost entirely a nation of northern and western Europeans. But, during the peak immigration period beginning around 1880, millions of eastern and southern Europeans joined in the mass immigration. By 1914, which marks the end of the peak immigration period, southern and eastern Europeans made up the majority of our immigrants and their numbers were staggering. Between 1820, when immigration records were first kept, and 1900, over 19 million legal immigrants were counted. During the peak years around the turn of the century, more than a million immigrants entered the U.S. annually, primarily from Italy, Greece and Poland. From 1930 through 1960, however, we saw another radical change, with a great decrease in southern and eastern Europeans, and an increase in northern Europeans and Latin Americans. The reason was simple. The WASP majority of the U.S. became frightened by this mass influx of southern and eastern Europeans and Congress passed restrictive immigration laws in 1929 aimed at trying to retain the ethnic composition of the U.S. as it was in 1890. Quotas for each country were set up which favored northern Europeans over all other ethnic groups.

All these quotas were changed when Congress passed the 1965 Immigration Act to try to rectify an immigration policy which had come to be viewed as tantamount to racial discrimination. Under the 1965 law, about 270,000 immigrants were allowed per year who didn't qualify as immediate relatives of U.S. citizens, with no more than 20,000 allowed from any one country. Also, around 300,000 immigrants come every year who do qualify as immediate relatives. What has the effect on immigration been? From 1965 through 1969, we experienced a tremendous jump in the number of Latin Americans and a big decrease in northern Europeans. Beginning in 1970, waves of Asians joined the Latin Americans and the Asian immigration continued to swell to 42% of our immigrants during the 1980s. Since 1960, people of European stock have dropped from about 80% of our immigrants to less than 10% today, and of course we're speaking only of legal immigrants. If we include illegal aliens, which number anywhere from three to ten million, the proportion of European immigrants is in reality even smaller.

Think of it! The European immigrants have gone from 80% to less than 10% in a matter of about twenty years. This is the most dramatic change in immigration patterns we have seen since the great immigrations of the late 1800s. Since 1965 we have admitted 6.1 million legal immigrants, and 2.2 million of these are Hispanics and Asians who have come in the last six years. Where are these people located?

California is home to almost one of every three Hispanics. Nearly 70% of all Hispanics reside in four states: California (4.5 million), Texas (3 million), New York (1.7 million) and Florida (858,000).

Three-fourths of all Mexican-Americans live in California and Texas, while over 60% of all Puerto Ricans live in New York and New Jersey. Those from Central America and South America are more scattered, but California is home to the largest number.

Asians are also concentrated in a few states, with California home to well over one-third, followed by New York, Hawaii, Illinois, Texas and Washington. Over 80% of all Asians reside in those six states. California is the principal residence for all Asian groups except Indians, who are more likely to settle in New York.

As a group, the fertility of Hispanic women is 60% higher than the U.S. average. Fertility is highest among Mexican-American women and lowest among Cubans. Aside from the Vietnamese and other Southeast Asian refugees, Asian fertility is not particularly high. Japanese fertility is well below the national average and so is Chinese. Korean and Filipino fertility rates are just about the same as the national average.

Age differences among the newest immigrants run parallel to differences in fertility. Hispanic groups, except the Cubans, are quite young. The Hispanic median age is 23, compared with 30 for the nation as a whole. This is a result both of relatively high fertility and heavy immigration of young adults. The Cuban age composition is radically different. The many Cubans aged 40 to 59 and 15 to 24 reflect the number of young and middle-aged Cubans who arrived in the 1960s following Castro's revolution and raised families in this country. Among Asian-Americans, the median age is close to that of Americans as a whole, except for the Vietnamese, who have a median age of about 21 years.

What do these new minorities mean for business in general and the insurance business specifically? First, new immigrants will probably be the solution to the expected U.S. labor shortages that have been forecasted for the 1990s due to the "Birth Dearth," which began in the late 1960s and has continued until now. Second, immigrants are jumping into all kinds of entrepreneurial activity. Koreans, for example, run nearly 900 of New York City's 1,600 corner grocery stores, and Indians own 800 of California's 6,000 motels. In Texas, Vietnamese-Americans now control 85% of the shrimp fishing business. Third, Asian and Hispanic immigrants have become new customers for a long list of consumer products.

Although Asians constitute less than 2% of the U.S. population, they're the fastest growing ethnic group in America. There are increasing at a rate fourteen times greater than that of the general population and they will triple their number by the year 2000.

Unfortunately, there is very little market research available on Asians in terms of their consumer behavior: brand loyalty, how they feel about advertisements in their native language versus advertisements in English, or their attitudes toward a sales force which speaks an Asian language. Even less information exists about their ownership of specific insurance and other financial products.

The lack of information on the Asian-American market is due to a number of factors. They've been a small segment and not a lot of people have paid attention to them. Second, you're talking about many different languages, whereas Hispanics all speak Spanish. Also, many Asians have assimilated very quickly into the American mainstream and aren't that easy for market researchers to identify.

However, the limited private market research available shows that the Asian-American market is very sophisticated due to their high educational level. They find Asian language sales materials to be helpful but not essential because most Asians learn English quickly after arriving here in the U.S. -- although that is not universally true. Those that know the Asian American market do feel that print advertising in Asian-language periodicals is a cost-effective method of reaching this segment.

Although Asian language radio and TV stations are experiencing an increase in advertisements from non-Asian owned businesses, and oriental faces are turning up in more network TV commercials, major advertising firms feel that it's more important to portray a brand as quality rather than as a product used by Orientals.

What has been the experience of the insurance business with the Asian-American market? Until recently, only a few insurance companies have attempted to target the Asian-American market. Of those companies which have had any activity in this area, most have focused their attention on the hiring of Asian-American agents. Individual agencies, particularly those located in California, have advertised in Asian language publications. One Chicago based company produced sales material in Vietnamese for an agent who planned to sell to the large Vietnamese population in Houston, Texas. The plan, apparently, was not successful. Consequently, that company advised other insurers to move slowly in the development of marketing plans and sales material aimed at the Asian market.

Other companies, however, seeing the above average income of Asian-Americans, high savings rates and strong family attitudes, see the Asian-American market as too good an opportunity for the insurance industry to pass up. One such company recently announced its effort to win over the Asian-American market. Encouraged by the success of their Chinese-American agents (the company's top agents for 1984 and 1985), the company has begun to print sales material in several Asian languages. In addition, they have begun to advertise in Asian language publications and are now considering an Asian language toll-free consumer telephone service for inquiries from Asian-speaking customers.

Companies with experience in the Asian-American life insurance market find most Asians prefer permanent life insurance because of its savings feature. In addition, individual agencies which focus on the Asian-American market report very little replacement and policy lapses among Asian-American policyholders.

Some people have suggested that Asian-Americans would be a good market for key man insurance because of the number of Asian-owned small businesses. Other products which may have success with Asians include interest-sensitive life insurance and products which save money for a child's college expenses. Because of the strong attitudes toward family responsibility among Asian-Americans, new insurance products which protect one's children as well as one's parents against financial risk may be good bets for this market.

Let's turn now to Hispanics. Because of the overall size and growth rate of the U.S. Hispanic market, American business has paid greater attention to Hispanics than they have to Asians. As we mentioned earlier, the U.S. Hispanic market is concentrated in five key States: California, Texas, Florida, New York and Illinois.

Los Angeles is the number one U.S. Hispanic market. In fact, of all cities in the northern hemisphere, Los Angeles has the second largest Spanish-speaking population (Mexico City ranks first) and is number eight in the world. New York City is the number two Hispanic market, followed by Miami, San Antonio and Chicago.

Unlike the U.S. Asian market, there's a lot of information on the U.S. Hispanic market. According to research conducted by major marketing research firms, Hispanics are not a homogenous market in terms of discretionary income, the type of products they purchase, or their English language skills. But among Hispanics in the U.S., we've found a high degree of brand loyalty.

How about language? Less than half of all U.S. Hispanics are bilingual and English language skills among Hispanics differ greatly by state. Various market surveys indicate that Hispanics highly rank the importance of Spanish language advertising and most prefer salespeople who are Hispanic or who at least are able to speak Spanish. I think the implications are obvious.

While the Hispanics who have been in the U.S. for a number of years are relatively well-off, the U.S. Hispanic market in general tends to be a low-income market. Hispanics tend to purchase life insurance policies with lower face amounts than the general population and most opt for whole life insurance or other cash value products. Educated Hispanics, such as some segments of the U.S. Cuban population, tend to purchase interest-sensitive financial products.

Much of the Hispanic market at this time is only a potential. They are young, many have low incomes, but they are upwardly mobile. They are going to college in increasing numbers and in the long run will be one of the major financial service markets, as they are for consumer packaged goods today.

Again, I want to emphasize that Hispanics are very brand loyal, and once they learn to trust a brand, look out, because they are nearly unshakeable! I think it behooves any financial services company that hopes to maintain or improve its market position in the United States to get in early and develop name recognition and loyalty.

MR. HALPERN: Tom Sullivan is counsel in the legal department of Aetna Life and Casualty and is responsible for group, pension and individual life. Tom will cover the future political and regulatory environment.

MR. THOMAS M. SULLIVAN: My speaking experience has suggested that it is always wise to begin a talk with a quotation, more than one if possible. Commencing with quotations provides at least two advantages to a speaker: it abbreviates the time for his own remarks and creates at least a possibility that the erudition cited will be attributed to him in the memory of his listeners.

FORECASTS FOR THE FUTURE -- THE YEAR 2000

How does one predict the future? For guidance, I turned to the American patriot Patrick Henry, who said, "I have but one lamp by which my feet are guided, and that is the lamp of experience. I know no way of judging of the future but by the past." Thus convinced that experience is the key, I referenced the English philosopher Edmund Burke, who said, "You can never plan the future by the past." Having failed to determine whether experience can be relied upon as an indicator of future events, I will settle for the observation of psychologist B. F. Skinner: "I remember the rage I used to feel when a prediction went awry. I could have shouted at the subject of my experiments, 'Behave, damn you, behave as you ought!' Eventually, I realized that the subjects were always right. It was I who was wrong. I had made a bad prediction."

I have been asked to postulate some possibilities for the legislative and regulatory environments we will find in the year 2000. As a former operative in the Aetna law department's government relations section, I've accumulated a few other quotations which I believe are apt when making such predictions. I'm sure you've all heard the observation of a 19th century New York jurist, "No man's life, liberty, or property is safe while the legislature is in session." I then remind you of Bismarck's cynical observation, "The public should never be permitted to see how either laws or sausages are made." Finally, as we look to the year 2000, I think we will do well to remember Seneca's soothing maxim, "Our fears always outnumber our dangers."

So let me sketch a little scene for you using the brush strokes and colorings of my experience, research, prejudices and concerns.

It is 2:00 a.m. on January 1, 2000. The last guest (a nonactuary who thus had more than one New Year's toast) has just left a party you have held for friends. Having unfrozen a nightcap using your computerized liquor center, you settle into your favorite easy chair with your dog, whom you have waggishly dubbed Elizur Wright, at your feet. You modulate the odor-reduction mechanism in your home's environmental control center and light up a Cuban cigar (the U.S. having long ago reestablished relations with the Cuban government) and begin to muse about the developments of the last thirteen years of the twentieth century. By the way, as you light up, you swear once again that this will be your last cigar, smoking having become a social no-no comparable to public drunkenness.

PANEL DISCUSSION

You are almost sixty years old, and have been the chief strategic planner for the Prudential companies since 1985. You are in good health, but don't particularly savor the eight additional years you must work before retirement, the normal retirement age having crept upward as medical science has significantly curbed the threat of the killer diseases.

In your personal and professional lives, you have been fascinated to track the social and political trends wrought by America's changing demographics. America is getting older. There has been no successor baby boom, and thus there have been very large proportional increases of those over 50. Indeed, you have predicted that more than 20% of the population will be over 65 by early in this century.

Minorities have grown tremendously as well, particularly Hispanics and Asian-Americans. You are now predicting that in twenty years Hispanics will overtake blacks as the country's largest minority. The number of Asian-Americans is growing at a rate fourteen times greater than the general population.

Not surprisingly, the elderly are increasingly affluent, having been most shielded from the effects of inflation and cuts in government spending. It very much appears that before you retire, there will be a perceptible dichotomy between youth which will be primarily minority, and the elderly who will be predominantly white.

Your company and other insurance entities have tried mightily to respond to the ever-increasing demands for enhanced health care and retirement mechanisms. Private industry has achieved some success but the nation's political system has had difficulty meeting the challenge.

Revenues have been a problem generally. Federal, state and local taxes have increased significantly on a proportional basis and federal power has slowly grown as states have scrambled for tax revenues and not finding enough, have turned to Washington. Property taxes have predictably become less significant as sources of state and local income and you estimate that early in the century direct taxes will account for only 65% of all state and local revenues.

In vying with one another for jobs, states have formed alliances and have co-operated to attract new regional industry. Those states with the best educational resources are making a resurgence. Somewhat surprisingly, the mid-western states have awakened from a long slumber and are on the ascendancy while the Northeast and Sun Belt are coming on relatively hard times.

Politically, there have been some dramatic changes. Public financing of congressional campaigns has been in place since 1993; although it was seen as a device to reduce the influence of political action committees, it has fallen short of that goal and has increased the reliance of campaigners on slick media campaigns.

The 1996 presidential campaign saw victory for the Democratic candidate, for the first time a man of Italian extraction. Also for the first time, a woman became vice president. Voters have continued to be generally apathetic in state and local as well as federal campaigns, but those that take an active role are more angry and aggressive than ever, and strong coalitions have formed of minorities and special interest groups. Candidates have eschewed their parties and have chosen instead to build their own constituencies with many pandering to the desires of older Americans and minorities. While voters are generally more conservative, because active voters continue to be older, it is now more clear than ever that social wants have become social needs with increased pressure on government spending, increased taxation, a continuing demand for greater income redistribution and greater employment benefits.

As you predicted, Congress was unable to tackle successfully the budget deficit, leading to a constitutional amendment to limit government spending in the mid-1990s. Four years down the road, it's still difficult to gauge the results; the cuts made most readily were in defense spending (Star Wars was cancelled in 1990) and in social programs having small or ill-organized constituencies. You're not even guessing where they go from here.

Business and private life continue to be influenced by the incredible growth of computers. You are proud of your computer skills, but concerned that those unwilling or unable to use computers may have become a permanent underclass. There has been no fundamental progress in race relations. There are still the haves and the have nots. One of six workers is on a government payroll, about the same as fifteen years ago. It has been a relatively stable economic period.

Unemployment has remained in the range of 6% to 7% for the last fifteen years. Eighty percent of families now have two incomes. There has been a tremendous increase as well in single person households.

Despite the best efforts of government, interest rates have continued to be unstable and despite the increasing progression of the income tax, it was necessary to install a small value added tax in 1997.

National health insurance has never made it onto the books, but there is increasing demand for it as hospital costs continue to rise primarily because usage has continued to decline dramatically in recent years, the older population utilizing flourishing long-term care facilities. While there have been no watershed breakthroughs in longevity, significant progress has been made in many of the killer diseases such as heart disease and cancer. The nation is still recovering both psychologically and economically from the AIDS crisis which culminated in the development of an effective vaccine in 1995. By that year, over twelve million Americans had developed the antibody and it long ago was conclusively demonstrated that virtually all seropositive people will die a premature death. Already, two million deaths have been linked directly or indirectly to AIDS. The enactment of state health insurance pools came too late to help much. The insurance industry opposed the establishment of pools that did not include private employers, and the ERISA roadblock to inclusion was not removed until a Supreme Court decision of 1994. The states sought to cope with the AIDS problem through a combination of direct employer payroll taxes and the use of federal funds, but the task ultimately proved impossible to solve at the local level and massive infusions of federal funds have been necessary to support treatment at hospital and other facilities.

As you take another puff on your cigar, you ponder the changes at your place of employment as emblematic of those that have occurred in the insurance industry generally. The Prudential is still primarily an insurance underwriter but the game has changed very significantly. Now its insurance operations are only one part of its very diversified financial enterprises. In 1992, it joined a host of other major financial powerhouses in becoming a registered financial services holding company under the Financial Services Holding Company Act of 1991. As such, its operations are regulated by the Federal Financial Services Control Board, an amalgam of portions of all the federal supervisory agencies that up until its formation in 1991 controlled the discrete operations of financial services entities. As now constituted, it consists of elements previously housed at the Federal Deposit Insurance Corporation, the Federal Reserve Board, the Securities and Exchange Commission, the Federal Savings and Loan Insurance Corporation and the Comptroller of the Currency. Virtually all financial services conglomerates are regulated by this entity, each subject to a variety of requirements, primarily depending on the level of involvement in traditional banking activities.

State insurance departments continue to regulate the solvency of insurance enterprises domiciled in their jurisdictions, but have absolutely no part in the integrated regulation of the conglomerates. You continue to believe that insurance commissioners should have played a more aggressive role in the shaping of financial services regulation. Ironically, the erosion of state regulatory primacy over insurance began at the state level, when in the absence of comprehensive federal regulation at the end of the 1980s, bank holding companies secured a firm foothold by exploiting what was then called the "South Dakota loophole," abetted by a 1989 Supreme Court decision upholding their right to enter the insurance business through the acquisition of state-chartered banks having insurance powers.

Besides having convinced Congress (at last) of the dire necessity of comprehensive financial services legislation, this decision seemed to take what remained of the wind from the NAIC's sails. Instead of aggressively promoting the benefits of traditional insurance regulation, the NAIC watched passively as Congress stripped the insurance exemptions from McCarran-Ferguson, thus allowing the Federal Trade Commission to release its pent-up insurance predilections.

State insurance regulation thus began its regression to its original functions, monitoring the solvency of insurance entities, more dependent than ever on its uneasy partnership with federal regulators. The process was accelerated by the tremendous growth of self-insured plans even among relatively small employers, spurred by aggressive third party administrators and unyielding state legislatures.

The catch phrase of this hasty regulatory evolution was, and remains, "functional regulation." And it has worked reasonably well. Indeed, it is difficult to visualize any other kind of regulation being capable of dealing with the startling complexity of today's life and annuity products, intertwined as they are with investment and savings features. You see another round of unbundling coming, wherein simplicity will (once again) become the key to enhanced sales.

Commercial banks and savings institutions, although retaining distinct nomenclatures, are virtually indistinguishable from one another. Their functions are dictated by their form of organization. While no one kind of traditional financial institution dominates among the new super-corporations, the landmark joinder of the last few years was CitiCorp's acquisition of Aetna Life & Casualty in 1997. Perhaps not surprisingly, the amalgamation is not yet complete and rumors abound of cultural differences that have made the marriage rocky. Nonetheless, the resulting super-corporation is impressive if only because of its size and the influence it wields.

Mergers and acquisitions have, of course, been rampant for the last few years, permitted, indeed encouraged, by the government in a continuing attempt to respond to the growing domination of foreign financial giants, especially those of Japan and West Germany. The CitiCorp/Aetna joinder caused the biggest splash, but others were no less remarkable. General Electric, through the acquisition of several small insurers, has become the 20th largest writer of life insurance and annuities. And the total number of freestanding life companies has been reduced to just over 1,200.

There have been fundamental changes in insurance distribution channels as well. There are many fewer agents and agencies than only a few years ago. Those who remain are members of relatively large organizations and are characterized by their aggressiveness and sophistication. While financial "supermarkets" have largely failed, the sales of many kinds of insurance are now accomplished by computer with service and price being the foremost considerations among shoppers. The advent of widespread computer usage made cost of paramount importance and at least indirectly contributed to a casualty/property down cycle which was the worst of the last sixty years. A rash of small casualty company failures and restoration of more realistic pricing have stabilized the industry somewhat, but experts, including yourself, are already predicting another fierce price war within the next five years.

Old-line brokers have now become principally consultants, marketing not only insurance, but comprehensive advice to self-insureds and in some cases even providing capacity.

Foreign markets have exploded, providing competition not only to U.S. insurers abroad, but also in a variety of lines, especially high risk coverages, in the U.S. itself.

Unfortunately, the Herculean efforts of the casualty industry to enact "tort reform" in the late 1980s accomplished much, but failed to stem completely the tide of litigation and huge plaintiff awards. There is increasing use of arbitration and mediation, but you and others predict that it will be many years before a more rational system of compensation is in place, if ever.

The erstwhile life mutuals have done very well in the property-casualty lines, using to great advantage their agent loyalty, long-range planning expertise, diversification and their enormous financial capacity. Virtually all of them, Prudential, Metropolitan, Equitable, The John Hancock, Mutual of New York and New York Life are financial services holding companies, although all retain a strong insurance identity, reflecting their origins.

The last few years have seen the advent of innovative coverage techniques such as no-limit, no-peril, all-risk policies with stiff deductibles. Risk classification is still an issue but unisex rating has not made the inroads that its proponents foresaw ten or fifteen years ago. There continues to be an increasing use of the insurance mechanism to deal with perceived problems of social inequities including a recent effort by the State of Massachusetts to base auto premiums on affordability. Individual life and health lines have stagnated while group coverages have flourished, in part because individual products have increasingly been sold in a quasi-group format, for which, unfortunately, the states with the most lenient standards have become the regulatory norm.

In sum, the insurance industry has coped reasonably well with changes in the financial services marketplace. Although the market is dominated by relatively few large players, there has remained room for smaller enterprises of various kinds to serve select market niches and to be quite successful.

Well, it's almost three o'clock and you catch yourself dozing. Elizur is sound asleep at your feet. Some things have not changed. As on every recent Christmas Eve, a few days ago you read your grandchildren selections from *A Christmas Carol.* As you contemplate the future, you remember the graveyard scene where the Ghost of Christmas Yet to Come points to Scrooge's tombstone and will not respond to his pleading question, "Are these the shadows of the things that will be or are they shadows of the things that may be, only?"

Well, you and I know the answer to Scrooge's question. He said it himself: "Men's courses will foreshadow certain ends, to which, if persevered in, they must lead. But if the courses be departed from, the ends will change." I suggest that as we look to the year 2000, we could do worse than be hopeful, and remember the words of Tiny Tim, "God bless us, every one."

MR. HALPERN: Ed Friend will speak about employee benefits and the implication of the future environment on benefits design.

MR. EDWARD H. FRIEND: Mr. Bowen Northrup, writing in a recent *Wall Street Journal Supplement* on the general subject of Aging, observes, "when the American Republic began, life expectancy was 35. Now it is 75, and bizarre disparities result. Lots of today's older people have bodies that physically test out at several decades less than their ages." Robert Butler, head of the Department of Geriatrics at Mount Sinai Medical Center in New York, recalls a family in which a healthy 85-year-old woman cares for an ailing 65-year-old. . .her own child.

Butler says that 50% of all 85-year-olds are "going concerns." But many 65-year-olds are ready for the rocking chair. Clearly genetic factors figure in these disparate patterns of aging. Diseases that strike some people at 60 leave others (and their progeny) untouched until 80 or later.

With respect to that portion of the population that remain "going concerns" well into the upper ages, I am reminded of a gentleman I know who recently visited the company doctor for the usual retirement physical, a service generously provided by his employer for those moving from active to pensioner status. After examining Bill for about 15 minutes, the doctor expressed amazement at Bill's unusually fine physical condition. He said: "Tell me Bill, when did your father die?" "Who said my father died?" queried Bill. "Why, he's got a farm in Maine. . .is up every morning at 5:30, feeding the chickens and the hogs and baling his own hay. . . He wants me to come up and help him. . .but he really doesn't need me. . . He's doing all right by himself." The doctor was amazed and asked, "OK Bill, but tell me. . .at what age did your grandfather die?" Bill snapped "Who said my grandfather died?. . .Why, last week he got married!"

"Why would a man who is probably 110 years old want to get married?" the doctor asked, half in shock. "Who said he wanted to get married?" was Bill's reply.

More on the disparate physical conditions later.

Let's focus on the health care issues mentioned by both Mr. Christiansen and Mr. Sullivan. By the turn of the century many state legislatures and eventually the U.S. Congress will have grappled with questions such as:

1. Is unlimited health care a right of every citizen, wealthy or indigent?

2. What percentage of the GNP should be dedicated to health care? If the cost of providing unlimited care to all would exceed an acceptable percentage, how do we close the gap? How do we ration medical care?

3. Should all workers have a minimum level of health coverage to be financed in large part by their employers?

4. If so, what shall the minimum menu of coverages be and how much cost may the employer shift to the employee?

5. Will the minimum menu of coverages be supplemented by a national program of catastrophic medical expense reimbursement when employer sponsored program benefits plus out-of-pocket costs exceed so much money?

6. If, indeed, catastrophic coverage is to be provided, how much other financing will be required before catastrophic protection cuts in if indeed catastrophic care is to be provided? Will it be a fixed dollar amount? Indexed

upward? How? A regular consumer price index (CPI) or a medical CPI? Or will it be a percentage of W-2 compensation for active workers?

7. What about the unemployed, the indigent who have no out-of-pocket resources?

8. What about retirees, spouses, children, etc?

9. Will catastrophic coverage be provided through a socially financed vehicle? If so, will the cost be collected from the employee and the employer or will general revenue be a third source?

10. Will employers be permitted to opt out of a federally sponsored program of catastrophic coverage, diverting payroll taxes otherwise payable to facilitate company/employee financed protection?

11. Is the concept of catastrophic insurance doomed to fail, despite its apparent answer to everyone's fears about being without medical care? Will it fail because catastrophic insurance implies unlimited medical care unless deductibles are so high that catastrophic coverage will not be a reachable reality for many, an unacceptable social alternative?

12. What will attract students to the medical profession if the arduous training and sacrifice lead to controlled income opportunities? And what about the cost of medical malpractice coverages?

13. Finally, what about the issue of the "right to die"?, extended use of life support systems, etc.?

All are questions with no answers. On the funding front, the next Congress will likely deal with the head-on collision between the need to raise additional tax revenue and the desirability of encouraging the financing of private post-retirement medical coverage supplements to Medicare through tax exempt insurance trusts or other trust accumulations. This is another issue without an answer today but which by the year 2000 will long ago have been answered, with advance funding approved despite loss of tax revenue.

FORECASTS FOR THE FUTURE -- THE YEAR 2000

By the year 2000, the cost of medical coverage supplemental to Medicare will be escalating at a rate far in excess of the rate of growth in medical care costs alone. This is because the increasing cost of supplements will be leveraged, as the level of underlying base Medicare coverage is controlled and perhaps even reduced.

Employers will increasingly provide lifetime maximums as retiree medical coverage. It will be more a question as to when, not whether, the maximum will be expended. Retired workers and their spouses will spend the maximum "nest egg" judiciously.

Responsibility for paying for retired Medicare supplements will shift to the employee. He/she will pay the costs and claim reimbursement from the insurance company or trust fund accumulated maximum "nest egg" financed by the employer. Certain medical care expenditures will qualify for reimbursement and others will not. But the prospect for eventual exhaustion of the maximum will be on the horizon. At death, remaining funds will revert to the funding employer for use in financing "nest eggs" for other retirees.

By the year 2000, we will not yet have come to grips with the haunting recognition that a major proportion of retirees and their spouses will need to rely on Medicare and Medicaid as their only source of care. But they simply won't be enough by current standards.

By the year 2000, corporate sponsored medical centers will have begun to proliferate. These will be the successors to independent HMOs and PPOs. The majority of medicine will be moving to or have gone the corporate route. Doctors will be employed by the corporate medical center of a major employer or a consortium of employers. Hospitals, presurgery and post-recovery outpatient hotel-like facilities, ambulatory outpatient surgicenters, illness treatment centers and all other medical care services will be provided in this one complex for enrolled employees. Under affordable insurance programs, employers will be reasonably protected against potential oppressive malpractice litigation as the result of a newly defined "best effort" criterion for acceptable medical care.

Employees will share the cost through payroll deduction. Specialty medical services such as burn units, expensive new equipment not needed in every headquarter facility and certain medical specialists will be shared by several corporate entities. Almost all employees will seek medical care from these corporate owned facilities because the cost of alternative care will be extremely expensive, not readily available and the corporate reimbursement will be only a fraction of the cost of the alternative care.

Retirees on the other hand will seek out membership in affiliated programs joined to these corporate entities. However, instead of unlimited care, Medicare components will be billed to the government and supplemental care billed to the subscribing member. Such costs will be assessed against his maximum "nest egg" described earlier.

A new type of profession will spring up, that of financial medical treatment consultant. He will advise the elderly how to optimize his/her medical care resources in dealing with a particular condition or sickness.

Continuing care retirement communities will spring up along side the corporate medical centers. Insurance companies will organize and finance the creation of these centers for corporate clients, buying up existing facilities where possible and appropriate.

Employees not located at central headquarters or those employed by companies with scattered employee segments will participate in insurance company sponsored medical centers which spring up in urban areas. A premium will be levied by the insurance company for such locally enrolled employees.

Employees and their families away from home will visit nearby corporate facilities if stricken. A network of locations will be made known to the employee. Reciprocity arrangements will facilitate such out of town care. In addition, air ambulance services will proliferate.

Some of the questions asked earlier including the question of medical care rationing will be answered by limiting the premium. The corporate medical center will provide the care it can based on the dollars it receives.

Competition will spring up on what can be provided for what and smaller corporations will change medical center affiliations but, by and large, the corporation will control its own pocketbook limit on medical care. Management of the facilities, whose boards of directors will include officers of the corporations they serve, will ration the care through simple limitations on what is available.

As we have heard earlier, by the turn of the century, the proportion of the population over age 65 will move from 12% to 20%. At that time instead of just over one in ten of the 65-and-over group being at work, we expect that proportion will grow to one out of four or perhaps one out of three -- partly because of good health and desire by those in the vigorous segment mentioned earlier and partly because service industries will more highly value, as the result of a dearth of eligible young workers, the services of this relatively youthful and vigorous segment of the older population. From this we may conclude that roughly 5% - 7% of the work force will be over 65 at the year 2000.

This fact will present a challenge to corporate America, a challenge whose patterned solution will probably be partly preempted by age discrimination in employment (ADEA) legislation/rulings and heavily impacted by the anticipated dramatic increase in the cost of health care.

Part-timers will likely be included in the work force in greater numbers by a further expansion of the definition as to who must be included in employer plans. By way of illustration, the definition of an included worker might be expanded to embrace those whose regularly scheduled work is as low as one day and a half per week, or 600 hours per year.

Many elderly employees will work for a minimum wage just to be eligible for medical care out of the corporate medical facility. This will postpone the day when it will become necessary to join an affiliate program and pay Medicare supplements from the limited retiree "nest egg."

MR. HALPERN: I would like to go back to Niels and Tom for a few minutes for reactions to the other presentations.

MR. CHRISTIANSEN: I thought that what was said about the future of medical treatment was very much on target. One thing I do question is whether more vigorous people are going to want to work longer. This goes against the trends we have seen whereby an increasing proportion of workers are choosing early retirement. I believe it will be more a matter of working longer in order to qualify for medical insurance or otherwise earn enough to pay for medical costs.

MR. SULLIVAN: The problem with all these presentations is that they presume a certain amount of rationality in the political system. This is the first wringer I would caution everyone about. I think we all are aware of the developments in the political world to understand that rationality is not necessarily a part of the process. I think it is easy on the basis of past experience, particularly with people like Claude Pepper about, to presume that at least as long as Claude lives the elderly will pretty much get their way in Washington. I am not so sure that even thirteen years from now that it is going to be so. I am not sure that it won't be concluded prior to that time that the nation maybe cannot afford to provide the elderly with all that they want. It seems to me that there is some possibility with the growing demands for recognition and different kinds of benefits that we could see some very difficult political problems emanating from the tension between minorities and the elderly.

MR. CHRISTIANSEN: In a recent survey people were asked how willing they were to support the elderly. The survey concluded that people are going to be willing to spend the money that it takes in order to take care of their elderly parents. People see that they are going to have to pay for it one way or another and they also have some familial concern.

MR. FRIEND: I think that the point is well made that the political process may overcome rationality. It might not deal with the question of how much medical care we can afford, but rather attempt to provide the feeling that medical care in an unlimited fashion will be available to everyone. Of course, that would result in broken promises and a rationing of medical care in a different way.

MR. HALPERN: I have one question I would like to ask the panel. One of the areas we have not specifically addressed is the impact of technology on the environment. I would like to ask any of the panelists how they see future technological changes impacting either products, delivery systems or benefits design.

MR. FRIEND: Technology has, of course, in the area of medical care caused problems in the other direction. Newer more advanced technology is more expensive and creates questions of how to ration it. I anticipate significant strides in medicine far beyond those that we could even imagine right now, given research endowed grants and the massive attention being given to medicine. The attack on AIDS in my opinion will be receiving unbelievable sums of money over the next two to three years and I believe that we will indeed find the solution sometime in the early 1990s as a result of this massive delivery to the issue. When we do, this money will be diverted to other technological advances to solve other medical problems, the solutions of which will become problems themselves.

MR. DONALD A. SKOKAN: I am interested in what you think the ramifications are of Claude Pepper leaving the scene. Will that diminish the effectiveness of the elderly to voice their concerns to affect the political arena?

MR. SULLIVAN: The short answer is no. Believe me there are scores of politicians waiting for him to leave the scene so that they can take over his constituency. There will be just a blip on the radar screen, if that.

To get some idea of the political consciousness of the elderly, you may remember a recent program talking about an organization run by one of the Roosevelts, which collects literally tens of millions of dollars per year essentially to hold back any changes in the Social Security system. Right now there are no threats out there. The elderly are so concerned about their security that they are willing to give big bucks to an organization that has no clear function or purpose.

MR. CHRISTIANSEN: The other factor, obviously, is the time the retirees have to devote to political activities. I guess I feel a little different in that I don't think the question is going to be whether or not the country is going to be willing to pay for what retirees need and want but a question of how we are going to do it. We have to at least make people feel that they have adequate access to medical care.

MR. PAUL A. HEKMAN: We hear more and more in the news all the time about the fact that the world is increasingly an international community. What impact, if any does this have on how we deal with the aging problem?

PANEL DISCUSSION

MR. FRIEND: My thoughts are that dealing with problems of the aged in this country is a cultural problem and that the culture in the United States is different, for example, than the culture in Japan which is a country having a significant financial impact on the United States. I think our culture will prevail and we will have our own answers.