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Long-Term Care Insurance: What are the Opportunities?

By Catherine Ho

The standalone long-term care (LTC) market has had a rough couple of years. Sales were severely impacted by the 2009 recession. While other insurance products have rebounded with the improving economy, LTC sales have remained flat. Industry instability, mainly due to issues of profitability, has caused carriers to exit this market. Of LIMRA's Individual Long-Term Care Insurance Sales Survey, 15 participating carriers have left the market since 2008.

Sales growth trends going back further show that individual LTC sales had been on a steady decline since 2003. While the shrinking number of carriers contributed to declining sales, other factors such as invariable rate increases, unfavorable economic conditions, and the end of richer benefit products also played starring roles. Over the past decade, sales for the first half of the year have been good predictors of total sales for the year. Sales for the first half of the year show a steep decline. Even ignoring past experiences, it is hard to foresee a massive increase for the second half of the year to offset the negative twenty percent sales growth thus far. So the question is *will LTC survive?*

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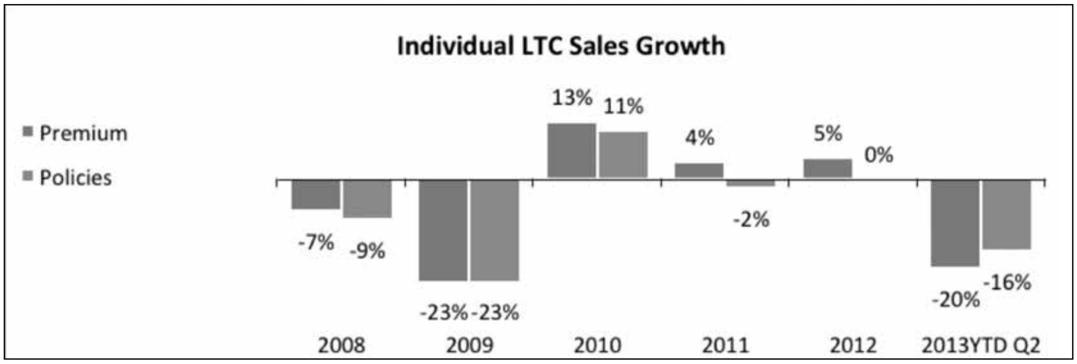

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THE NEED FOR LONG-TERM CARE

With 10,000 Baby Boomers turning 65 every day and their increasing longevity, the target market for LTC will only increase over the next decade. Government inaction to this rising problem and continued increase in LTC expenses will fuel demand. Even with fewer carriers, the need for LTC insurance will perpetuate the survival of standalone LTC.

From a consumer standpoint, the problem is cost. Many consumers underestimate the cost of LTC insurance and underestimate the cost of LTC expenses. In LIMRA's *LTCI: An Industry Subdued* (2012), 41 percent of respondents believed standalone LTC is becoming a niche product for affluent Americans. In addition, large organizations such as associations are finding it difficult to negotiate a lower cost product that provides the coverage members want. For carriers, previous attempts at offering scaled down products for the middle markets have been poorly received by producers and consumers.

We all know that needs and attitudes change over time. Just like we accept the inevitability of paying more for gas at the pump, consumers will eventually accept higher LTC premiums. At the same time, carriers must look into less expensive products, too. The question then becomes, how do you reach the right consumers with the right product?

THE DISTRIBUTION QUESTION

LTC has had its share of distribution challenges. While those who specialize in LTC feel equipped to sell there are fewer producers overall who sell standalone LTC due to the complexity of the product and licensing requirements. This means carriers need to invest in their producers, but how?

First, they need to build their distribution channel. For the first half of 2013, the career channel sold the greater portion of VUL, roughly 43 percent of new premium. And not surprisingly, due to the licensing requirements needed to sell VUL, more carriers sell through the career channel more than any other distribution channel. However, the top companies are more focused on the independent channel and sell more through it.

Next, they need to expand worksite sales. While some believe "employers won't provide this as a benefit for their employees due to cost," (LIMRA's *LTCI: An Industry Subdued*) a worksite model could prove profitable in the wake of the Affordable Care Act (ACA), particularly with employers that have switched to a defined contribution health plan. The problem with that: carriers have shied away from building the needed infrastructure to sell LTC in the worksite because of cost.

Another reason to build worksite has to do with the comeback of the employer-sponsored market. With the recession behind us and the economy picking up, companies will have the means to fund these benefits. As a result, companies can begin to offer richer benefits, such as LTC coverage, to retain key employees.

DIFFERENT PRODUCTS, SIMILAR PATTERNS

In the 1980's, individual disability (IDI) sales climbed. Economic conditions were just right and the pricing was competitive. Carriers were offering products with rich benefits and taking on larger amounts of risk while still making a good profit. By the 1990's, conditions were no longer favorable for IDI carriers. Interest rates were declining, profitability was dropping, and carriers were having bad experiences. Some carriers chose to exit the market. Those that remained pulled back on benefits, cut out unprofitable markets, and tightened up on underwriting. The recovery has been long, but the IDI market has normalized over the past couple of years. Now, sales grow at a moderate pace with some fluctuations due to economic conditions.

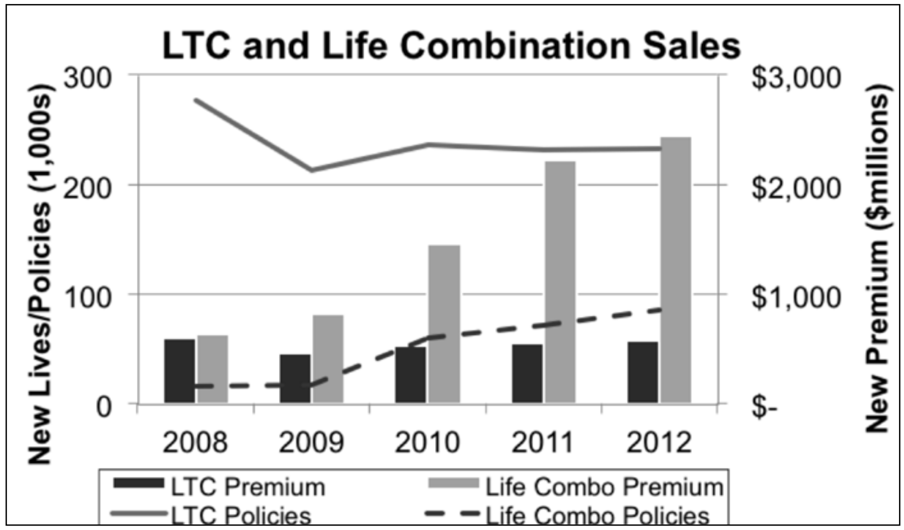
Another example is variable universal life (VUL) products. These are permanent life insurance products that provide death benefit protection with a savings component called a "cash value." Unlike other permanent life insurance products, the policyholder makes the investment decisions for the cash value and therefore takes on full investment risk.

Sales of VUL peaked in 2000, built by perfect market conditions. It was a bull market combined with falling interest rates, making VUL product much more attractive compared to other life insurance products. Sales quickly declined in 2001 with the burst of the dot-com bubble and within three years sales were half of what they were at the peak. As with IDI and standalone LTC, carriers exited the market during that time. With fewer carriers, sales rebounded only slightly in 2007, when individual life sales peaked. Sales growth took another severe beating with the 2009 recession. Since the recession, total new premium has leveled off to roughly a quarter of the peak sales in 2000.

Is this the same trend for the LTC market? The standalone LTC market has gone through similar experiences as IDI and VUL: declining sales, carriers exiting the market, and decline in consumer demand. Much like what happened with IDI, LTC carriers have just started on the road to normalization with their recent scale back on benefits and pulling out of less profitable markets. However, the consumer view of LTC may be more comparable to the VUL market. After the dot-com bubble, pessimistic consumer views of VUL revived with each market downturn. Similarly for LTC, negative views of the industry and product surfaced after each rate increase announcement. It may be several more years before we see sales get to a more normal rate.

COMBINATION PRODUCTS

Another parallel between LTC and VUL is the availability of substitute products. Unlike IDI, where there is no close substitute, a consumer looking for coverage has alternatives when it comes to LTC and VUL. For the most part the substitutes provide similar, but not exactly the same benefits to consumers. In the case of VUL, indexed universal life (IUL) products have gained significant market share in the past five years with a portion of the market share coming from potential VUL buyers. While it's not an investment product, IUL policies allow the policyholder to share in stock market gains while the insurer takes the brunt of the investment risk. IUL products have a cap and floor on returns. Most floors are zero or higher, protecting policyholders from the loss of their principal when the market crashes but at the cost of reduced gains when the market soars.



The substitutes for standalone LTC are combination products. Both life and annuity combination products have been around for decades. The annuity combination market has grown steadily over the past few years, but very few carriers have entered and stayed in this market.

Life combination products have gained traction with double digit growth over the last four years. Part of the growth can be attributed to new carriers entering the market. Over the past five years, at least seven carriers have entered this market and a few more are expected in the coming months. The most prevalent products are the acceleration riders, where the death benefit is accelerated for LTC or chronic care needs. While these products can provide LTC benefits, the majority are still sold for life insurance needs.

For sales focused on the LTC benefits of life combination products, the main sales pitch has been the "use it or lose it" argument against standalone LTC.

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Table 1: Average premium and benefit for LTC and Life Combination products.			
	Average Annualized Premium	Average Monthly Benefit/Life Death Benefit	Total Max LTC Benefit
Standalone LTC	$2,400	$5,000	$420,000*
Life Combo – Extension of Benefits	$6,950**	$109,000	$327,000**
Life Combo – Acceleration	$6,600	$326,000	$326,000

*Average LTC Benefit based on $5,000 monthly benefit for 7 years.

**Annualized premium is 10% of single premium. Max LTC benefit assumed to be 3 times death benefit.

LIMRA's past survey results have shown that the concept of life combination products resonate more with consumers. But once costs are figured in, it's a different story.

Table 1 compares the average annualized premium and benefit amounts for standalone LTC and life combination products based on LIMRA's 2011 ILTCI Sales Survey & Supplement and 2012 Life Combination Survey. Standalone LTC, by far, provides the cheapest LTC coverage.

The cost difference brings to mind the slogan "buy term and invest the difference" from popular financial advisors on TV. Like term insurance, standalone LTC gives the buyer coverage. With term insurance, however, the majority of people who buy it do not expect to die. The difference with standalone LTC buyers is that a high number of them do expect to use the LTC benefits. For these consumers, a scaled down standalone LTC product may prove successful when paired with a smaller life combination product.

CONCLUSION

Growth in standalone LTC is declining, but the overall LTC market is still growing. The LTC market is in reality many different markets offering targeted products based on consumers' needs. Even though sales of life combination products have soared in recent years, most people are still purchasing standalone LTC. Consumers looking for the most cost effective LTC coverage are still better off with standalone LTC.

In order to be successful, carriers need to invest in their producers and their distribution channels. The education of producers should center on LTC solutions rather than one specific product. In some cases, due to age or health reasons, a buyer may not qualify for standalone LTC, leaving life combination products as their only option. While life combination products may have been initially designed for a more affluent market, many carriers offer the acceleration riders on smaller, lower premium policies that are more affordable to the middle class. ■