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EQUITY FORMS OF SAVINGS

A. What are the implications for life insurance companies of the increasing interest in equity forms of savings as evidenced by the growth of mutual funds, employer sponsored employee thrift plans, and the establishment of instalment purchase plans for common stocks?

MR. R. M. DUNCAN presented statistics covering the years 1948–1953 which showed that the largest share of the increase in liquid savings by individuals in the United States was devoted to reserves of private insurance companies and pension funds, and that the amount of life insurance in force per family as a percentage of disposable personal income had risen from about 110% in 1948 to 120% in 1953. The net assets of mutual fund investment companies rose approximately 167% from about $1\frac{1}{2}$ billion dollars at the end of 1948 to about 4 billions at the end of 1953, whereas the assets of U.S. life insurance companies grew about 60% from $55\frac{1}{2}$ billions to $78\frac{1}{2}$ billions over the same period.

Mr. Duncan felt that all indications pointed to life insurance and fixed dollar guarantees as the foundation for the average family's financial security plan. At the same time there is a growing demand to provide a more satisfactory relationship between the purchasing power of premiums and the consequent benefits under long-term insurance and pension programs. He felt that the higher yields available in equity investments were a contributing factor in the conclusion reached by more and more people that a combination of equities with insurance and fixed dollar obligations offers one of the most hopeful methods currently available, imperfect as it may turn out to be.

He reported that about one-fourth of the deferred annuity policyholders of Teachers Insurance and Annuity Association had already started to participate in the College Retirement Equities Fund during the first eighteen months of operation. Nearly all participants in CREF had elected to have the maximum percentage (50%) of their TIAA-CREF premiums paid into CREF.

MR. M. A. LINTON thought the present interest in common stocks was somewhat reminiscent of the twenties but that nobody knows whether or not there will be a corresponding aftermath. He had no doubt that the popularity of common stocks can be justified on the basis that the values of our basic industries are going to be preserved, although substantial fluctuations in market values are likely. He felt that life insurance companies should stress the availability of fixed dollar values in good times or bad, a feature found in life insurance contracts but not in common stocks or mutual funds. For the individual, the rate of return in such an investment program is apt to be misleading in that if he were forced to liquidate his holdings during a time of depressed prices the results of the whole program might be very disappointing. In the same connection, Mr. Linton recalled that in the 1930's investment trusts had proved to be unsatisfactory as bases for loans.

He was uncertain as to whether a life insurance company should get into the field of unit-annuities based on common stocks. He believed a good deal of business could be sold, but that long-range consequences and policyholder reactions would be doubtful if adverse experience developed. However, he wished that some way could be found to invest life insurance funds to a larger extent in common stocks and he would not object to a common stock investment of up to about 20% of assets, if we could find a satisfactory solution to the year-end valuation problem. This increased investment in stocks would introduce the variable element in the net cost of insurance, but not in the guaranteed values.

Mr. Linton noted the present emphasis on term insurance as a supplement to savings in other fields but was not sure that it was wise for the life insurance companies to tie themselves in with mutual funds in such arrangements. He wondered whether this would weaken the appeal of the guaranteed values of the life insurance contract, and he also touched on the agency problem presented by the size of commissions on term insurance.

MR. H. M. SARASON explored several approaches to meeting the problem of a changing purchasing power. He mentioned as possible experiments differing from present life insurance contract provisions the use of equity investments and varying benefits with respect to paid-up portions of the ordinary life policy, dividends, and portions of loading. All of these would have present legal or practical objections, but he felt that in any event the crux of the matter was the uncertainty of stock market prices.

MR. H. R. LAWSON said he considered the College Retirement Equities Fund as one of the most significant developments in the life insurance business in recent years, but that since business and economic conditions have been quite good in the last few years it was yet to be seen how the idea will work out under adverse conditions. He presented several reasons why life insurance companies need not be concerned about the current public interest in common stocks.

First, life insurance is not primarily an investment and the protection benefits outweigh the possible variations in purchasing power, particularly under the lower premium plans of insurance comprising the large bulk of business in force. He pointed out that in any event a well balanced program should have fixed dollar guarantees and suggested that the savings part of life insurance be considered as fulfilling this need. In addition, many legal and practical difficulties stand in the way of substantial investment in equities by life insurance companies. He referred to the probability of decreased premiums in poor times and the consequent inability to invest at low stock prices. Moreover, if benefits were to be paid in units, the usual solvency test of good management would be absent.

Even if the above difficulties were surmounted, he felt that the companies should not get into the position of appearing to offer greater benefits than might subsequently be realized and thus risk the serious disappointment of their policyholders. Finally, it was his opinion that the current interest in equity forms of savings was transitory, reminding him of the situation in 1929, and that no one can be sure whether or not common stocks are worth investing in at their present level.

MR. E. G. WENDT, JR. thought the increasing interest in equities might accelerate the growing popularity of term insurance and that the life insurance companies should consider the effects of this on their company objectives.