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Interest in Preneed Accelerating

by Kevin Gough

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Preneed insurance — the sale of a life insurance policy or annuity contract to cover the cost, typically guaranteed, of a prearranged funeral — is a growing niche of the life insurance industry. Although prefunded funerals have been available for some time through trust fund mechanisms set up by funeral homes, preneed insurance has distinct tax and other advantages, such as the flexibility and greater guarantees of payment it offers. This edge — plus the fact that only a small percentage of the growing age-65-and-above population currently has preneed insurance — suggests that the market potential for this product is very high.

Today's market

Preneed insurance exhibited double-digit growth during the mid-1990s. Sales (new premium written) increased at an annualized rate of 12.6% over the three-year period 1994-96. During the same period, preneed insurance in force increased at a 29.3% annual rate.

A handful of insurers controls the \$1.1 billion-plus premium market, while the balance is fragmented among many very small local or regional competitors that are regarded as relatively unsophisticated marginal players. Seven preneed specialists represented approximately 85% of the preneed market in 1996. These companies — Forethought Life, United Family Life, Homesteaders Life, Pierce National Life, American Memorial Life, Mission Life and Security Industrial Insurance — continue to dominate, albeit with some ownership changes. (Most significantly, Fortis Group, owner of the number two company United Family Life, acquired Pierce National Life in 1998, doubling the Fortis book of preneed business.)

Preneed's future

Preneed offers a number of favorable financial characteristics. Cash flows are stable, due to reliance on the noncyclical and growing death care industry. Mortality experience is relatively stable, due to the small face size of the policies, while policy persistency is high. Most important, a natural sales outlet exists through funeral homes, where commodity pricing does not apply and customers generally do not comparison shop.

The funeral services industry remains highly fragmented, despite an accelerating trend toward consolidation in urban areas initiated by funeral home consolidators. A focus on profitability among the consolidators has helped to fuel the growth in preneed arrangements, which in turn has created incentives for some of the consolidators to enter the preneed insurance business via acquisition.

Sales success will require access to a sustainable distribution channel that is not overly vulnerable to competitive pressure from the larger funeral home consolidators. Funeral home distribution will remain a viable channel, because many of these businesses will remain independent, especially in non-urban areas. Entrance of some of the leading funeral home consolidators into the preneed insurance industry will drive demand for additional "independent" preneed insurers to service their needs. Also, exclusive arrangements between carriers and funeral homes appear to be the exception within the industry. Insurers that can establish effective distribution agreements with these independent homes — especially on a multi-regional or national scale — will profit and flourish. The Midwest and South are particularly attractive target areas, because rural funeral homes are much more prevalent.

Players changing

The configuration of preneed players is changing. Consolidation, increasing participation of the funeral home consolidators, and the exit of small

"mom and pop" insurers will reshape the industry significantly in the next decade.

Consolidation among the dominant players, along with their acquisition of small, local insurers, will leave just a few large national companies — Forethought and others. In total, this dominant segment will control a reduced market share, while that of the surviving companies likely will increase.

There will be a declining number of small, local preneed insurers as "mom and pop" businesses sell out and less involvement of multiline companies as they shed businesses outside their core strategic lines. In many cases, reinsurers and administrators will acquire these profitable existing books of business to facilitate the owners exiting the industry.

Finally, funeral home consolidators will be increasingly active in offering preneed, either through directly owned subsidiaries or joint ventures, which will help them integrate prefunding with their funeral home ownership. As such, they have the best future preneed business prospects because of their ability to vertically integrate all aspects of the death care business. They will be extremely formidable competitors, especially in urban areas.

The future also is bright for Forethought Life and the one or two other dominant specialist carriers that will service the remaining independent funeral homes, especially in non-urban areas. On the other hand, the funeral industry will continue to support alternatives to Forethought Life in order to prevent the company from *de facto* monopoly status.

Finally, reinsurers, TPAs and venture capitalists will profit — though to a lesser degree — as marginal players exit the business and consolidators look for profitable acquisition targets.

Conning's strategic study, *Preneed Insurance — A Business to Die For?*, analyzes this growing niche of the life insurance industry.

Preneed Funeral Insurance Survey

(\$ in millions)

	1993	1996	Annualized Growth Rate 1994-96
Sales (New Premium Written)	\$612.3	\$874.2	12.6%
Insurance In Force	\$5,118.7	\$11,066.4	29.3%
Number of Policies In Force	2,939,285	2,981,032	0.5%
Number of Policies Sold	308,629	430,968	11.8%

Source: Life Insurers Conference

1996 Preneed Market

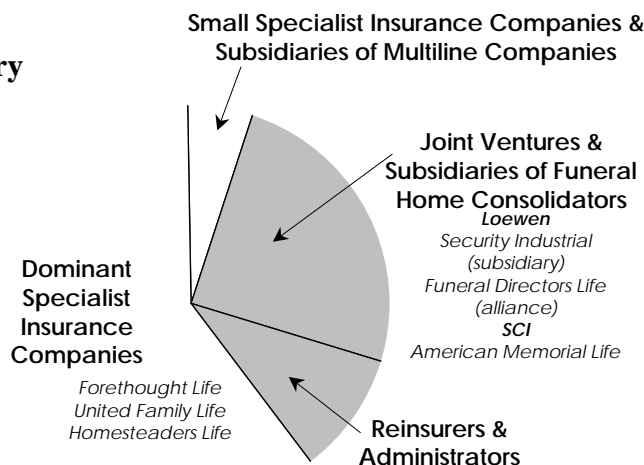
(\$ in thousands)

	Preneed Sales – New Premiums Written	Net Premium Written	Insurance In Force	Admitted Assets
Forethought Life	\$411,258	\$479,682	\$2,450,075	\$1,686,454
United Family Life	100,887	146,245	1,439,606	734,623
Homesteaders Life	94,362	111,990	887,576	293,910
Pierce National	47,589	104,939	1,583,309	769,642
American Memorial Life	67,590	97,258	665,738	411,560
Mission Life	19,881	36,465	335,676	213,730
Security Industrial	6,835	31,492	1,027,902	212,720
Seven Dominant Carriers	\$748,402	\$1,008,071	\$8,389,882	\$4,322,639
Total Preneed Market*	\$874,152	\$1,135,566	\$11,066,382	\$5,394,223
<i>Seven Dominant Carriers % of Total</i>	<i>85.6%</i>	<i>88.8%</i>	<i>75.8%</i>	<i>80.1%</i>

Note: * Represented by results of 1996 Life Insurers Conference survey of 23 preneed carriers (including top 7)

Source: OneSource, Life Insurers Conference, Conning & Company

The Future of Preneed Industry



Source: Conning & Company
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Reduced Market Share
 Expanded Market Share