Life Settlement Marketplace: After the Storm

By Steve Shorrock, ChFC, CLTC, FLMI

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The past 12 months have been, to say the least, dramatic. Global financial markets came perilously close to a total meltdown and left the world mired in what appears to be the worst global recession since the Great Depression. The secondary market for life insurance policies—life settlements—has hardly escaped unscathed. But given the unique characteristics of this asset class, there is good reason to believe the market will not only recover, but come back stronger than ever.

Although 2008 was a very volatile year for financial markets in general, the life settlement market continued to grow robustly through the first three quarters. Investors liked the "uncorrelated" nature of the asset, as well as the perception of limited credit risk and relatively high returns over long durations. Accordingly, even as equity markets peaked and declined dramatically and bond prices turned choppy, money continued to flow for the purchase of life insurance policies.

After September 2008, however, the combination of "frozen" capital markets and the nearly simultaneous announcement of new mortality tables by the major Life Expectancy (LE) providers created a great deal of turmoil in the life settlement marketplace. Longer LEs and a limited number of potential buyers had a tremendous impact on the market. The number of successful transactions completed during the first half of 2009 was substantially reduced.

But now there are a number of encouraging signs.The threat of a global meltdown has largely receded and financial markets in general have stabilized. While credit is still very tight, money is moving once again and the appetite for risk on the part of money managers is gradually returning. Investors, after all, are not willing to pay substantial fees for professional management only to have the funds sit in cash or cash equivalents. As a result, the market for life settlements is much more active, although buying parameters are tighter than in the past.

Generally, the more desirable policies will fit the following profile:

- Insureds 75 or older
- Face amounts $500,000 to $5 million
- LEs < 140 months
- Two LEs less than 10% apart
- Universal life (non-guaranteed) or SUL with one insured deceased
- Term which is convertible to current assumption UL
- Premiums to maturity less than 4% of face amount
- Account values sufficient to carry the policy 3 -4 years without additional premiums.

For policies which fit the "buy-box", there are multiple buyers and competition is resulting in much better net offers to the policy owner. As an additional bonus, due to the amount of "slack" in the market, transactions are progressing much more rapidly than they might have in the past. As additional capital is committed to the market over the next few months, there are a number of indications that the buying parameters will be relaxed as well, and a greater appetite for both longer LEs and larger face amounts will emerge.

The appetite for financed policies (even full recourse) is currently very limited. Variable policies can also be difficult; the FINRA requirement for Broker/Dealer involvement limits the number of buyers and it can be very difficult for producers to be fairly compensated, particularly when there are multiple parties involved

Although the market continues to improve, marginal cases (younger insureds, longer LEs, higher premiums) are still difficult to place at this point. For policy owners who can afford to pay additional premiums, waiting for further improvement in the market might prove to be a better strategy for the long run. From this perspective, all potential settlements need to be carefully evaluated. Sending out a file which languishes in the marketplace can kill the potential value for the future. FA

Steve Shorrock is President of LifeVentures Corp, which designs new life insurance products and develops marketing concepts for agents and Director of Veris Settlement Partners, a life settlement firm that brokers seniors' unwanted or unneeded life insurance policies. You can reach him at his Northport, Long Island office at 631-239-6655 or steve@lifeventurescorp.com