# The Life Settlement Business After The Storm

BY RUSSEL DORSETT

THE PAST 12 MONTHS HAVE BEEN, TO SAY THE LEAST, DRAMATIC. Global financial markets came perilously close to a total meltdown, and in the aftermath the world is mired in a deep recession. The secondary market for life insurance policies—life settlements—did not escape unscathed. Given the unique characteristics of the asset class, there is no good reason to believe the market will not only recover, but will come back stronger than ever.

Although 2008 was a very volatile period for financial markets in general, the life settlement market continued to grow robustly through the first three quarters of the year. Toward the end of the third quarter, two significant events (one external and the other internal) had a dramatic impact on market momentum. Externally, AIG "bailed-out" through a de facto nationalization, and Lehman Brothers faltered and was allowed to fail. The financial soundness of even the largest global financial institutions suddenly seemed questionable.

During the same period, 21st Services announced the introduction of a revised mortality table, ostensibly triggered by the introduction of the 2008 VBT table. The new mortality table was advertised as resulting in "slightly" longer life expectancies at some ages, and 21st offered to update "old basis" LEs at a reduced fee .

In practice, all previously issued 21st LEs were invalidated, and the other major LE providers quickly followed suit. The most immediate impact was on files in the closing process. As new basis LEs were received, "slightly" longer turned out to be 20%-30% longer in the many cases. While most funding sources honored offers already extended and accepted, many chose to "re-price" on the new basis, resulting in offers being withdrawn or substantially reduced.

While most of the investment capital already committed to the settlement market was not withdrawn, very few money managers were willing to commit funds to any new investments other than cash. As previously committed pools of funds were exhausted during the early part of the 4th quarter, the market for settlements ground virtually to a halt—a condition that persisted through the first half of 2009.

**The state of the market**

As we move into the 4th quarter of 2009, 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.

During the 3rd quarter we began to see more capital committed to the space, and all indications are that additional funding will be in place as the year progresses. As a result, the market for life settlements is much more active, although buying parameters are tighter. Generally the more desirable policies will fit the profile shown in the chart.

For policies that 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, the buying parameters will be relaxed as well, and a greater appetite for both longer LEs and larger face amounts will likely 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. NU

**A GOOD FIT**

**PROFILE OF MOST DESIRABLE POLICIES**

- **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 insure 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.

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