



# What hinders ILS manager from investing in life settlements?

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# Motivation and contribution of the study

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## Motivation

- Highly specialized group of insurance linked securities (ILS) managers
- ILS manager did hardly consider a life settlement investment so far
- Making the life settlement market attractive for a wider range of investors

## Contribution

- Analysis based on interviews with 10 ILS managers and 6 life settlement providers
- Survey reveals hurdles for an investment in life settlements
- Suggestions for improvements to make the market more accessible for investors

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Part I

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# Survey among ILS managers

# Methodology

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## Target group

ILS fund managers which invest in a wide range of ILS products

## Survey

- Interviews and standardized questionnaire
- Open questions as well as multiple choice questions (participants were asked to assess importance of certain topics between 1 and 6)
  - 1 = very low importance
  - 6 = very high importance

# ILS market size

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- 10 largest ILS funds have about 42.5 Billion USD AUM (source: insurancelinked.com)

Manager	Head Office	Approximate AUM (USD bn)	Inception
Nephila	Hamilton, Bermuda	9.5	1998
CSAM	Zurich, Switzerland	6.5	2003
LGT	Pfaffikon, Switzerland	5.0	2005
Fermat	Westport, Connecticut	4.5	2001
Securis	London, UK	3.5	2005
Stone Ridge	New York, New York	3.5	2012
CATCo	Hamilton, Bermuda	3.0	2011
Aeolus	Hamilton, Bermuda	2.5	2006
Elementum	Chicago, Illinois	2.5	2009
Leadenhall	London, UK	2.0	2008

# Participants

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- 10 ILS managers (10 questionnaires plus 7 interviews)
- Participants manage insurance linked securities worth about 25 Billion USD, mostly invested in collateralized reinsurance
- Good level of knowledge regarding life settlements (half of them invested already once in LS)

<b>Investors' base structure (in % of total assets)</b>	<b>pension funds</b>	<b>family offices</b>	<b>private clients</b>	<b>insurances</b>	<b>banks</b>	<b>other</b>
	61%	8%	5%	2%	9%	16%
<b>Percentage of 'life' related investments</b>	<b>5%</b>					
How much of that is invested in:	embedded value	extreme mortality	longevity risk	XXX	other	
	12%	71%	3%	3%	12%	
<b>Expected loss of their investment funds</b>	<b>0 - 0.5%</b>	<b>0.5 - 2%</b>	<b>2 - 5%</b>	<b>5 - 10%</b>	<b>10 - 15%</b>	<b>&gt; 15%</b>
	0%	48%	38%	13%	1%	0%

# Preferred structures and target clients

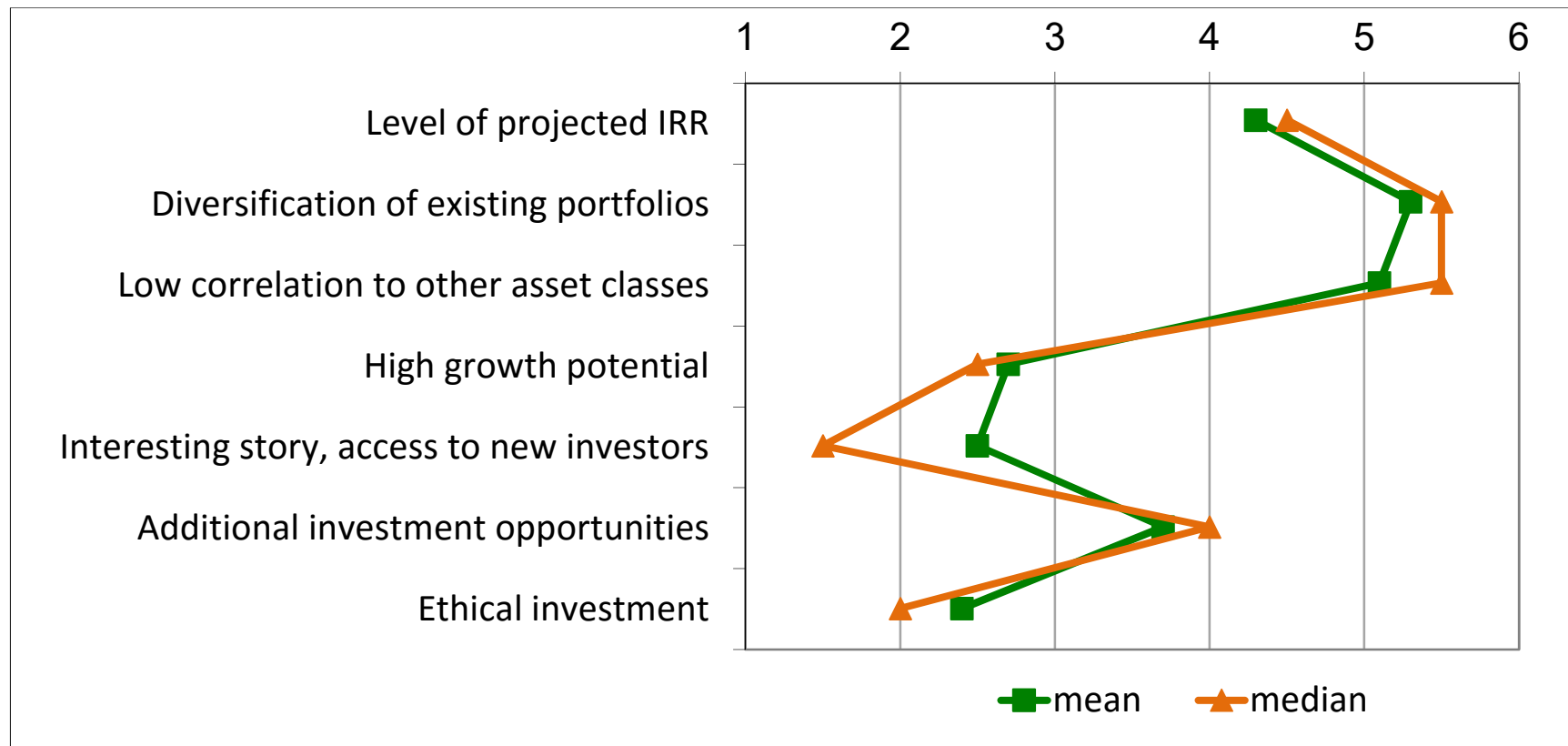
Preferred structures in order to invest in life settlements (in the long run)			
Own or third-party product?	own product	third-party	
	8	3	
Fund, index investing or structured product?	fund	index-product	structured product
	7	1	2
If a fund is chosen, open-end or closed-end fund?	open-end fund	closed-end fund	
	3	4	
Adding LS to an existing product or creating a new product?	adding to an existing product	new product just with LS	new product mixed with other ILS
	0	6	2

- No financial engineering, rather conservative structure
- Target clients → Family offices  
→ Pension funds are obviously not interested
- But manager doubt whether they can raise enough money (ramp up period)



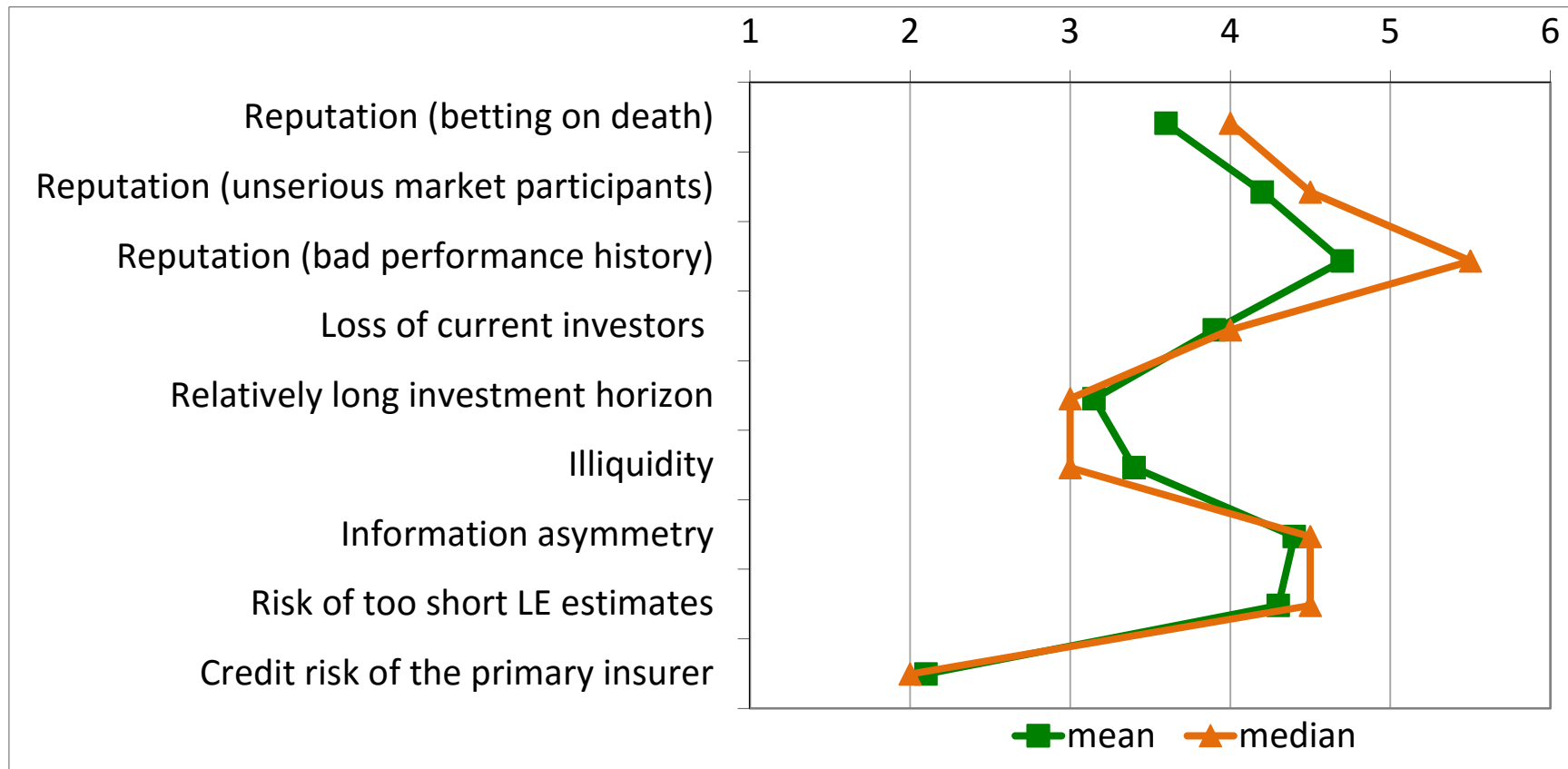
# Benefits of life settlements

- Currently life settlements have just a few benefits for ILS managers...



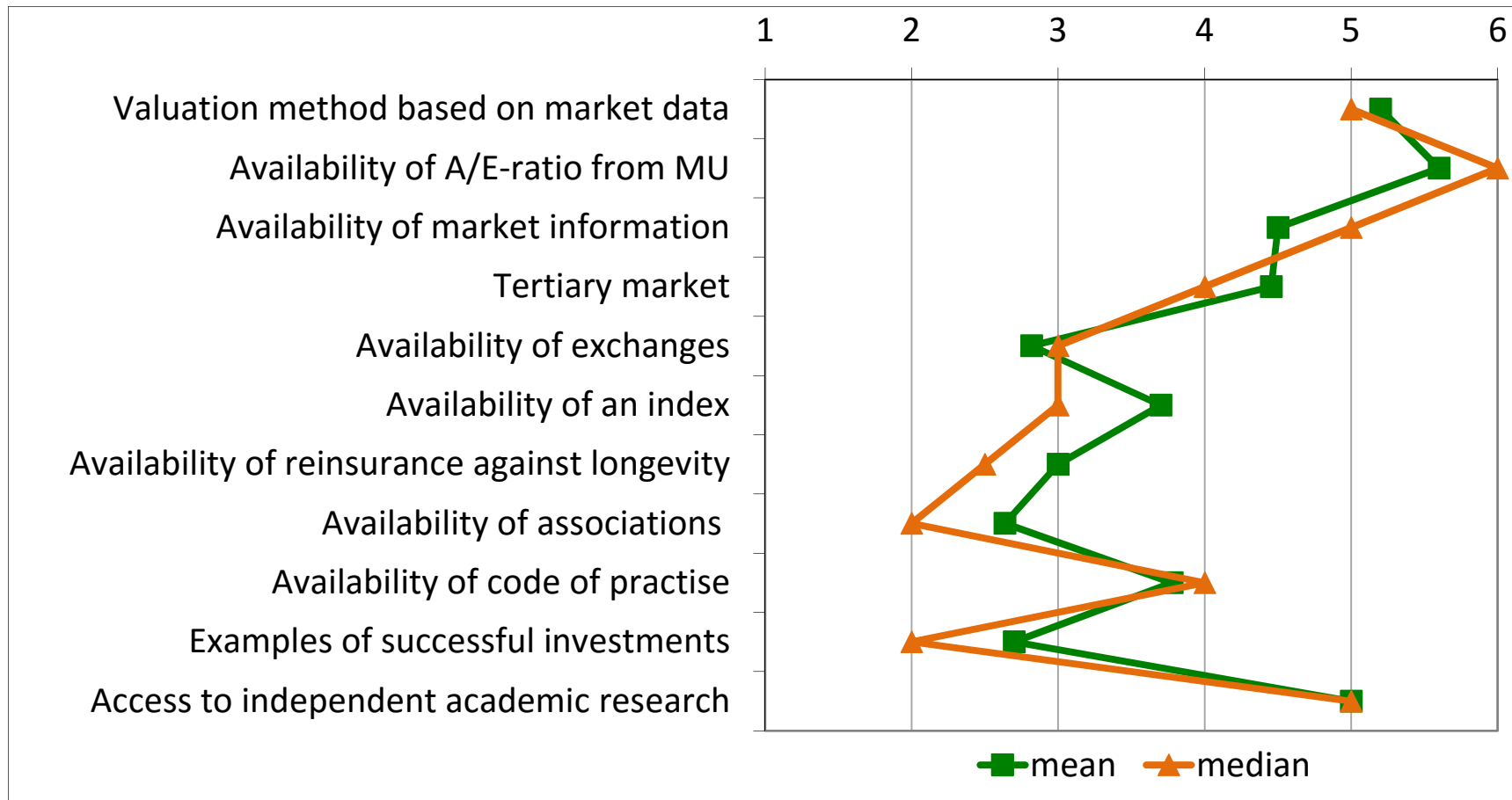
# Risks / drawbacks of life settlements

- ... but many hurdles which hinder them to invest



# Preconditions for an investment

- Which preconditions need to be met until life settlements could become eligible?



# Need for improvement

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## **Transparency**

- Accuracy of medical underwriting
- Dubious market participants / black sheep
- Reputation (due to historical performance and black sheep)
- Non-alignment of interests (wrong incentives)
- Transparent pricing (market data available)

## **Liquidity**

- An established tertiary market is desirable but more important is price certainty

## **Standardization**

- Increased self regulation or regulation through an authority (e.g. auditor, association)

## **Education**

- Independent academic research
- Good news (e.g. by opinion leaders)



Part II

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# Survey among life settlement providers

# Methodology

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## Target group

- Life settlement providers

## Survey

- Email with a standardized questionnaire
- Open questions as well as multiple choice questions (participants were asked to assess importance of certain topics between 1 and 6)

## Participants

- 15 providers were asked to participate
- 6 providers returned the questionnaire

# Accuracy of medical underwriting

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<b>A/E-Ratio of medical underwriters is of imperial importance and needs to be available.</b>	<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>	<b>5</b>	<b>6</b>
Do you agree?	-	-	-	-	-	6

## **Who should ask for A/E-Ratios from medical underwriter?**

- Medical underwriter should publish A/E-ratio
- Investor / asset manager

## **Is there a reasonable alternative to improve the availability of A/E-Ratio?**

- Industry trade association or independent third-party should look at each underwriter's data and publish accuracy

# Dubious market participants / black sheep

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The life settlement market contains black sheep which destroy the reputation and the trust into the asset class	1	2	3	4	5	6
Do you agree?	-	-	1	1	-	4

## Which part of the value chain is most vulnerable to contain black sheep?

- Broker
- Provider
- Investor / asset manager

## How could black sheep be avoided going forward?

- Investor drive this process with their capital → due diligence on the provider and the provider need to do due diligence on the broker
- Media coverage as well as education of the investors and policyholders



# Reputation

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<b>The reputation of life settlements as an asset class is bad (among asset manager and investors)</b>	<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>	<b>5</b>	<b>6</b>
Do you agree?	-	-	-	2	1	3

## **What damages the reputation of life settlements most?**

- Bad performance history
- Black sheep
- Intransparency

## **How could the reputation of life settlements be improved?**

- Associations and/or independent third-parties should make information available
- Associations and AA Partners should not include bad actors

# Non-alignment of interests

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<b>The interest of the sell side is not aligned with the interest of the investors which is a hurdle for investing.</b>	<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>	<b>5</b>	<b>6</b>
Do you agree?	1	1	-	-	1	3

## Which part of the value chain has the largest potential to take advantage from non-alignment of interests?

- Manly brokers
- Partly insured / policy seller and medical underwriters

## How could the non-alignment of interests be improved?

- Few recommendations (several providers think it is not a serious problem or the situation just has to be accepted)
- Investors and asset managers need to do due diligence on their business partner



Part III

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# Conclusion

# How can the market be made more accessible?

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- Pricing**
  - Accuracy of A/E-Ratios need to be published (preferable through MU)
  - Market data need to be available to make transparent pricing possible and reporting of used data needs to be standardized (best practice)
- Black sheep**
  - Binding practices across industry participants (through regulator, auditor or association) and improved self regulation
  - Educating policyholders as well as investors
  - Providers need to strengthen due diligence on brokers or fee structures need to be introduced to align interest of brokers/sellers and investors
- Reputation**
  - Independent third-party research
  - Good news / reports from opinion leaders (what has changed/is changing)



Thank you for your attention