



Overview of Fraternal Insurance Company Performance

An extract from Conning's "Individual Life-Annuity Growth and Profit Leaders – 2019"

About the Author



Terence Martin, FSA, MAAA, is a Director and leads the research team responsible for the life and health insurance industry. Prior to joining Conning in 2004, he was director of actuarial reserving for Oxford Health Plans and previously was at Arthur Andersen, providing actuarial consulting regarding life insurance, health insurance and managed care, continuing care retirement communities, GAAP and statutory financial reporting, demutualization, and expert witness testimony. Mr. Martin earned BS and MS degrees in actuarial science from the University of Michigan.

Companies Included in this Analysis

Definitions of Company Groups

Small Individual Life- Annuity Specialists

Assets < \$2b or Surplus < \$200m

Ranked > 126th

Individual Life + Individual Annuity
> 50% of premium

Fraternals

Excluded:

Thrivent

Knights of
Columbus

Modern Woodmen

“Leading Small”

5 Companies

“Remaining Small”

41 Companies

“Fraternals”

37 Companies

Criteria to be considered “Leading”

Measurement	Performance Hurdles from 2009 to 2018
Operating Metrics (Meet all 3)	
Operating Margin for:	
Individual Life or	Average > 5.0%
Individual Annuities or	
Both Combined	
Return on Average Surplus	Average > 5.0%
Direct Premium Growth	> 5.0% CAGR
Sales Metrics (Meet at least 1)	
Annualized Individual Life Sales	> 5.0% CAGR
Individual Annuity Premiums	> 5.0% CAGR

Of the 37 Fraternal included in this analysis, three met the criteria to be considered “Leading”:

- GBU Financial Life
- Greek Catholic Union of the USA
- Portuguese Fraternal Society of America

Key Findings Regarding Fraternal*

Operating Margins

Individual life operating margins for Fraternal have generally lagged the Leading Small Companies and Remaining Small Company groups

Individual annuity operating margins for Leading Small has increased to compared to Remaining Small companies, with the Fraternal having results between the two groups.

Direct Premium Growth

Fraternal had only a 2.5% CAGR in direct premium growth over 2009-2018, compared to the Leading Small companies and Remaining Small companies with CAGRs of 11.7% and 4.4%, respectively.

Asset Growth

Leading Small companies have seen average net admitted assets increase at a 13.2% CAGR from 2009 to 2018, compared to 5.4% for Remaining Small companies, and only 4.7% for Fraternal.

Asset Mix

The Fraternal had more invested in mortgages and real estate than the Leading Small and Remaining Small companies. The Fraternal had significantly less invested in cash.

The Fraternal average bond maturity of 9.92 years is shorter than the Remaining Small and Leading Small averages of 10.15 and 14.50, respectively.

Investment Return

The Fraternal had lower net investment return, but also paid slightly less in investment expenses.

Capital Leverage

Fraternal have been consistently more highly leveraged than the Remaining Small companies, but less leveraged than the Leading Small companies. Capital leverage for the Fraternal has decreased 20% from 2011 to 2018 (10.5x to 8.4x).

* Throughout this analysis, Thrivent, Knights of Columbus, and Modern Woodmen of America were excluded.

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Three Fraternal Performed Significantly Better than the Others

Leading Fraternal

\$ in millions

Leading Small Companies	2018 Total Premium	2018 Ending Surplus + AVR	Combined Life & Annuity Operating Margin: 2009-2018	Average ROS: 2009-2018	Total Direct Premium CAGR 2009-2018
GBU Financial Life	433	223	8.7%	19.6%	15.3%
Greek Catholic Union of the USA	251	174	10.2%	23.0%	13.0%
Portuguese Fraternal Society of America	8	13	18.7%	7.7%	15.0%

Significant Performance Gap between the three Leading Fraternal and the 34 Remaining Fraternal

The performance hurdles for the Leading criteria is 5% for all the measures. The three fraternal listed above met the 5% hurdle by significant amounts

The performance hurdle would have to be lowered to 3.1% for the next fraternal to meet the criteria, a 4.5 percentage point difference between Portuguese Fraternal and the fraternal with the next best performance.

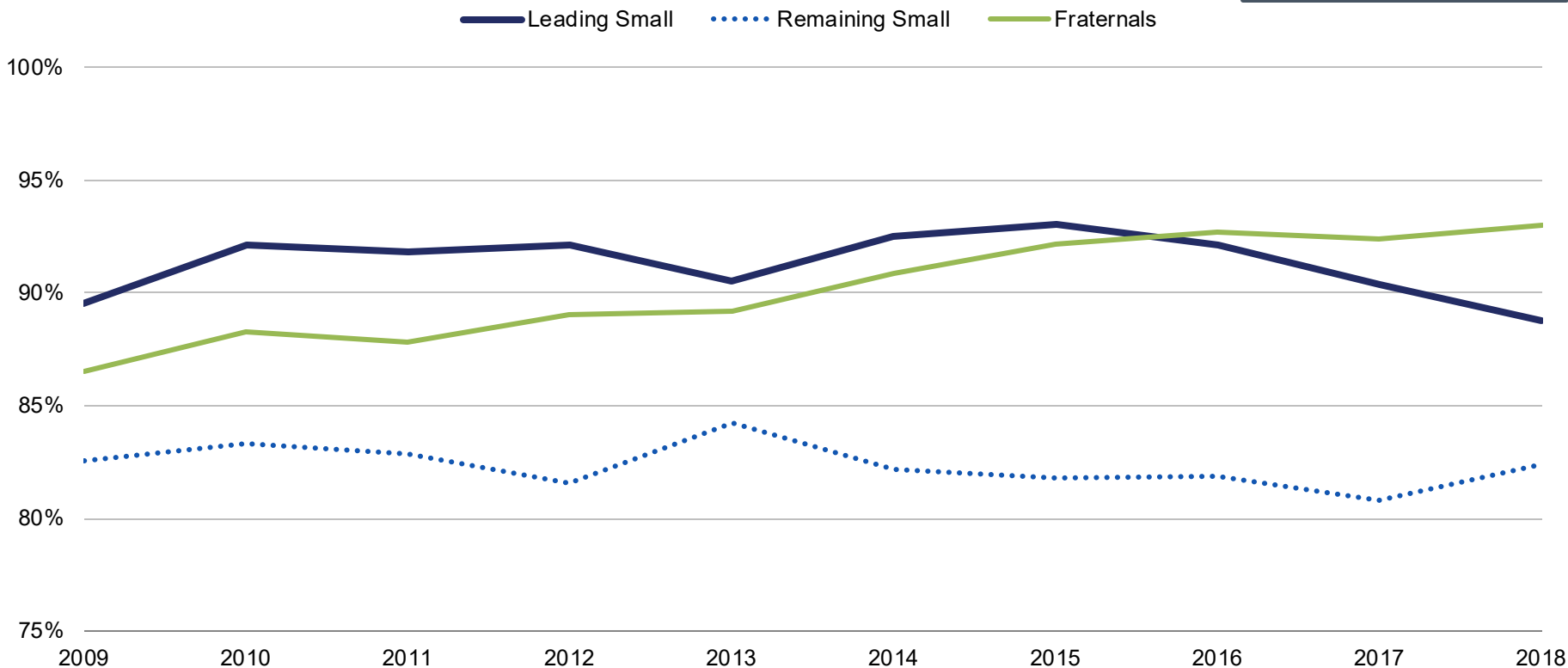
If the performance hurdle were set to 0%, 30 fraternal would still not meet the criteria.

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PREMIUM GROWTH AND PRODUCT FOCUS

Almost exclusive focus on individual life or annuity products

Percentage of Direct Premium from Individual Life and Annuity Products



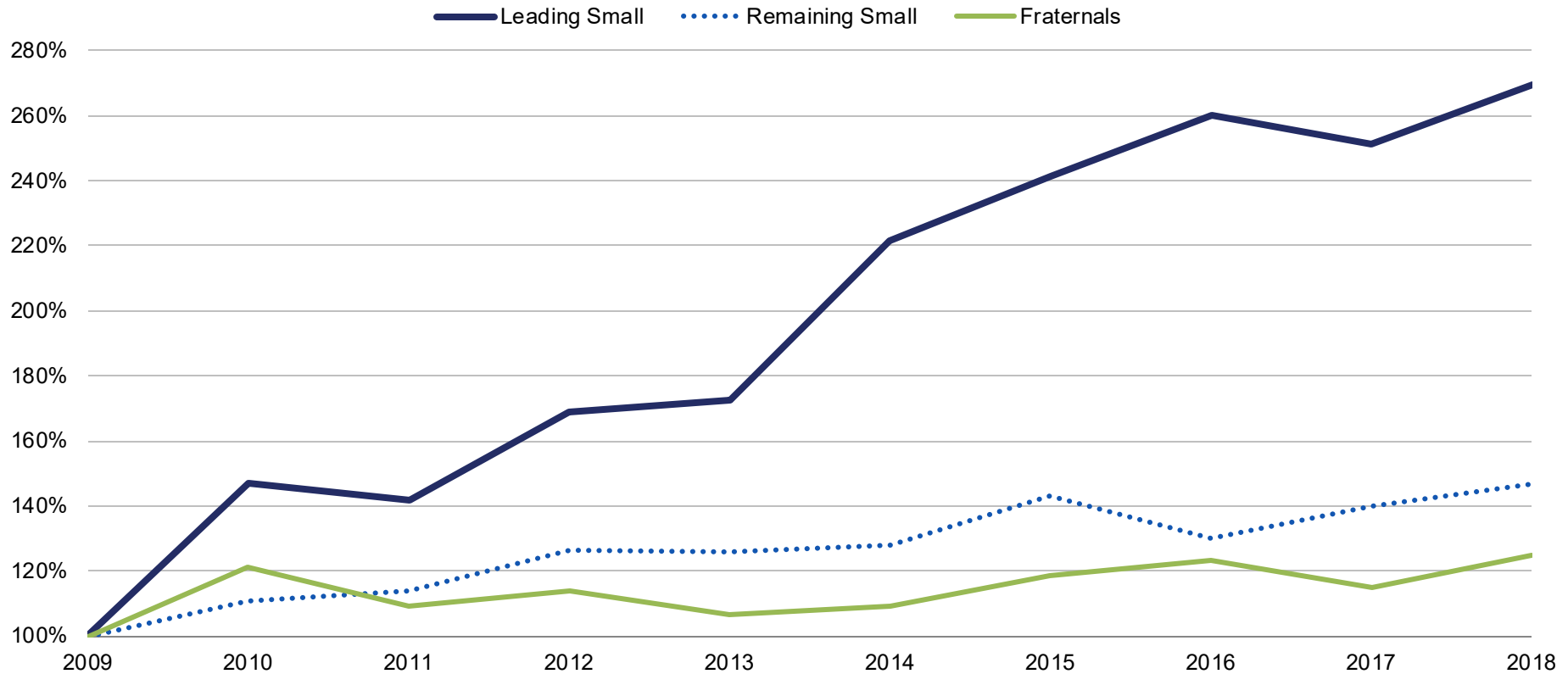
Fraternal have focused almost exclusively on individual life and annuity products, similar to the Leading Small companies.

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Fraternal Direct Premium Growth Lags

Total Direct Premium—All Lines of Business

Indexed from 2009



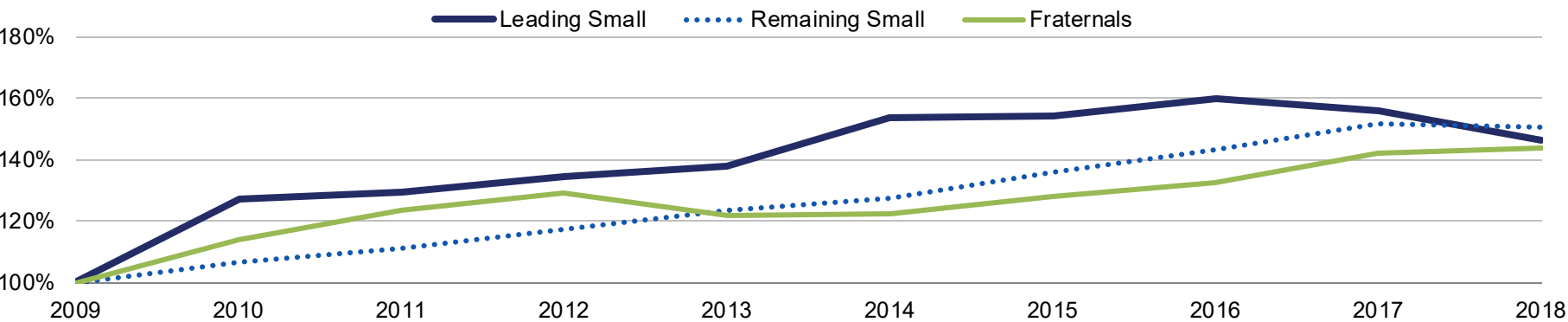
Fraternals had only a 2.5% CAGR in direct premium growth since 2009, compared to the **Leading Small** companies and **Remaining Small** companies with CAGRs of 11.7% and 4.4%, respectively.

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Direct Premium Growth by Product

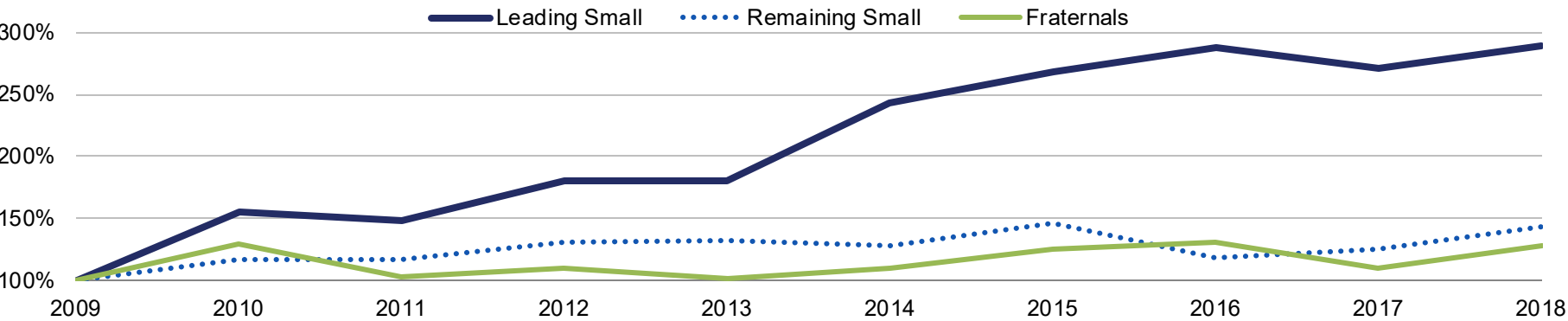
Total Individual Life Premium

Indexed from 2009



Total Individual Annuity Premium

Indexed from 2009



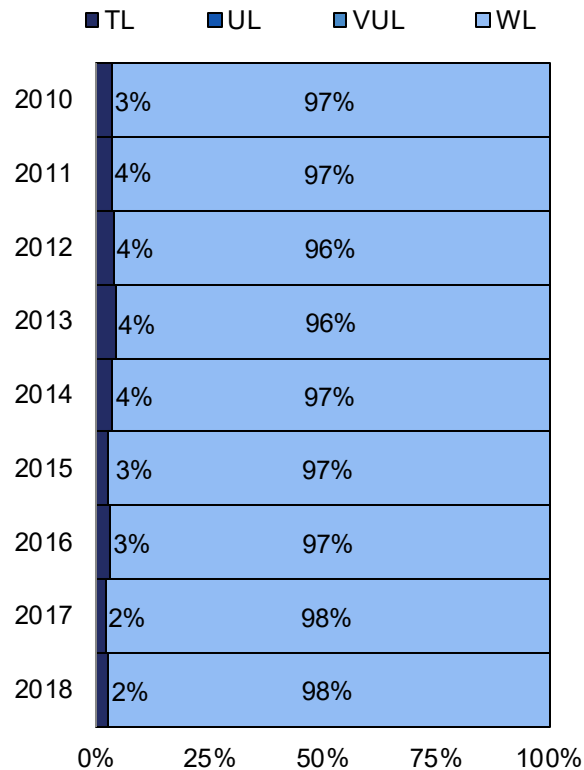
Total individual life premium growth for Fraternal lagged for several years, but caught up to the other Small company groups by 2018. Total individual annuity premiums for Fraternal is similar to the Remaining Small companies, but lags the Leading Small companies by a significant amount.

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Life Insurance Product Mix

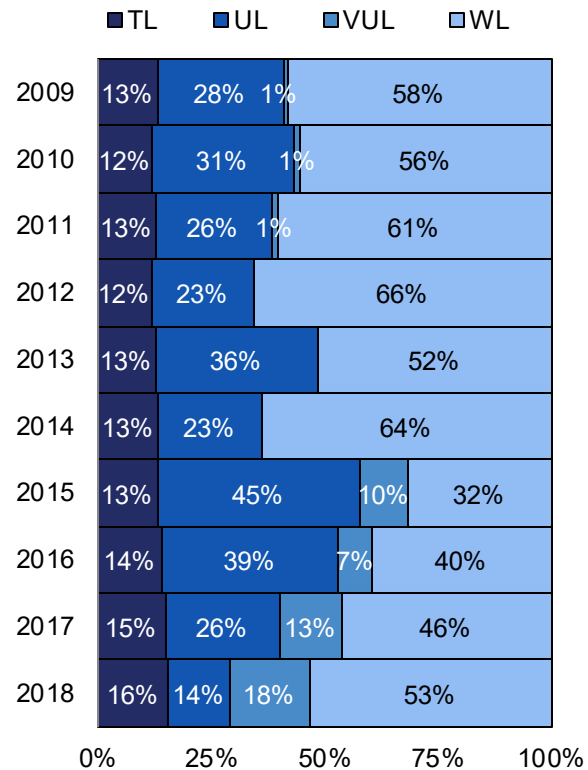
Remaining Small Companies

Product Mix Measured by Sales



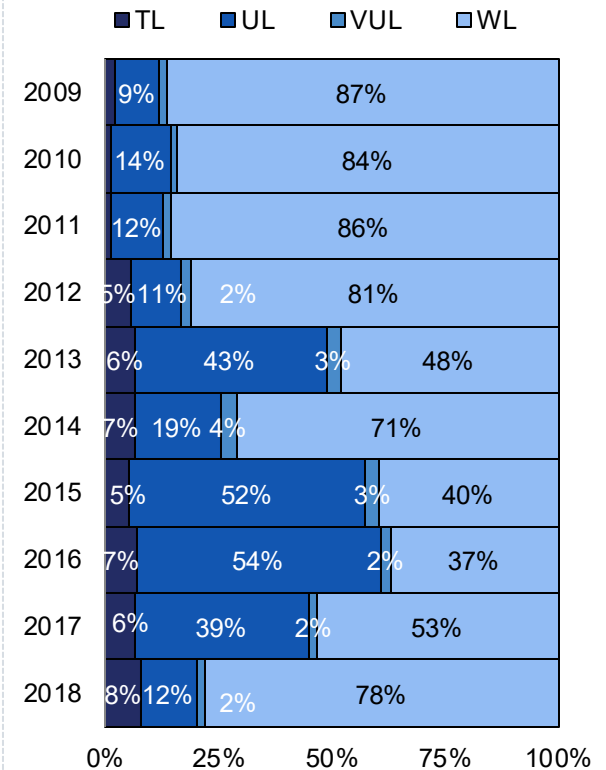
Leading Small Companies

Product Mix Measured by Sales



Fraternals

Product Mix Measured by Sales

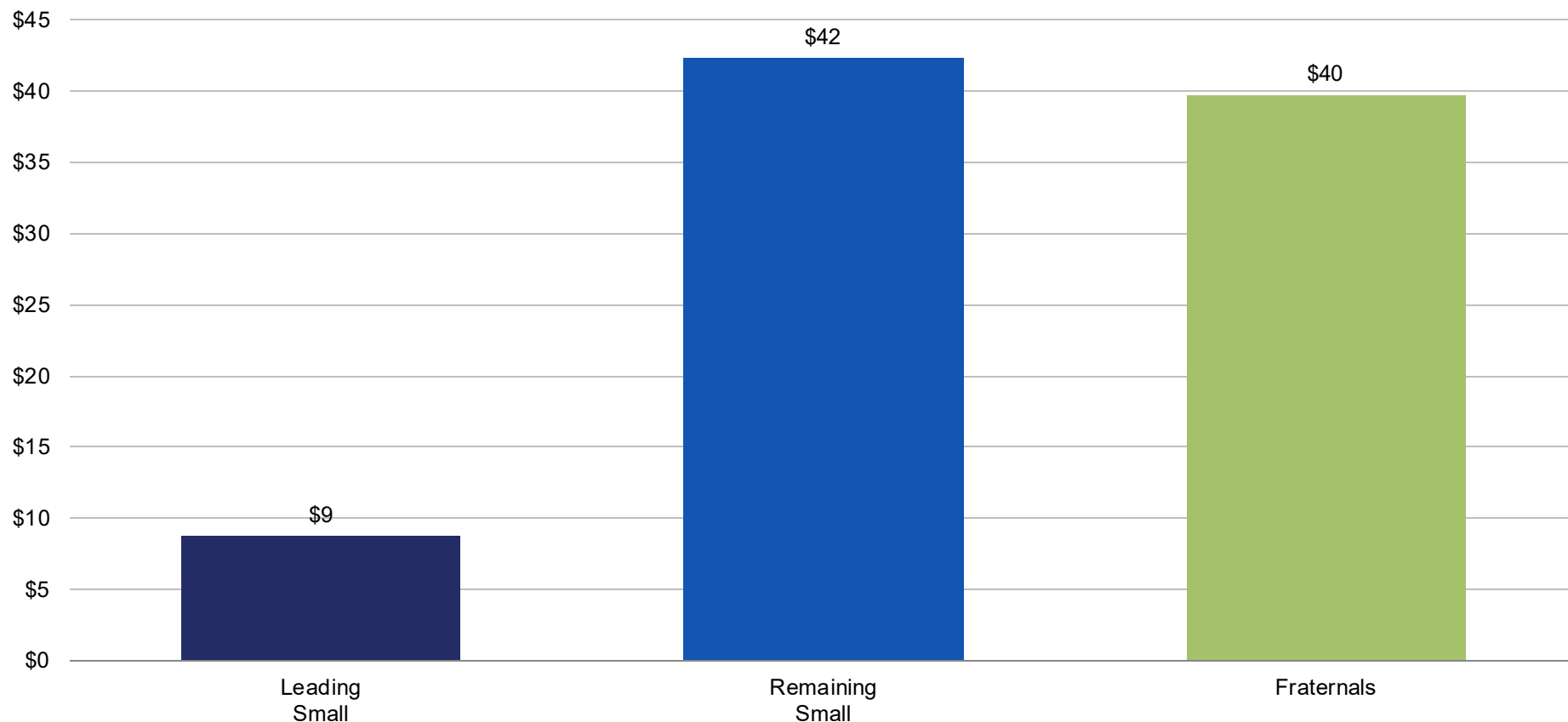


Fraternals have generally focused on whole life, although year to year volatility is evident.

POLICY FACE AMOUNTS

Average Policy Size of Policies in Force

\$ in thousands



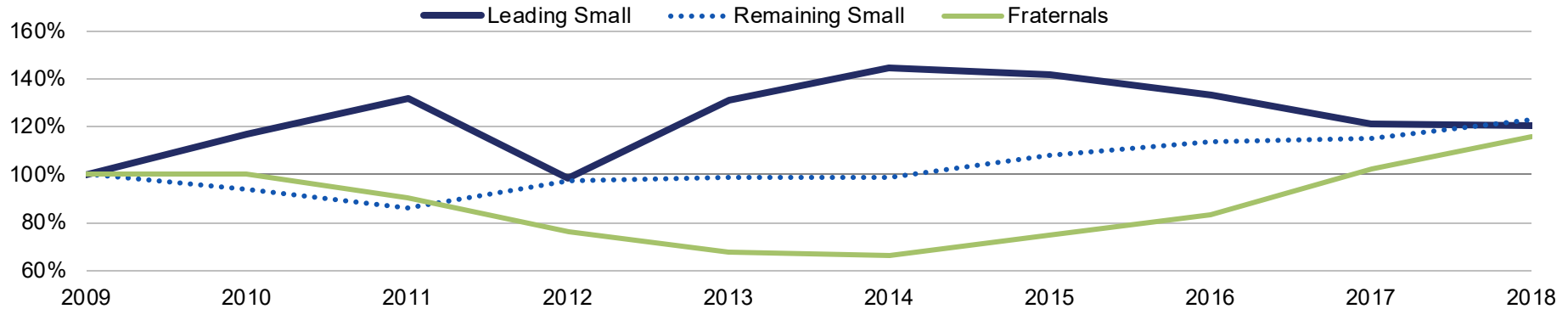
The average in force policy size for Fraternals is similar to the Remaining Small companies. Some of the Leading Small companies focus on final expense policies, resulting in a much smaller average policy size for that group.

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Total Face Amount

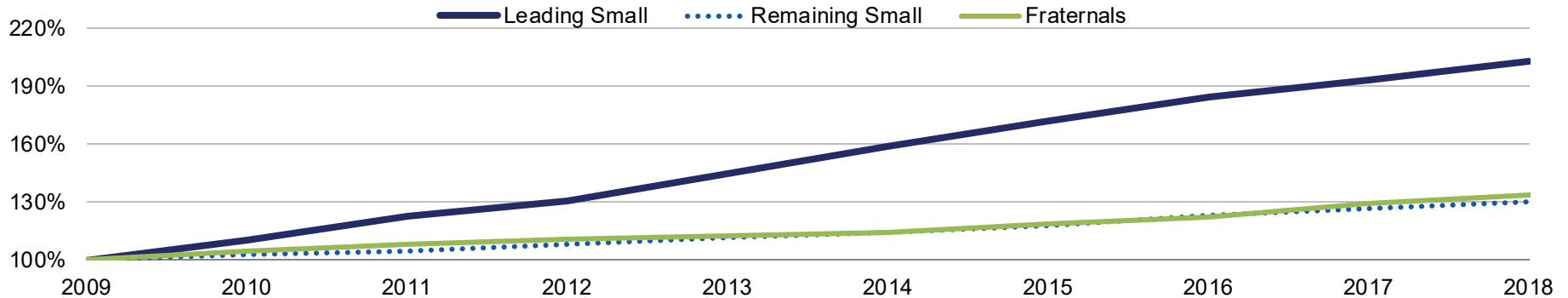
Total Face Amount of Individual Life Insurance Issued

Indexed from 2009



Growth in Face Amount In Force

Indexed from 2009



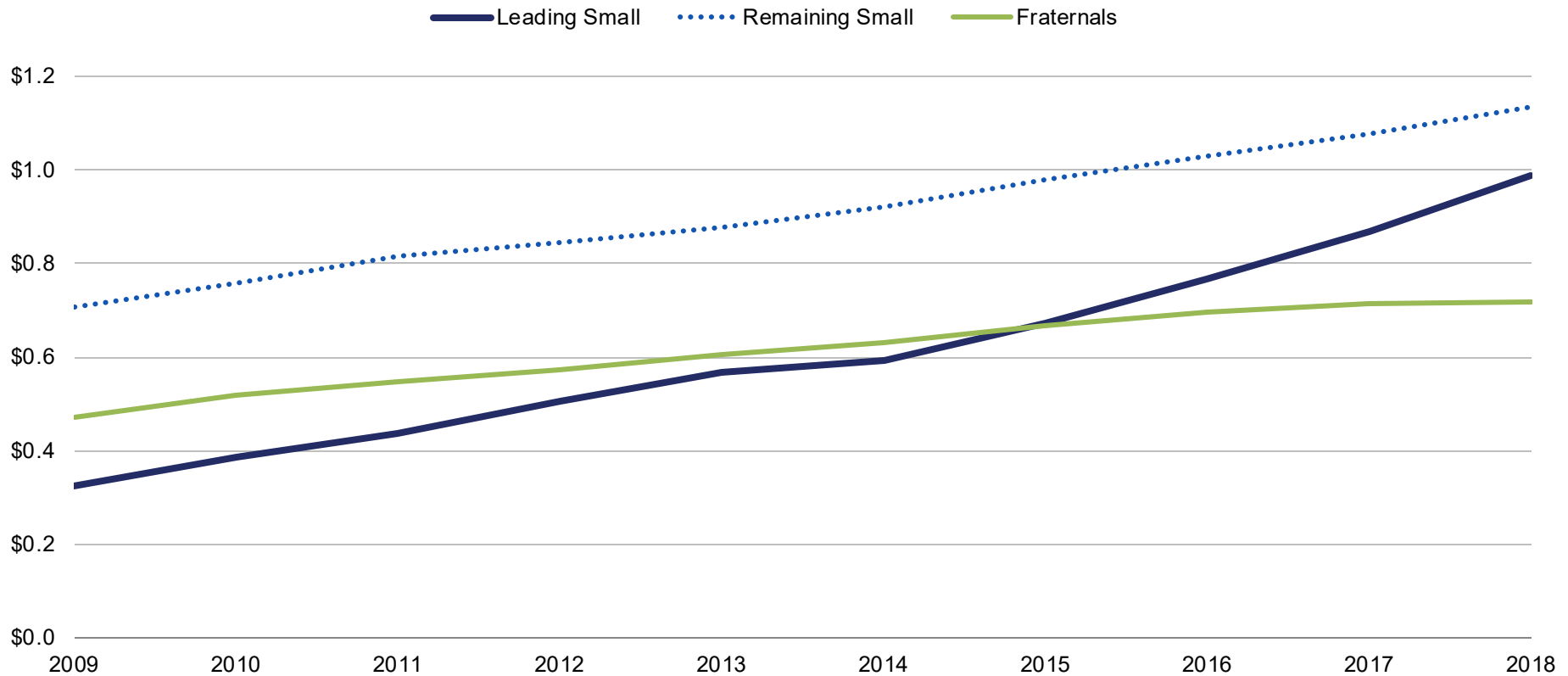
Growth in face amount in force for Fraternal has increased at a 3.3% CAGR, compared to 8.2% for Leading Small companies and 3.0% for Remaining Small companies.

ASSETS AND INVESTMENT PERFORMANCE

Asset Size

Asset Size—Average Net Admitted Assets

\$ in billions

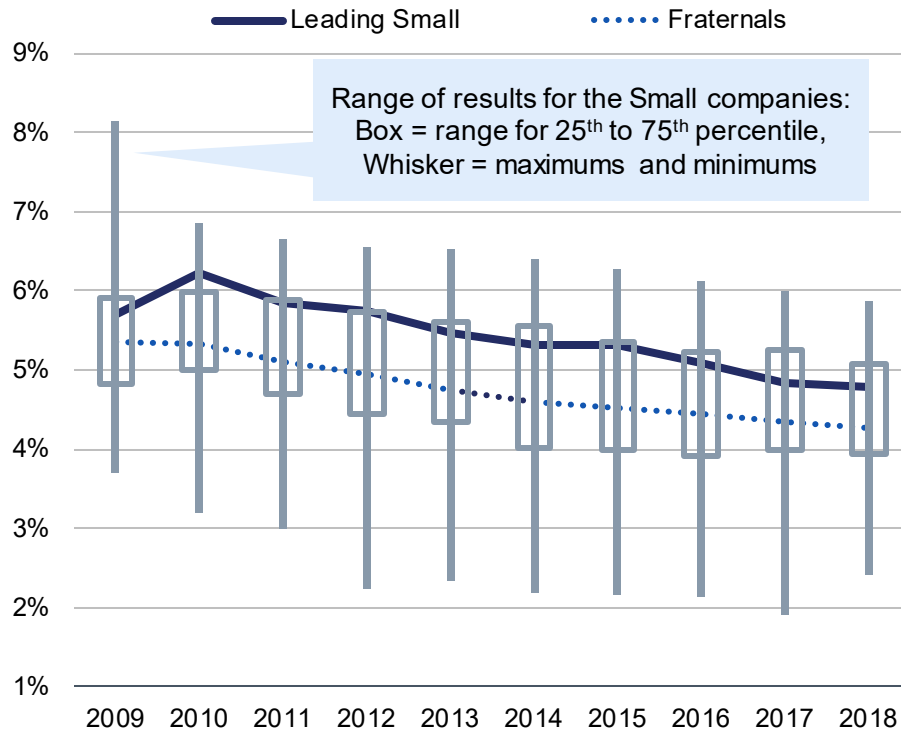


Leading Small companies have seen average net admitted assets increase 205.4% from 2009 to 2018, compared to 60.2% for Remaining Small companies, and only 51.6% for Fraternals.

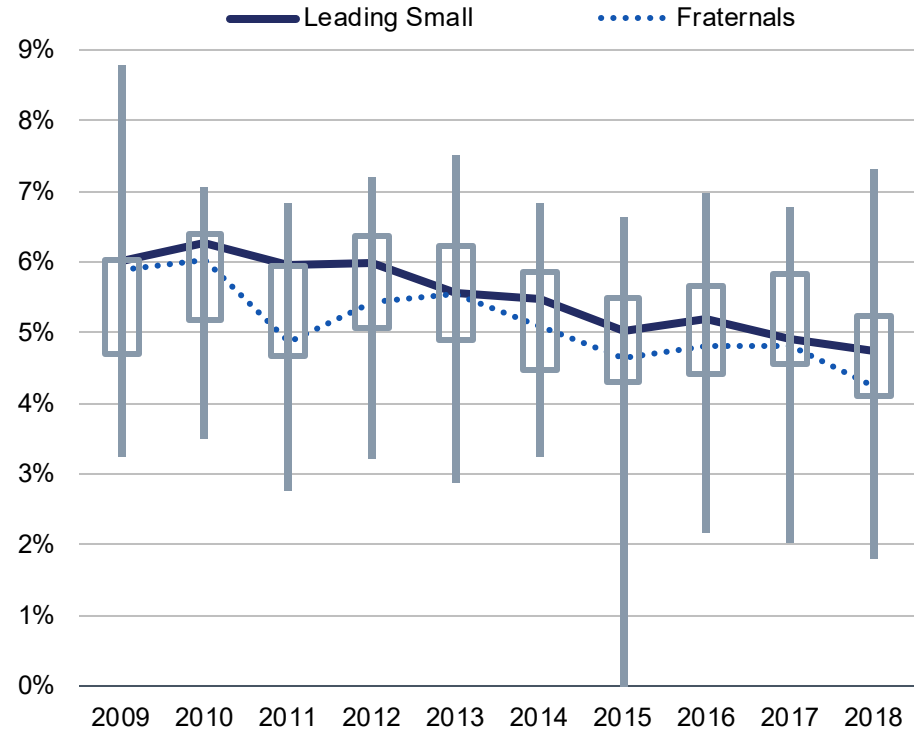
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Investment Return

Net Investment Income as a Percentage of Investable Assets*



Total Return on Average Investable Assets, Including Amortization of IMR*



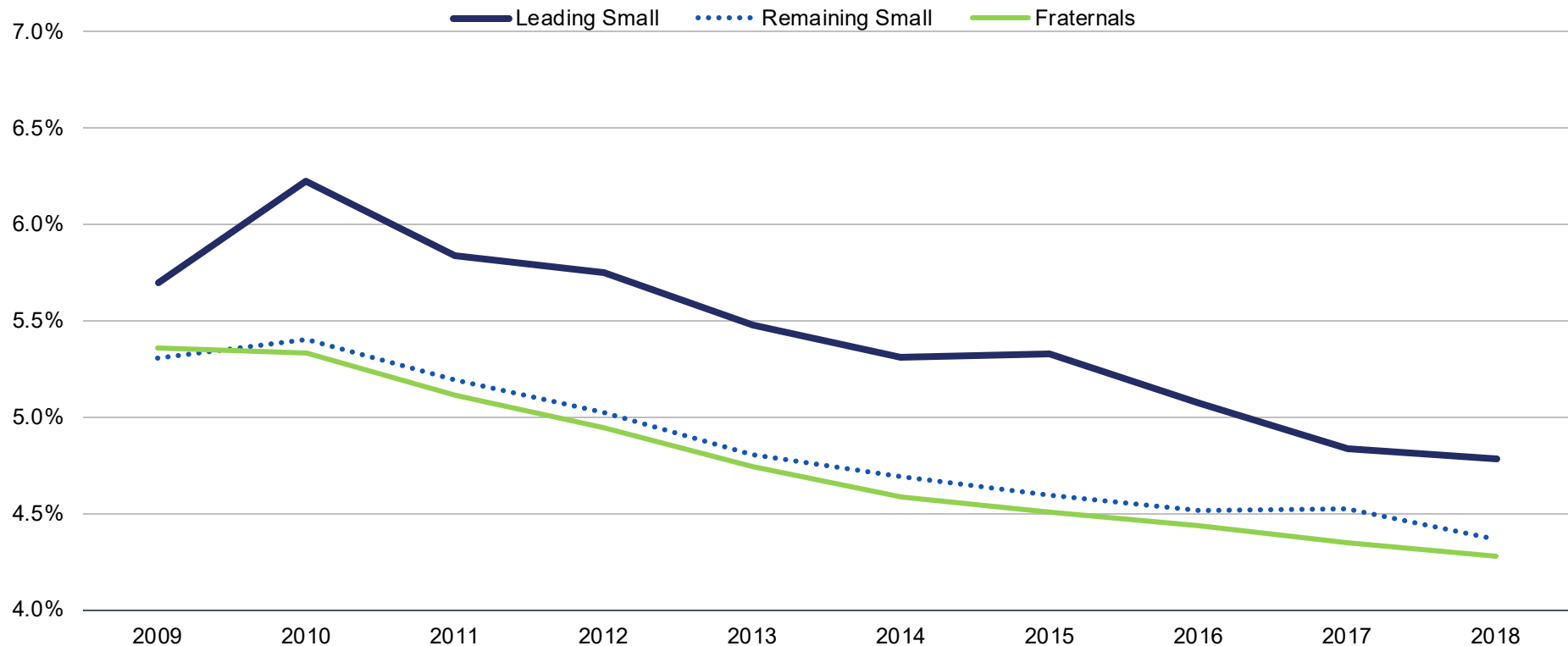
Investment return for Fraternals have been generally within the range seen for Small companies, but trails the Leading Small companies. Total return, including amortization of the IMR, has been more volatile for the Fraternals.

*Excluding outliers

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Fraternalists have Lower Net Investment Yield

Net Investment Income as a Percentage of Investable Assets

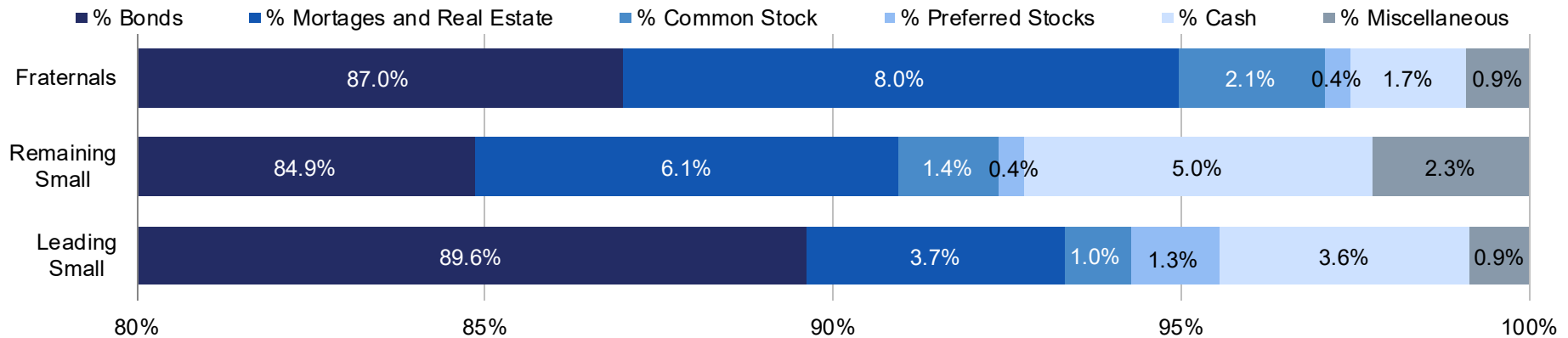


Leading Small companies had consistently higher net investment income as a percentage of investable assets compared to Remaining Small companies, and the Fraternalists had lower investment income than the Remaining Small companies.

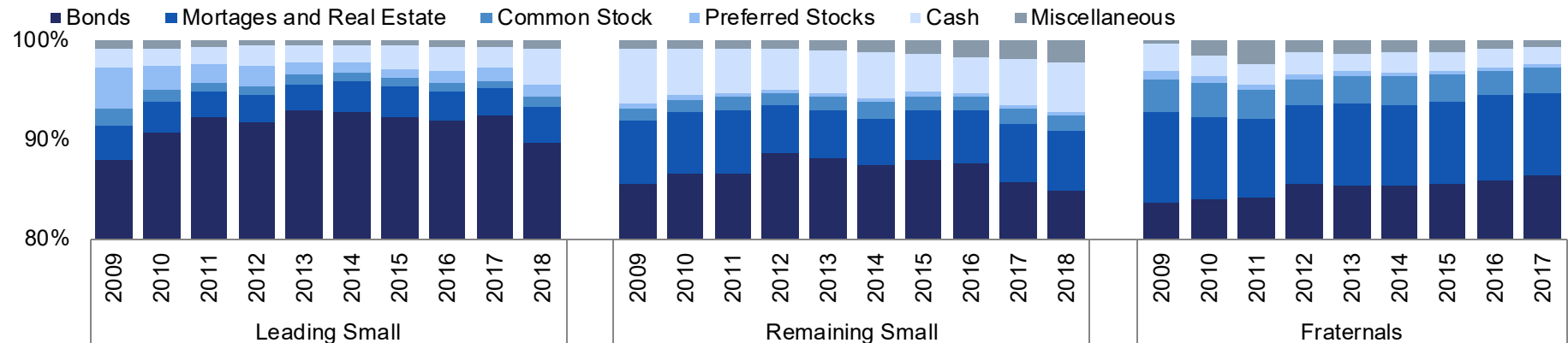
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Asset Mix of Fraternal

Percentage Distribution by Major Asset Class, 2018*



Percentage Distribution by Major Asset Class*



The Fraternal had more invested in mortgages and real estate than the Leading Small and Remaining Small companies. The Fraternal had significantly less invested in cash.

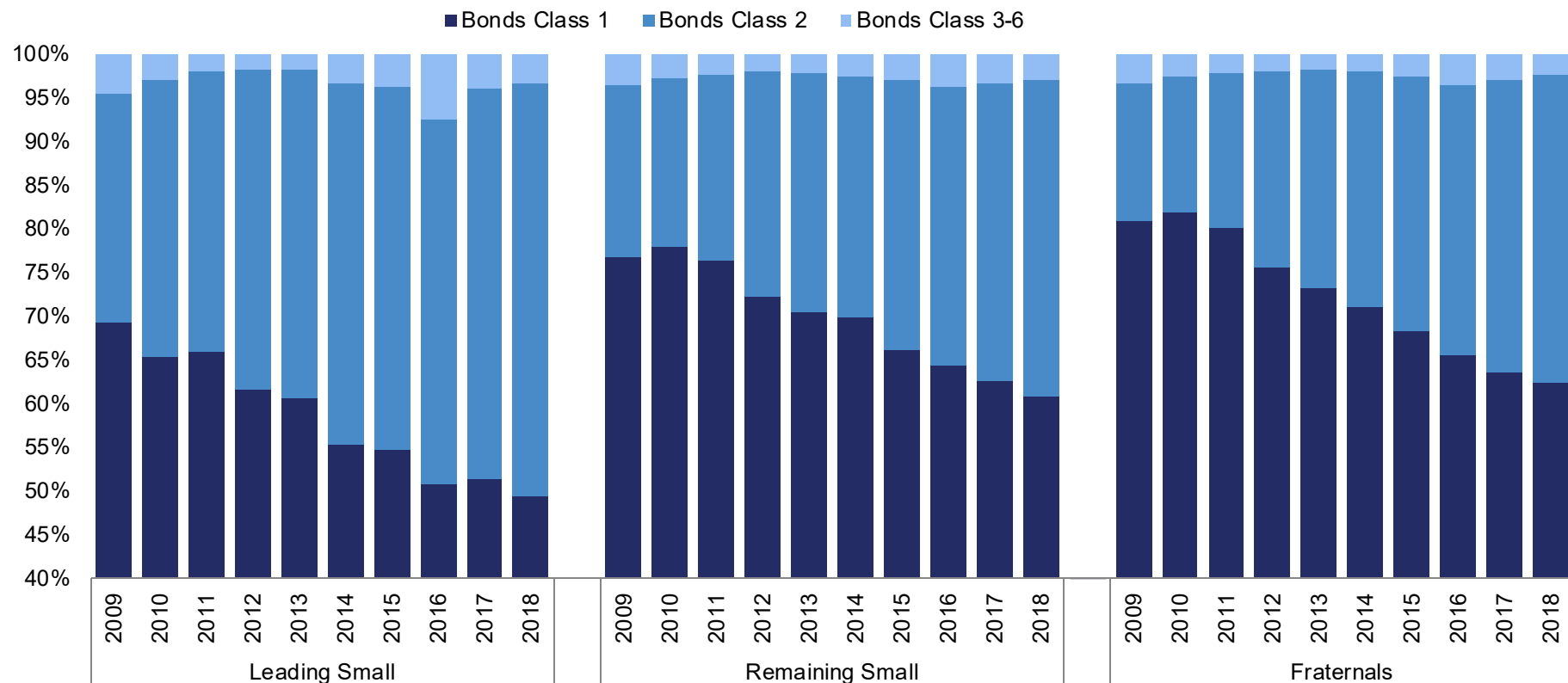
*Miscellaneous is the sum of assets reported in Schedule BA, receivables for securities, and aggregate write-ins for invested assets.

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Fraternal Bond Holdings more Conservative than other Small Companies

Bond Credit Quality—NAIC 1, NAIC 2, Below Investment Grade (NAIC 3-6), 2009–2018

% of bond portfolio

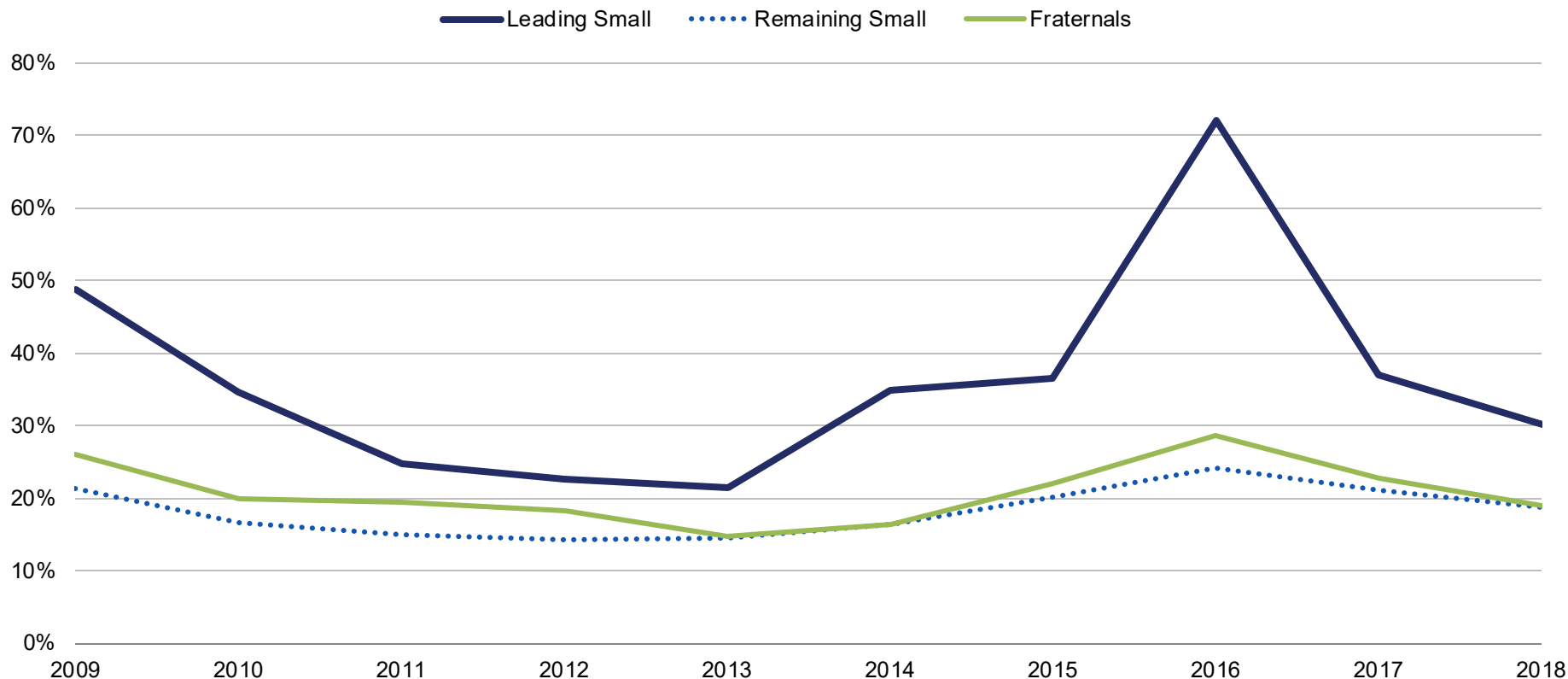


All three groups have increased their holdings of class 2 bonds between 2009 and 2018, searching for yield in the low interest rate environment, but the Fraternal retained more in Bond Class 1.

Bond Credit Quality Leverage has Remained Steady

Bond Credit Quality Leverage

Below Investment Grade Bonds divided by Surplus + AVR

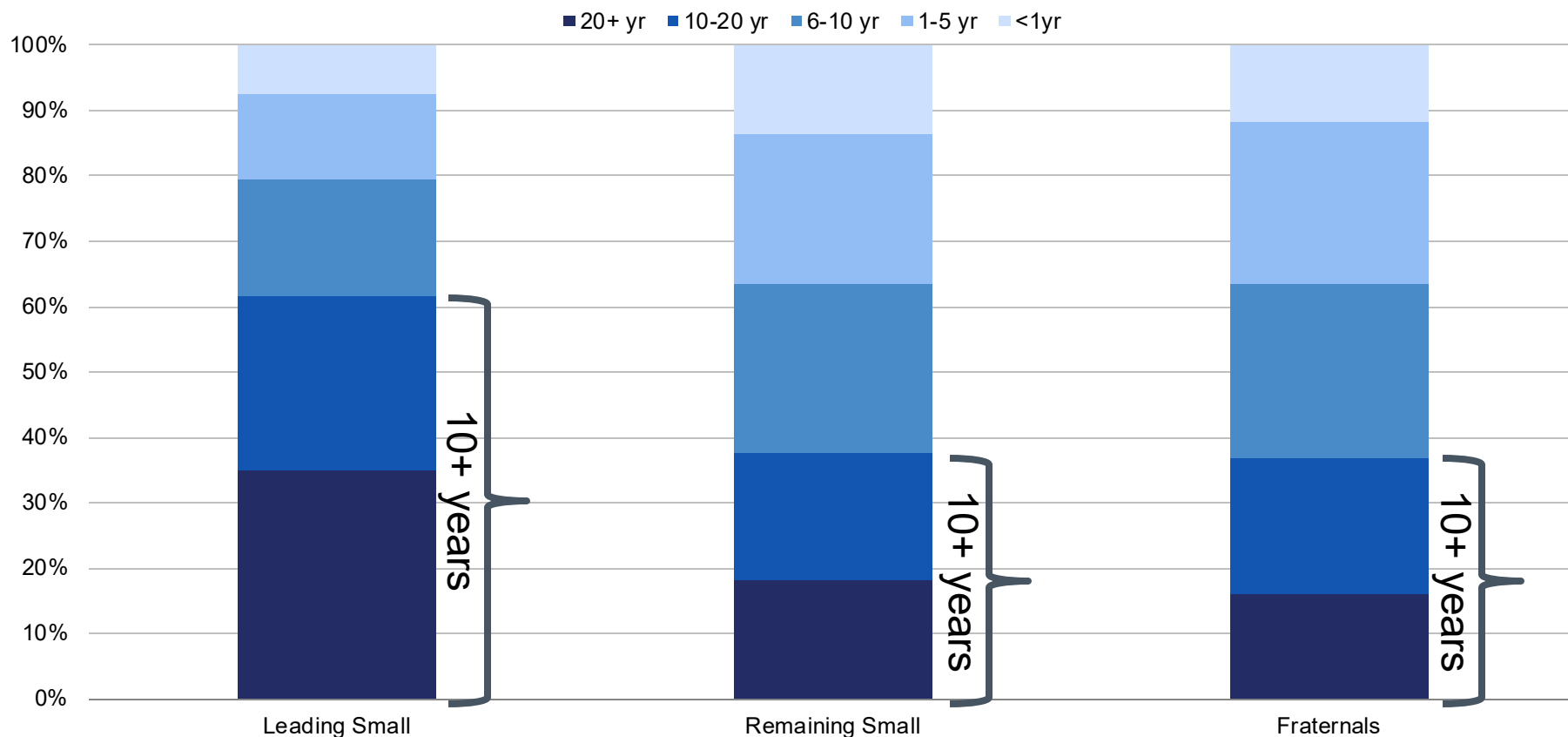


Leading Small companies bond credit quality leverage has fluctuated since 2009, falling to a low of 21.5% in 2013 and increasing to a high of 72.0% in 2016. In 2017, the leverage decreased to 36.9% and declined further in 2018 to 30.2%. The bond credit quality leverage for Fraternals and the Remaining Small companies has remained lower and more stable.

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Bond Maturity

Percentage of Bond Portfolio by Maturity, 2018

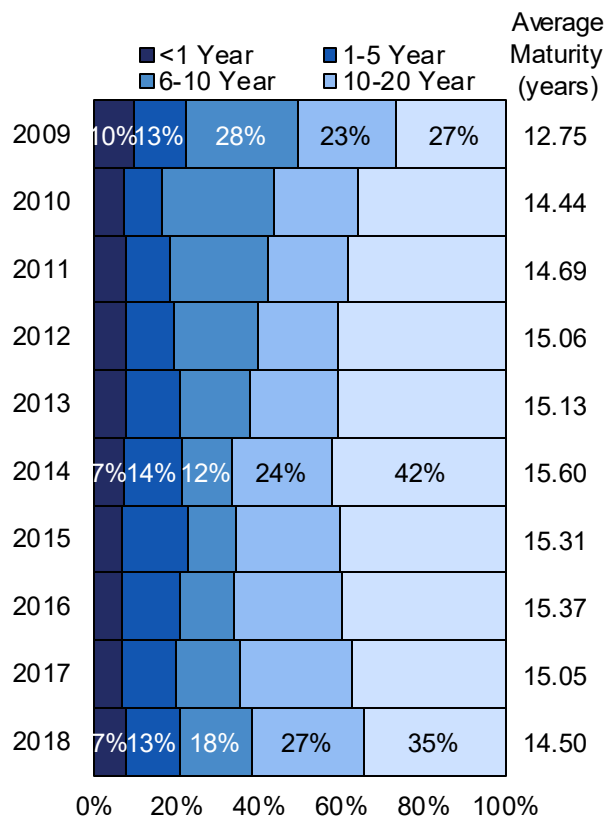


Leading Small companies have longer bond maturity, with 61.7% of the bond portfolio maturing in 10+ years. The Fraternals and Remaining Small companies had similar bond maturity profiles.

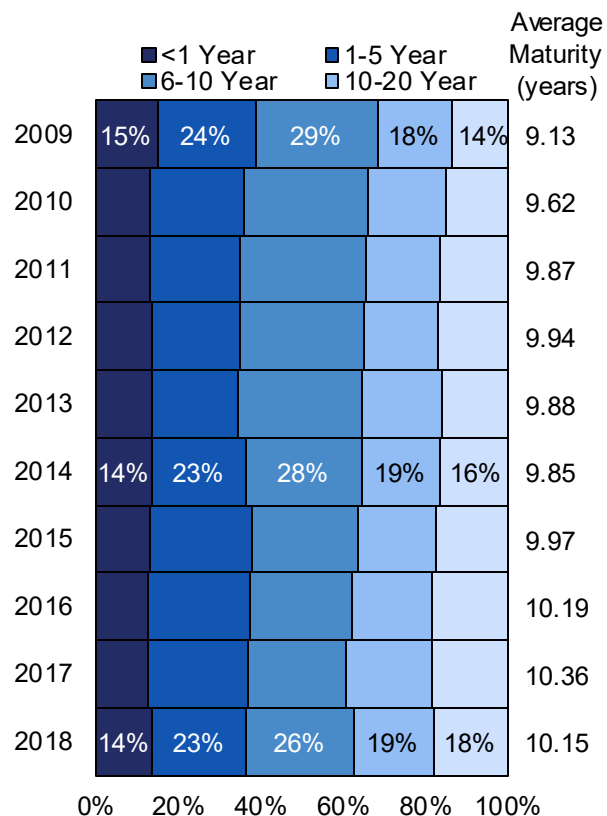
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Change in Bond Maturity

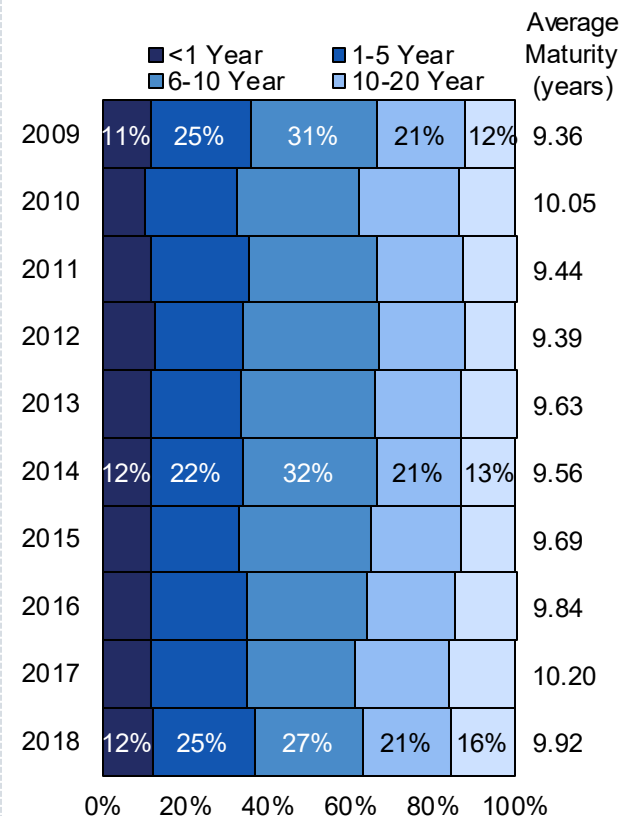
Leading Small Companies



Remaining Small Companies

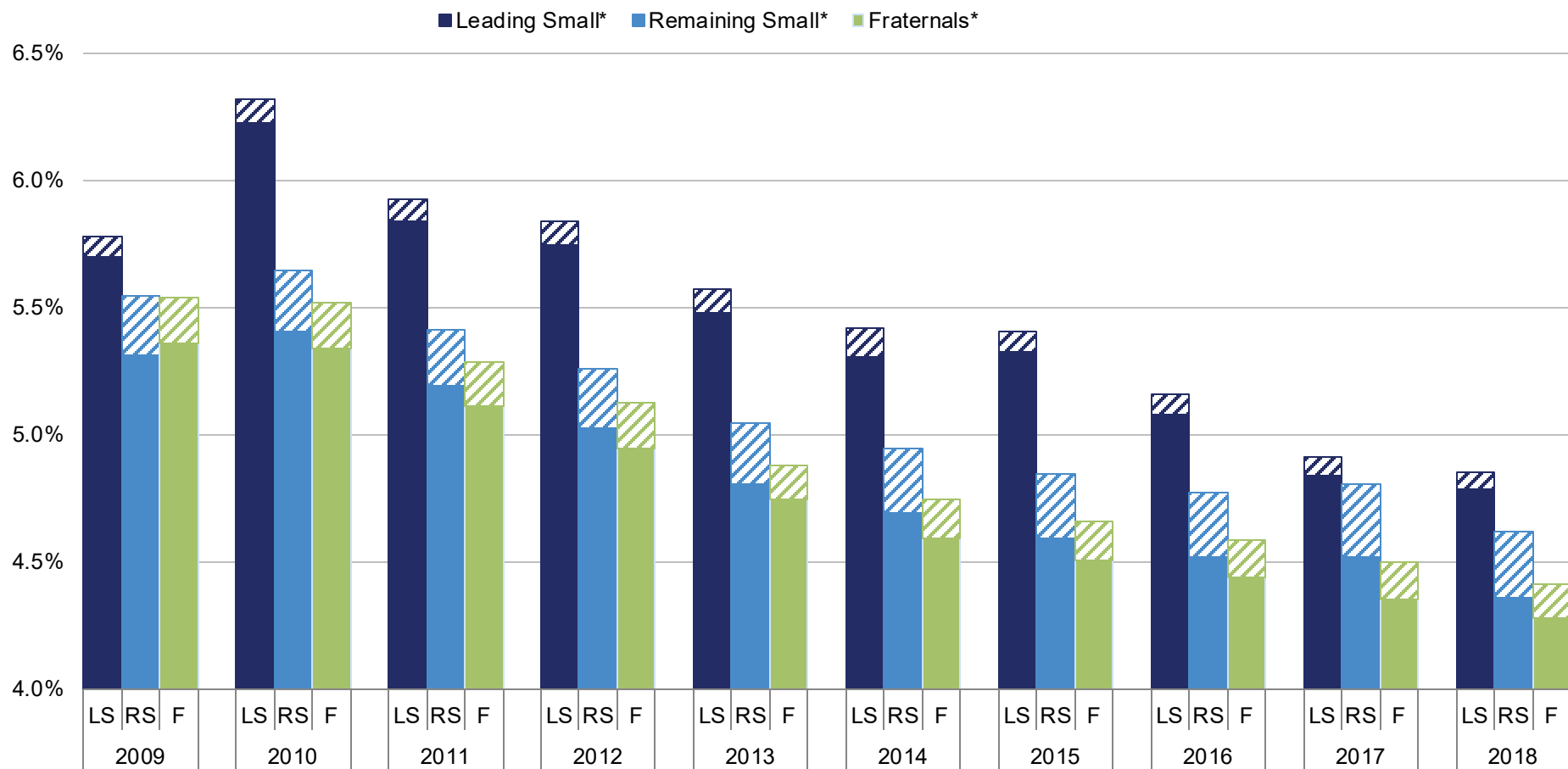


Fraternals



Leading Small companies significantly lengthened their portfolios and generated more net investment income than the Remaining Small Companies and Fraternal, which kept their portfolios shorter.

Investment Expenses & Net Investment Income



Leading Small companies had higher net investment return while also paying lower investment expenses to achieve that return, consistently outperforming Remaining Small companies. The Fraternals had lower returns, but also paid slightly less in investment expenses.

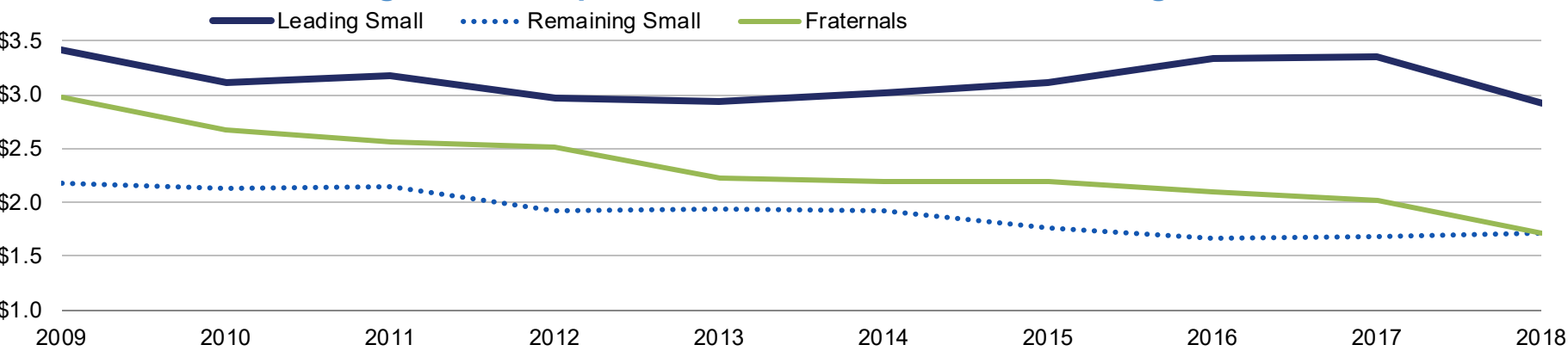
* The total height of each column represents gross investment income. The shaded portion represents the amount paid out as an investment expense. The solid portion represents net investment income.

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COMMISSIONS AND EXPENSES

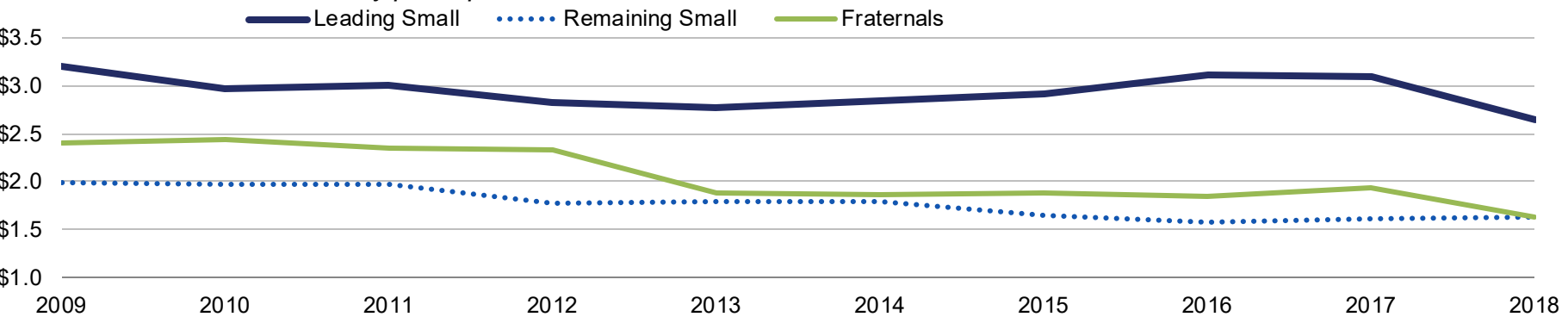
Sales and Commissions

Direct First-Year and Single Premium per Dollar of Direct First-Year and Single Premium Commission



Individual Life Sales per Dollar of Direct First-Year and Single Premium Commission

Excludes dividends used to buy paid up additions

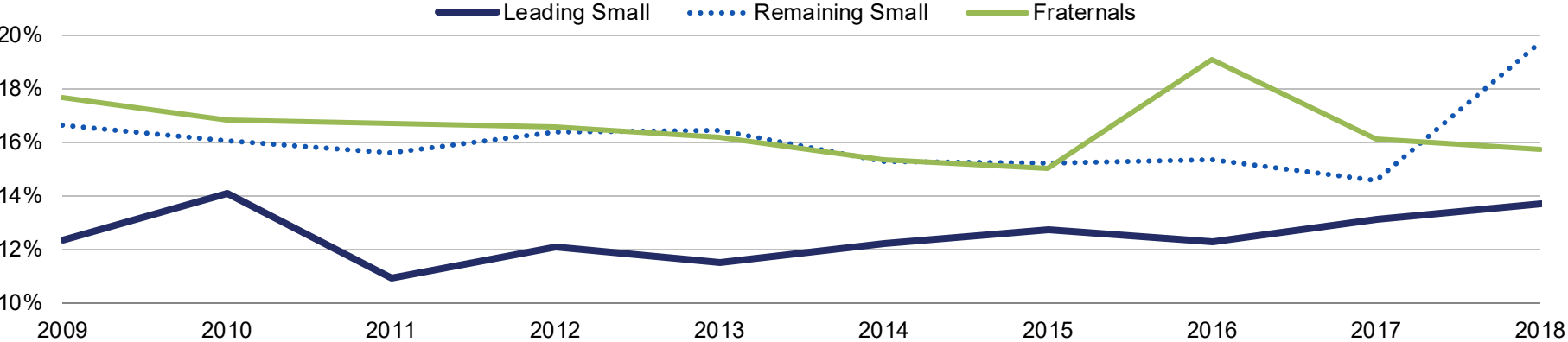


Individual life sales have decreased in 2018 for Leading Small companies, but remain above Remaining Small companies. Fraternal had similar results to the Remaining Small companies.

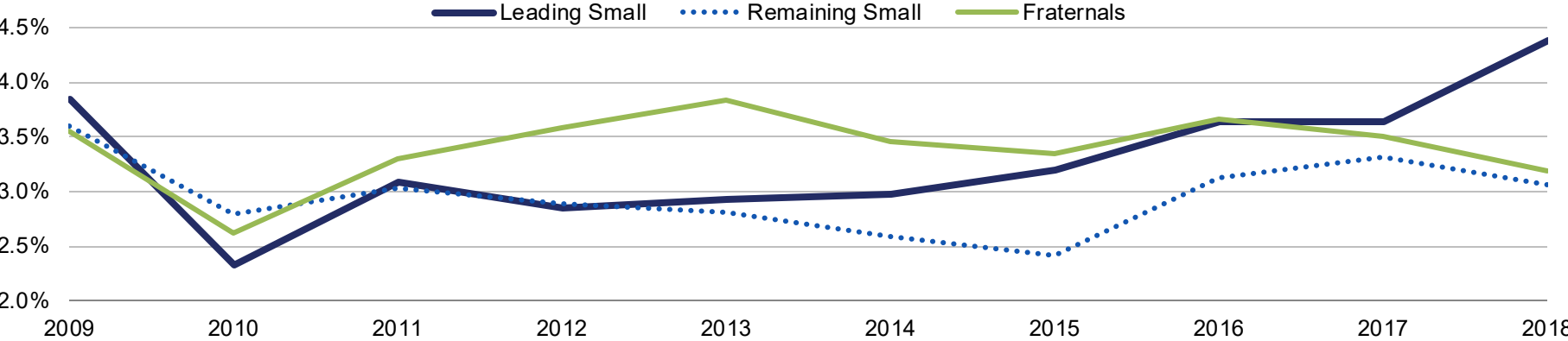
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General Expenses

Individual Life



Individual Annuities



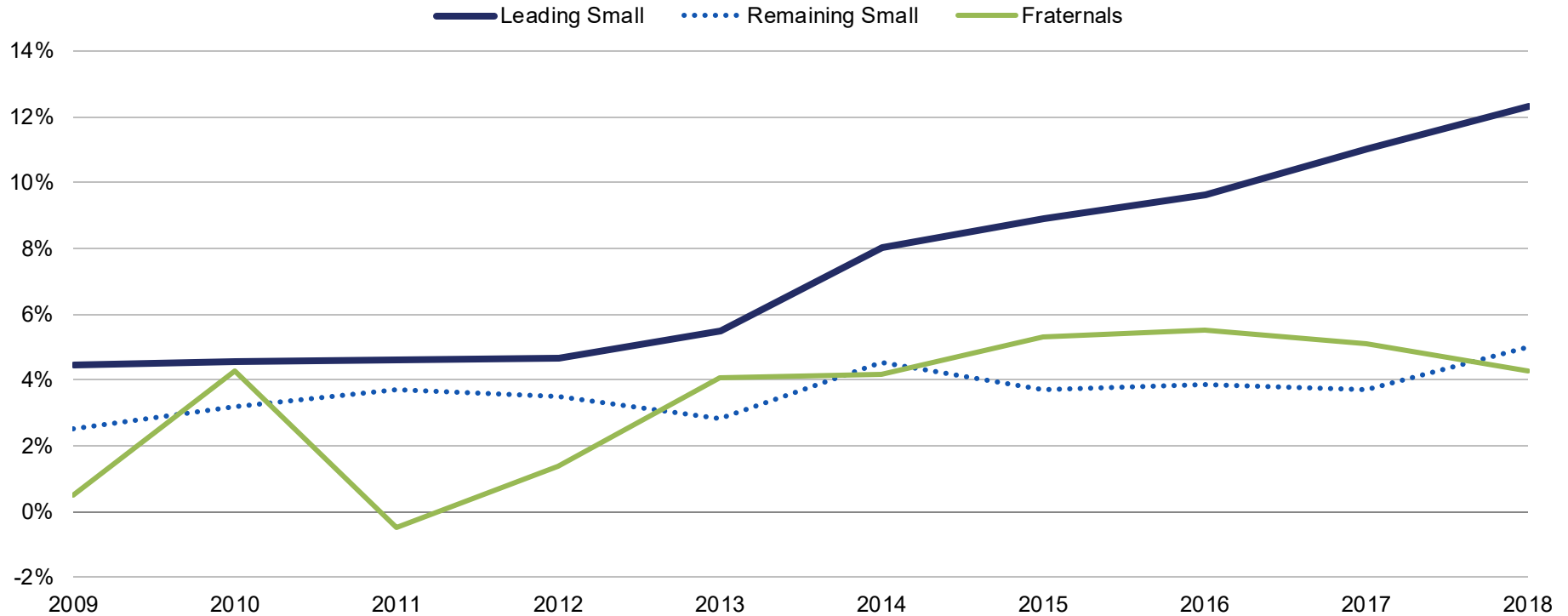
The Fraternal had individual life general expenses similar to the Remaining Small companies, apart from a spike in 2016. For individual annuities, the Fraternal had some years of higher expenses, but they have decreased since the peak in 2013.

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KEY PERFORMANCE RATIOS

Operating Margin

Combined Individual Life/Individual Annuity Net Operating Margin

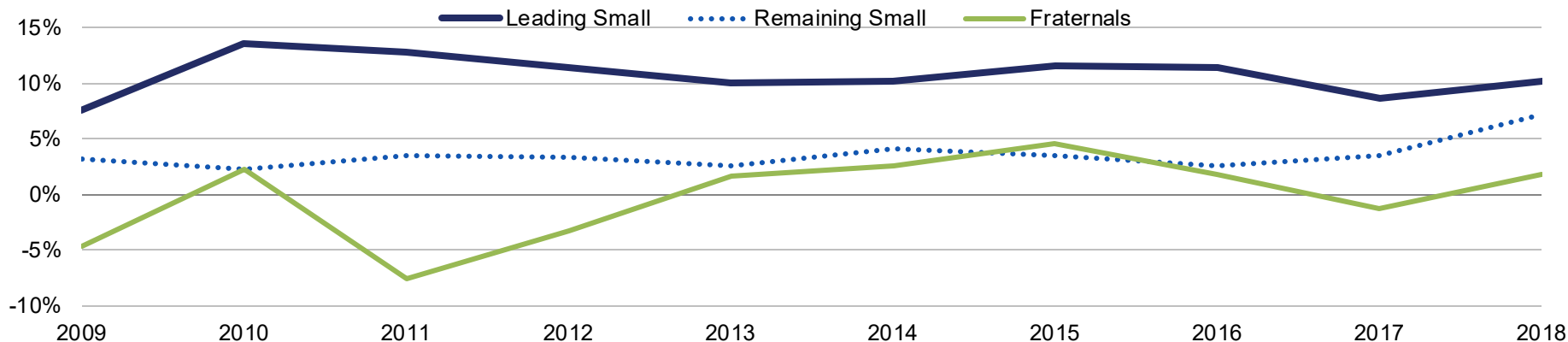


Fraternal operating margins have remained similar to the Remaining Small Companies, but have lagged the Leading Small company group.

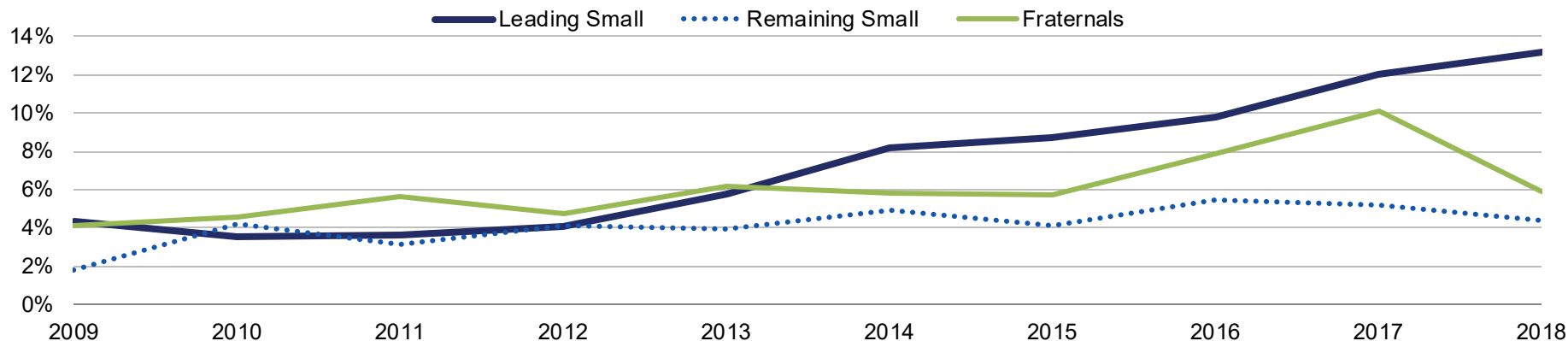
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Operating Margin

Individual Life



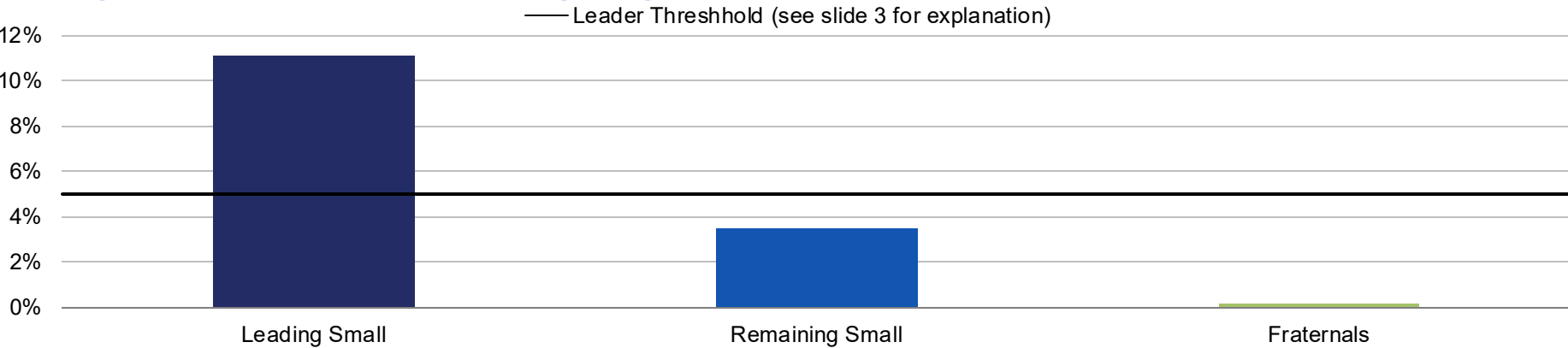
Individual Annuities



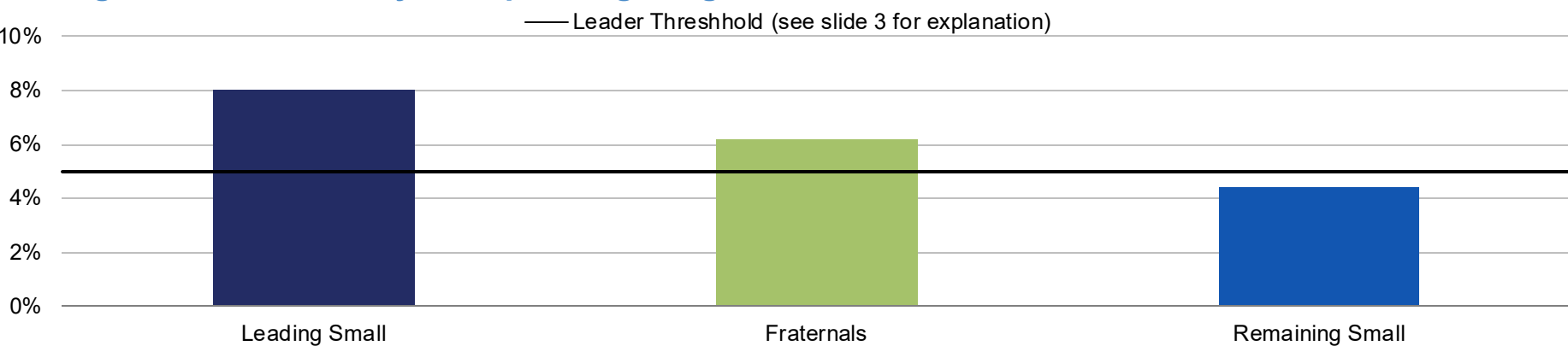
Individual life operating margins for Fraternal have generally lagged the other two groups. Individual annuity operating margins for Leading Small has increased to compared to Remaining Small companies, with the Fraternal having results between the two groups.

Operating Margin

Average Individual Life Net Operating Margin, 2009-2018*



Average Individual Annuity Net Operating Margin, 2009-2018**

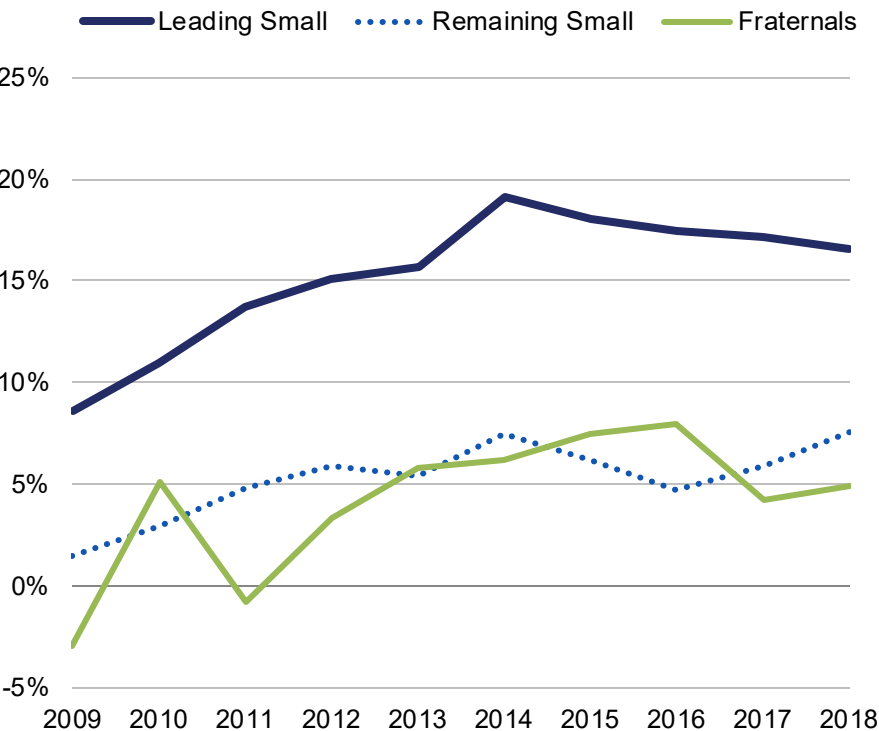


Losses in 2009, 2011, and 2017 result in the Fraternals having an average individual life net operating margin of only 0.2% for the 2009-2018 period.

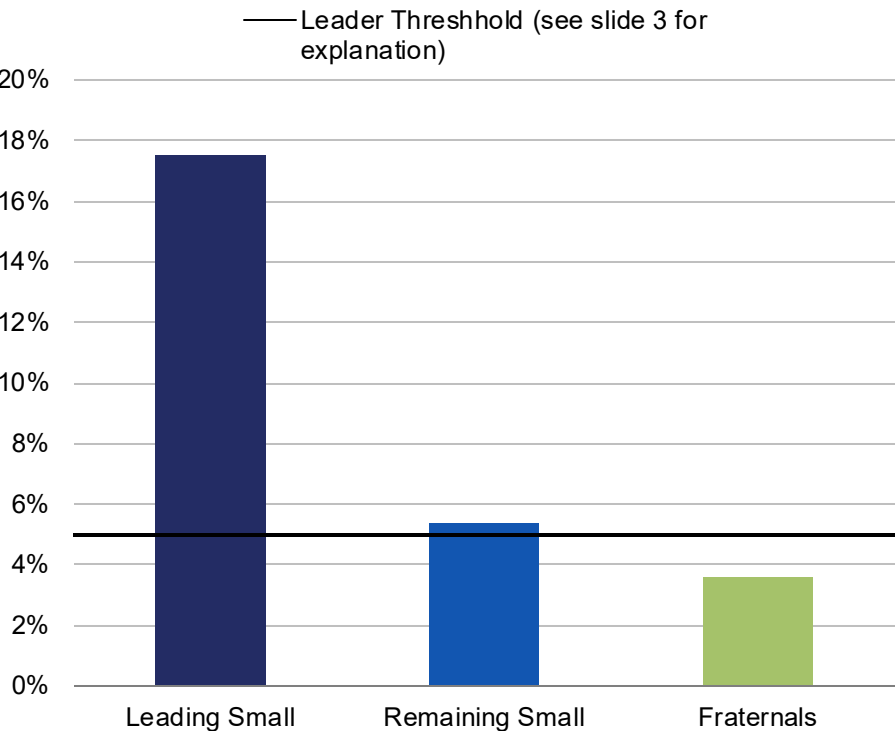
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Net Income Return on Surplus

Net Income on Surplus



Average Net Operating Gain Return on Average Surplus, 2009-2018

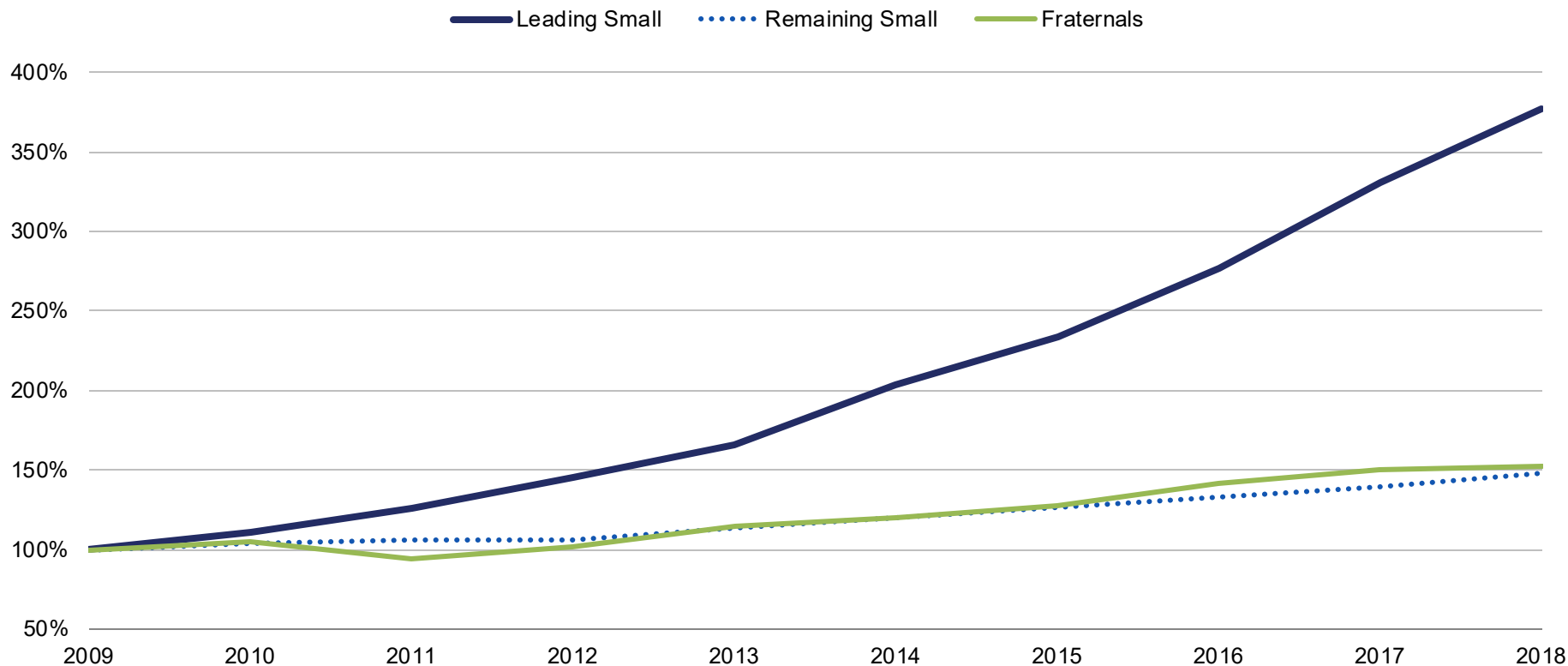


Net income on surplus for Fraternal has trailed the Remaining Small companies in most years. Leading Small companies had significantly higher net operating gain and net income compared to surplus than the Remaining Small companies and the Fraternals. That said, given their ownership structure, return on surplus may not be a priority for Fraternals.

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Capital & Surplus (Including AVR)

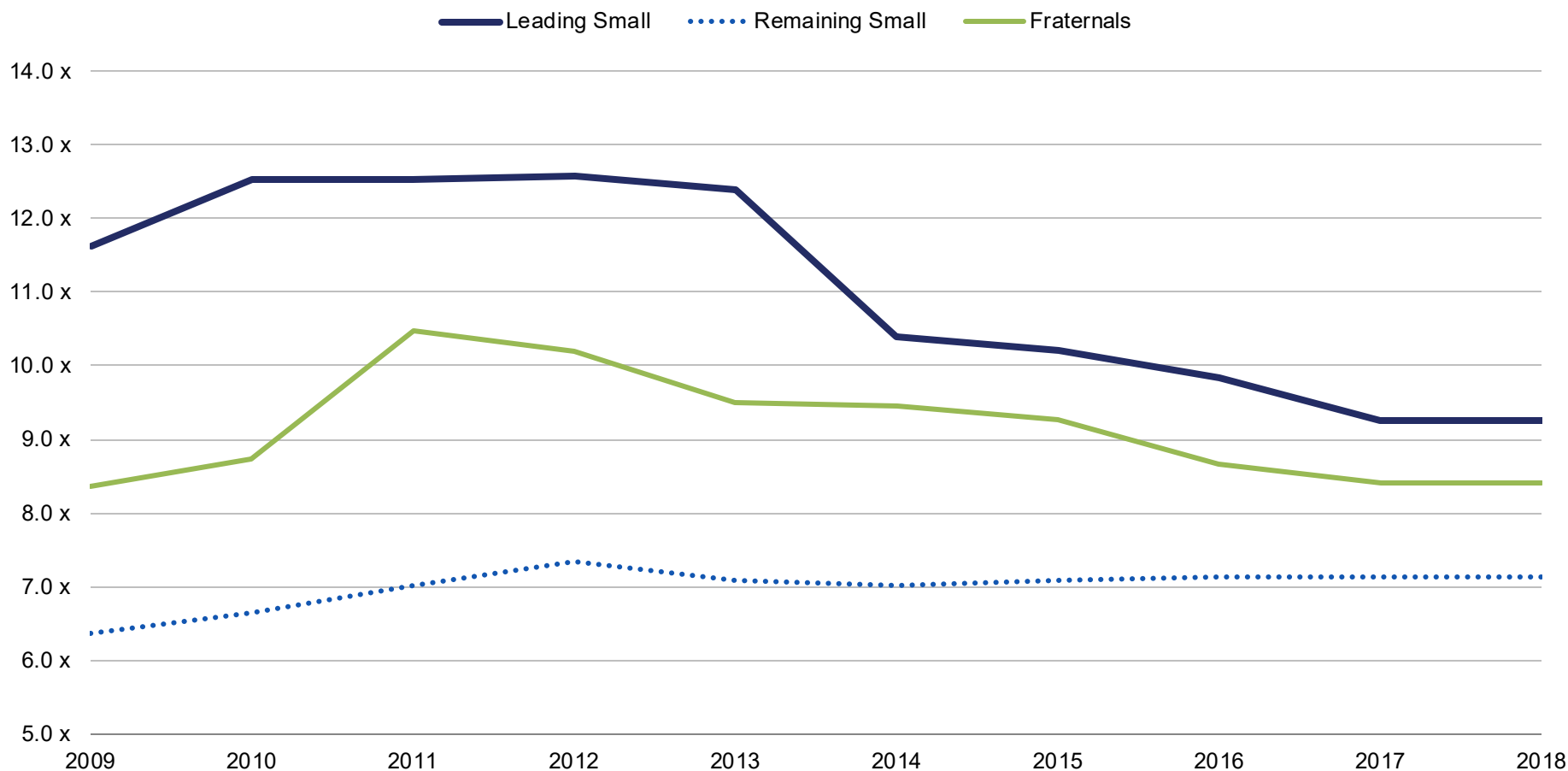
Indexed from 2009



The Leading Small companies have increased their surplus at a much higher rate than the Remaining Small companies and Fraternal, increasing 277.6% between 2009 and 2018, compared to Remaining Small companies and Fraternal which increased just 48.3% and 52.3% during the same period, respectively.

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Capital Leverage

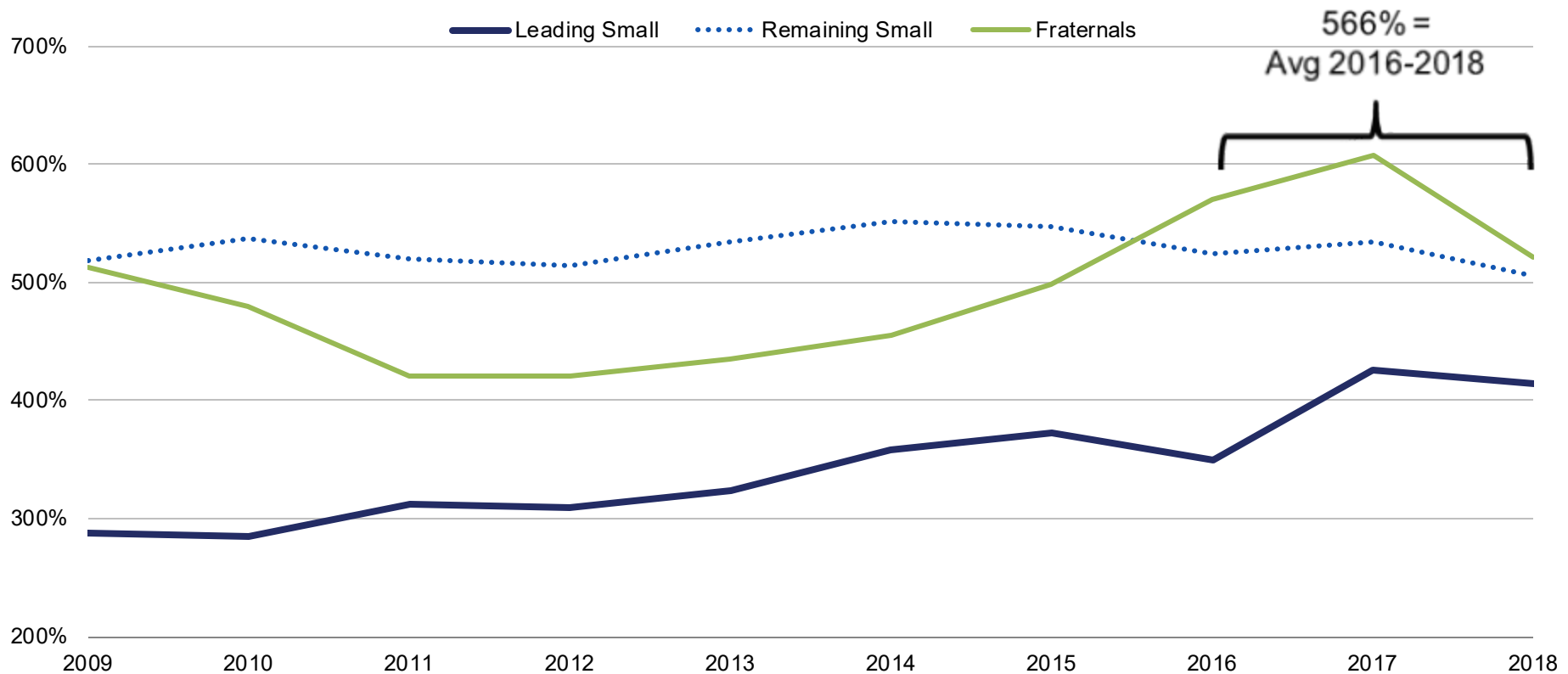


Fraternals have been consistently more highly leveraged than the Remaining Small companies, but less leveraged than the Leading Small companies. Capital leverage for the Fraternals has decreased from a high of 10.5x in 2011 to 8.4x in 2018, a decrease of 20%.

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Lower RBC Ratio, Ratios Have Increased

Company Action Level Risk-Based Capital Ratio



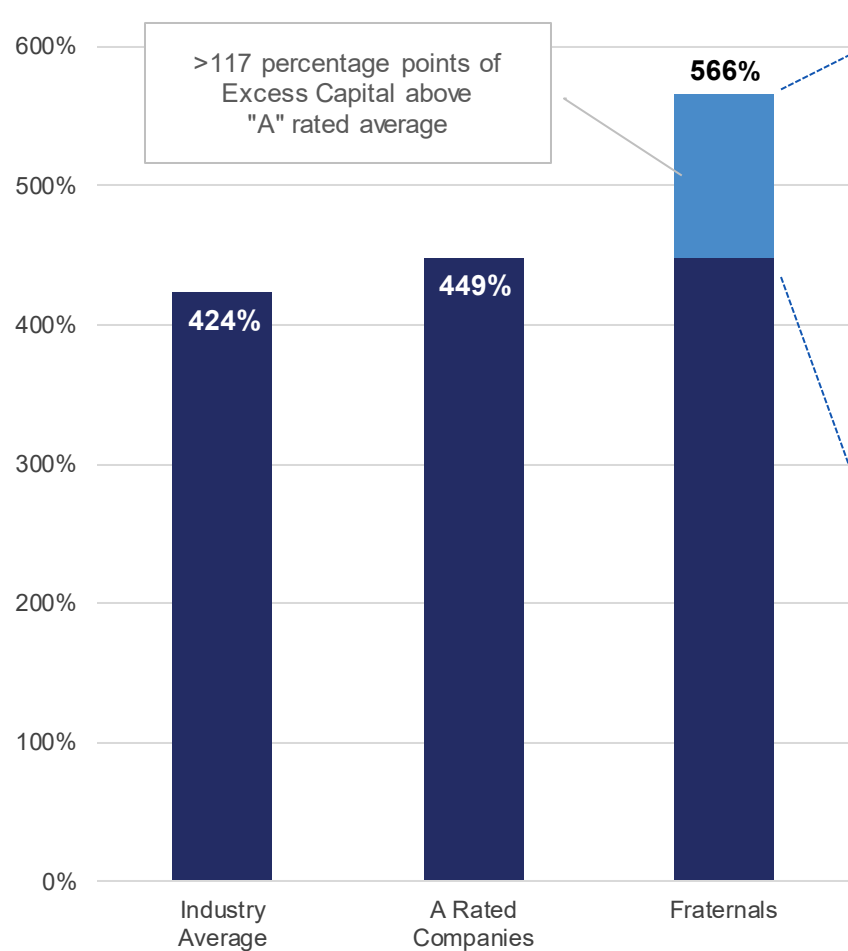
Fraternals have a slightly higher RBC ratio than the **Remaining Small** companies, but between 2010 and 2015, they had a lower ratio. **Leading Small** companies have maintained a lower RBC ratio than **Remaining Small** companies, but their RBC ratios have increased from 288% in 2009 to 414% in 2018.

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Strong Capital Position Generates Multiple Deployment Options

Fraternals Risk Based Capital vs Averages

Average 2016-2018, % RBC



Excess Capital Deployment Options

- Buffer above RBC
- Acquisitions
- Product diversification
- Process efficiency / improvement
- Change asset risk

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For More Information



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