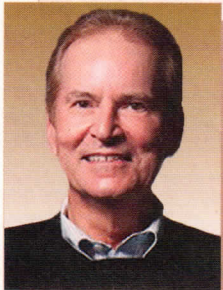


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# Life / Critical Illness Insurance Hybrids:

## Looking Forward, Looking Back

Life insurers are being severely tested by a shaky economic recovery complicated by dramatic changes in the benefits landscape. Ownership of individual life insurance (sold mainly through direct response and agent channels) has now hit a 50-year low, with 30 percent of today's households having no life protection whatsoever. (*Trends in Life Insurance Ownership* study, LIMRA, 2010).

And yet, despite significant reductions in consumer purchasing power, the desire for financial security continues to grow in proportion to concerns about protecting their assets and families. This period of economic and regulatory uncertainty presents a timely opportunity for those who are able to rise above the apparent chaos.

### The Case for Innovation

Individual life insurance is a mature industry in which conventional wisdom suggests that innovation is risky and being a fast follower is often the safer route. While this approach may work for market-tested products that are successfully selling under reasonably stable conditions, today's environment is anything but stable.

In these unconventional times, there are no easy fixes for those facing downward trends in core business sales and profits. Everyone in the business is facing the very serious challenge of persuading consumers that adequate insurance protection is essential, not optional.

Producers, as well as insurers, can either take a "wait and see" approach

(be a fast follower) or they can choose to break through with innovative products designed, packaged and marketed to fill the unmet needs of confused consumers (be a market leader).

### The Case for a Life/Critical Illness Insurance Hybrid

There are strong synergies for everyone in the market chain by packaging these coverages. A life-based policy with a critical illness component is an easily understood product that protects the insured's family through living benefits (critical illness insurance that pays cash to cover costs associated with catastrophic illnesses), as well as death benefits (life insurance that compensates for the loss of a primary wage earner).

Buyers who may want the protection of life insurance often delay purchase because of concerns about its affordability or cost benefit value. For many of these reluctant buyers, the addition of living benefits to a critical illness policy could well tip the scale and accelerate the purchase decision.

Critical illness insurance pays a lump sum upon diagnosis of critical conditions including life-threatening cancer, heart attack and stroke ("the big three"), along with other serious conditions such as renal failure, organ transplants and paralysis. Insurance proceeds can be used for medical costs, as income replacement, and for the countless other expenses families face when a breadwinner is critically ill.

The value proposition is equally compelling for insurers and producers who

are seeking new revenue sources to offset sluggish sales in core life business. Life/critical illness hybrids can offer strong positive product differentiation, as well as significant synergies in marketing, selling and underwriting. What's more, adding critical illness insurance living benefits need not be a significant resource drain for life insurers:

- The product does not appear to be impacted by Affordable Health Care Act provisions (including impending minimum loss ratio requirements for health insurance), and is relatively straightforward from a regulatory standpoint.
- Current in-house capabilities of life carriers can handle most critical illness insurance administrative functions, and/or they can be efficiently outsourced.
- Critical illness insurance is a relatively short-tail risk (in contrast to long term care insurance or annuities).
- The product is a simple, easily-understood proposition for consumers seeking value-added financial protection.

#### Considerations for Product Design

To optimize market appeal, product design should begin with consumer price points for each target market. A life/critical illness insurance hybrid offers pricing flexibility to enhance affordability, while delivering a range of higher-value options for various upscale markets.

Critical illness insurance can be linked to life insurance through acceleration, a lower-cost approach in which the policyholder receives a pre-determined portion of the life face amount, thus reducing the ultimate death benefit. It can also be positioned as an optional rider, delivering critical illness benefits in addition to basic life benefits, which can be tailored for a wider range of upscale prospects.

To maximize consumer appeal, we recommend that life/critical illness hybrids be packaged with term or whole life that offer guaranteed premiums/benefits. But no matter how a hybrid is structured, from a marketing standpoint it is preferable that the product be packaged as a one-app/one-sale proposition.

#### Making the Go/No-Go Decision

Most insurance executives considering hybrid products understand that the devil is truly in the details. Successful product innovation must take into account all factors that affect the decision of whether, when and how to proceed to market. Fortunately, recent advances in technology deliver streamlined proof-of-concept market testing capabilities.

#### Looking Forward, Looking Back

The untapped potential of hybrid life/critical illness products will be realized by those who successfully integrate life/critical illness insurance into their marketing/selling. In our opinion, the potential upsides of early market entry—especially building the foundation for ongoing increases in revenues/profits—far outweigh the risks at this time. We believe that future market leaders will look back on today's turbulence and uncertainty not only as a time of threat, but also as a time of great opportunity. ☉

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