THE WALL STREET JOURNAL.
MARCH 21, 2016

Low Rates Are Tormenting Insurers—and Their Customers; Long-term-care policies are among hardest-hit

By Leslie Scism

Life-insurance companies are scouring their policies to identify ways to raise rates and fees and lower the amount of interest they have to pay on savings products as low interest rates cut into their profits.

The bottom line for policyholders is they have to pay up or relinquish benefits.

The main culprit: the Federal Reserve's seven-year-old campaign to boost the economy. Life insurers earn much of their profit by investing customers' premiums in bonds until claims come due. They have typically favored high-quality, long-term corporate bonds to meet regulatory requirements to back their obligations with safe investments. As the Fed began driving down rates in 2008 to rescue the economy from a global meltdown, the yield on corporate bonds has tumbled.

While the Fed provided a glimmer of hope for life insurers when it raised rates in December, the benchmark yield important to insurers is now lower than it was back then, and the central bank said Wednesday it likely won't raise interest rates as swiftly as it had previously anticipated.

"We've been conducting a prolonged experiment in monetary stimulus, and the impact on savers is one of the great unintended consequences," said MetLife Inc. Chief Executive Steven Kandarian.

Life insurers' stock prices have suffered. Shares of 10 of the most prominent U.S. life insurers have lost 12% since 2008, wiping out nearly $30 billion in market value in a period when the broader market gained 40%, according to FactSet.

Blossom Blumberg, a retired New York schoolteacher, in the late 1990s purchased a long-term-care policy, a product designed to cover the cost of nursing homes, assisted-living facilities and home health care when people can't take care of themselves anymore. Then last fall the 84-year-old received a letter from the insurer, Genworth Financial Inc., informing her it was raising the cost of the policy by 60% to more than $6,000 a year.

"Nobody ever explained that the premium was dependent on how much money they made from interest rates," Ms. Blumberg said, adding: "It probably was in small print somewhere."

The Florida retiree said she couldn't afford the rate increase so she accepted an offer from Genworth to reduce the policy's future payout in exchange for maintaining the premium at about $4,000.

Insurers such as Genworth say all moves involving higher costs to existing policyholders are within contractual terms and that with long-term-care policies, regulators must approve rate increases. Genworth said it doesn't discuss specific policyholders.

Estimates of the number of customers hit with higher costs aren't available, but insurers' public statements and regulatory filings indicate rate increases and other maneuvers will cost consumers billions of dollars over time.

Long-term-care insurance is one of the products hardest hit by low interest rates, because insurers bank on investing customers' premiums for 20-plus years before claims come due. Eight million Americans own the policies, and many face annual bills that are 50% higher than before the financial crisis, according to regulatory filings and interviews with financial advisers.

Those policyholders aren't the only ones hit with higher costs as insurers pass on their pain. Many owners of "universal-life" insurance, a complicated type of coverage combining a tax-advantaged savings account with a death benefit, face unexpected bills of tens of thousands of dollars. That is because insurers credited less interest to the policies' savings accounts as interest rates fell. Many buyers intended to use built-up interest to help pay the policies' annual insurance charges as they got older.

Often in their 80s, these policyholders are struggling "to maintain their coverage just as they're ready to utilize it," said Henry Montag, a principal with TOLI Center East in Huntington Station, N.Y., which advises trusts on insurance issues. They are "in such an awkward powerless position where there are no good outcomes."

At Genworth, long a leader in sales of long-term-care policies, shares are down nearly 90% since before the crisis.

Genworth tallies its losses on long-term-care policies, many dating to the 1970s, at more than $2 billion. "We're trying to get these large premium increases...to get these policies just back to a break-even going forward," said Thomas McInerney, the company's CEO. "We're never going to recover what we've lost."

Mr. McInerney said Genworth priced many older policies on the assumption the company would earn 7.5% a year on invested premiums. But new premiums are being invested today at about 4%.

For customers with some of the oldest, most benefit-rich policies, cumulative increases are likely to be 100% to 150%, Mr. McInerney said. He said he speaks to about 50 upset customers a year and tells them: "I get it...It's awful" that they must pay more, but they still have "a fantastic deal even with the increase," given policies sold today aren't as generous as the ones they own.

In February, Standard & Poor's Ratings Services downgraded Genworth's life-insurance units to below investment grade, citing reduced profitability and other factors.

MetLife is one of many insurers that have quit selling long-term-care policies. In addition, it has trimmed benefits in some popular consumer offerings it does continue to sell. MetLife said it has been able to avoid raising costs on longtime policyholders as steeply as its older contracts permit, in part because it extensively uses derivatives to hedge risk associated with low interest rates.

In another sign of the toll of low rates, MetLife in January announced plans to divest itself of a chunk of its life-insurance operations, some of them highly rate-sensitive. One Wall Street analyst called it a "bad bank" for growth-challenged products.

U.S. life insurers are better off than some overseas peers. Moody's Investors Service says insurers in Germany, the Netherlands, Norway and Taiwan face the biggest risks. It says a key factor in vulnerability is whether insurers can "share the impact of declining interest rates with policyholders," as many U.S. ones are doing.

Still, U.S. life insurers are especially weighed down by having so much money tied up in high-quality bonds. The average portfolio yield for U.S. life insurers is down 22% since 2007, to 4.61%, according to insurance-focused ratings firm A.M. Best Co.

A.M. Best is monitoring a modest uptick in risk in life insurers' portfolios. In recent years, some insurers have boosted holdings of private-equity and hedge funds, thinly traded structured securities, private-placement bonds and unconventional investments such as wind farms and freight railcars.

Thomas Rosendale, who oversees a team of analysts at A.M. Best, notes that the next few years will be critical ones because the insurers have "pulled a lot of levers already" to maintain profitability amid low interest rates, and "they have very few levers left to pull."

Some consumers are worried more price increases are ahead.

"It's easy to go into a panic state" when notification arrives of a hike, said Jean Stern, an 80-year-old in Tucson, Ariz. The cost of MetLife long-term-care policies owned by her and her husband have jumped more than 50% since 2009, to $12,574 combined, even after they agreed to a benefit reduction. "We're too old to earn more money."

MetLife said in a statement that a price change on certain policies was necessary "due to cumulative changes in actuarial assumptions since the time these policies were initially priced."

Write to Leslie Scism at leslie.scism@wsj.com