

The Financial Crisis One Year Later



Lessons Learned

In the final months of 2008, long-simmering problems in the credit markets came to a boil and nearly brought world financial markets to complete collapse. The stock market tumbled more than 40%. Lending came to a standstill. And several “household name” financial service companies were forced to declare bankruptcy, while others needed to merge or to ask for capital from the government to remain solvent.

Fast forward to today. To judge simply by the stock and bond markets, it would appear that all has returned to normal. But you only have to glance at the headlines or talk to those around you to recognize that the crisis is far from over. The U.S. economy remains fragile, banks continue to fail at an above-average rate, unemployment is very high, and virtually every American still feels shaken by the events of the past 12-18 months.

If there is any silver lining to all of this, it’s that we learned some valuable lessons. We learned that risk can hide in unexpected places and have unexpected consequences. We learned that financial responsibility, both personal and corporate, is crucial. We learned that guarantees matter — and so does the strength of the company standing behind those guarantees.

Here are five lessons learned that are particularly important to keep in mind when choosing a life insurance company.

1 The past year has proved who the “risky drivers” are

With a few notable exceptions, most insurance companies survived the past year more or less intact. But this crisis has proved conclusively that all life insurers are not the same. In fact, the “quality gap” between the strongest and weakest companies has widened dramatically.

Just as you would want your family in a car with a proven safe driver, you should place your life insurance with a proven safe carrier — especially since the whole idea of buying insurance is to mitigate risk.

In the early months of the financial crisis, some large insurers saw their stock prices tumble by as much as 90%, putting them under tremendous pressure. Some sought and received help to bolster their capital positions in the form of government infusions of Troubled Asset Relief Program (TARP) funds, while others did not even meet the standards to qualify for such assistance.¹

But some insurers were extremely well prepared to weather the storm. And the common trait that those companies share? Mutuality.

¹ TARP was instituted by the U.S. Department of Treasury to enable the U.S. Government to strengthen financial institutions. According to FinancialStability.gov, the “Treasury’s intent is to provide immediate capital to stabilize the financial and banking system, and to support the economy.” <http://www.financialstability.gov/roadtostability/programs.htm>, 3/22/10.



Companies without public shareholders are better positioned to keep a long-term focus, enabling them to make decisions to safeguard their financial strength without considering the near-term impact on corporate earnings and, therefore, their stock price.

According to Moody's:

*"In an environment as harsh as that seen over the past year, the mutual companies — compared with their stockholder-owned peers — have displayed business and financial characteristics that have enabled them to better protect and maintain their robust creditworthiness. In Moody's view, the management, business orientation, and operational philosophies of most mutual companies serve to better insulate these companies during challenging periods such as the current one."*²

The quality difference between mutual life insurance companies and those that are publically traded is clearly evident in their financial strength ratings. Since the financial crisis began in late 2008, the financial strength rating of every publicly traded life insurer was downgraded at least once — and some multiple times.³

In contrast, every rating agency has confirmed New York Life's highest-possible ratings for financial strength.

A++ Superior A.M. Best	AAA Exceptionally Strong Fitch	Aaa Exceptional Moody's	AAA Extremely Strong Standard & Poor's
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Source: Individual third-party ratings reports. New York Life Insurance Company and NYLIAC as of 3/22/10.⁴

2 Significant risks still persist in many insurers' products and practices ...

The financial crisis has proven that some large life insurers can and do get it wrong when it comes to product features and pricing. That has had consequences.

Consider, for example, the aggressive guaranteed minimum withdrawal benefits that some companies offered on their variable annuities. These companies have come under intense pressure as interest rates have dropped. Others have been forced to limit their sales of products that require them to hold large amounts of capital.

At New York Life,⁵ our long-term focus extends to the design and pricing of our products. We will not sell a policy if we are not 100% sure we can pay the benefit, no matter what the economy brings. This has sometimes meant that we have to forgo market share to avoid risky product bets — a decision we can make because we are not owned by shareholders looking for short-term returns.

² Source: "Revenge of the Mutuals," Moody's Investor Service, August 2009.

³ "Publicly traded life insurer" refers to public life insurance companies listed in Fortune magazine's "Fortune 500" listing for 2009, Insurance: Life, Health (stock). Issue date: May 4, 2009.

⁴ Source: Individual Third Party Ratings Reports from Moody's, A.M. Best, Fitch and Standards & Poor's as of 3/22/10. New York Life ratings for financial strength: AAA from Standards & Poor's, A++ from A.M. Best, AAA from Fitch and Aaa from Moody's as of 3/22/10. The ratings for financial strength do not apply to the investment divisions of variable products, which are subject to market risk and will fluctuate in value.

⁵ "New York Life" as used throughout this document can refer either separately to the parent company, "New York Life Insurance Company (NYLIC), or collectively to the parent company and its wholly owned domestic insurance subsidiaries, including New York Life Insurance and Annuity Corporation (NYLIAC). NYLIC, a mutual company, issues whole life and term life insurance. NYLIAC, a stock company wholly owned by NYLIC, issues universal life, variable life, and fixed and variable annuity contracts. Variable life and variable annuities are offered by properly licensed Registered Representatives of NYLIFE Securities LLC (member FINRA/SIPC), a Licensed Insurance Agency.

According to Moody's:

*"Sales of products with aggressive guarantees, including variable annuities and no lapse universal life, have been heavily dominated by stock insurers, partly because of their heavy reliance on third-party distributors that demand products with attractive guarantees for marketing purposes."*⁶

We believe that the unrealistic lapse assumptions and reserving standards that continue to underlie the no-lapse guarantees on some insurers' universal life policies could well be the next shoe to drop when it comes to product risk. Investor-owned life insurance and premium-financed policies also pose significant risks.

3 ... and these risks may not become evident for many years

The implications of these risky product bets may not be felt for a decade or more. For example, New York Life estimates that the cash flow companies earn from aggressive no-lapse guarantees will begin to turn negative about 10 years after issuance, with the impact snowballing thereafter.

While those companies' executives may well have moved on before that impact is felt, where will the policyholder be when these issues come to the forefront? They will be older by a decade or more, which means they could be less healthy, less insurable, and therefore, they'll have fewer options if they need to make a change to their coverage.

4 Also be aware of the risks that remain in companies' investment portfolios

The past year has proven that it's crucial to understand how an insurance company invests its assets. What brought AIG down was not its life insurance business but rather the very risky investments it made in credit default swaps and other highly complex financial products.

While the impact of the residential sub-prime mortgage crisis on the investment portfolios of large financial institutions has largely been played out, the questionable underwriting and aggressive investing of the past decade still has many other implications that are still emerging:

- Bad credit card debt and auto loans are only now being recognized.
- Credit losses in the commercial real estate and leveraged buyout sectors are widely expected to be the next big trouble spots for corporate investment portfolios.

New York Life continues to maintain a prudent investment philosophy that includes these core tenets:

Diversification. We maintain among the most diversified portfolios in the industry, refusing to take an outsized stake in any single investment, no matter how attractive it may appear.

Fundamental research. We do not rely on ratings but rather do "bottom-up" research in every sector, which historically has resulted in credit losses that are significantly below the market average.

⁶ Source: "Revenge of the Mutuals," Moody's Investor Service, August 2009.



Liquidity. Because we recognize that claims must be paid in cash, we always maintain a healthy level of liquidity.

5 Now, more than ever, New York Life is built for times like these

When New York Life coined the phrase "built for times like these" in the early days of the financial crisis, it was not clear how long "times like these" would last. It still isn't. More than a year later, the economy remains fragile, and many corporations (including many financial institutions) continue to struggle.

But the proof continues to mount that we are, indeed, built for times like these — and all the other good and bad times that lie ahead: Amid an industry in which sales were down 15% in 2009⁷, New York Life enjoyed double-digit sales gains. And *Fortune* magazine recognized us as the World's Most Admired Life Insurance Company.⁸

The factors that set New York Life apart are clear:

- Our mutuality allows us to maintain a long-term perspective and keeps us uniquely aligned with our policyholders.
- Our industry-leading financial strength and prudent investment philosophy ensure we'll be able to fulfill the promises we make.
- We don't take unnecessary risks.
- And our Agents — who undergo an intensive three-year training program, followed by career-long learning opportunities — are there to help clients navigate an uncertain world.

For all these reasons and more, our policyholders enjoy the peace of mind of knowing they have protected what matters most, regardless of the economic climate. That's why, today and far into the future, New York Life is *The Company You Keep*[®].

⁷ Source: "LIMRA: Life Insurance Sales Drop 15% in 2009," InsuranceNewsNet.com, March 22, 2010.

⁸ Source: "The World's Most Admired Companies" survey, *Fortune*, March 22, 2010, p. 121.

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