



Global Concerns During an Influenza Pandemic

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Bird flu and a potential human influenza pandemic have received top billing in the popular press of late, but what do they mean for the global insurance industry? National health care plans and insurers have more to think about than just the obvious increase in claims. From a public policy perspective, these groups are aligned with the general population. Reducing morbidity and mortality, proactively preparing for a pandemic, and the side benefits of that preparation will benefit everyone. The best plans will be flexible and adjust as the pandemic develops. Leading this advance planning will also help the insurance industry build goodwill with the general public.

Background

During a global pandemic, large numbers of people will get sick, and some will die. In 1918 it is estimated that 30 percent of the US population became sick and 0.6 percent died. With a mortality rate much higher in developing countries, total global estimates range as high as 100 million deaths caused by the worst influenza pandemic in recorded history. For the US, given today's population of about 300 million, a similar event would correspond to 2 million dead and nearly 100 million sick over a very short period of time. In addition, during the 12-18 months that it is expected to take for an influenza pandemic to work through several waves of virus mutations, there will be other catastrophic events. Earthquakes, hurricanes, tornados and tsunamis, will continue to occur. Those countries unlucky enough to suffer a double hit that includes influenza will find very little help available during their time of severe need as supply chains are shut down and travel is dramatically reduced.

Seasonal flu primarily infects those individuals with weakened immune systems, mainly the elderly. In contrast, during the 1918 pandemic, those aged 15-40 experienced high mortality rates as their strong immune systems turned against their bodies. Pregnant women were especially vulnerable. The elderly, surprisingly, were spared. A future pandemic that impacts the elderly, as well as those young and strong, would magnify the impact beyond that experienced in 1918.

There are four broad planning issues for insurance companies to consider:

- Business continuity risk — how will insurers meet customer needs?
- Economic risk — what is the impact on insurers' assets?
- Insurance risk — could increased mortality and morbidity affect solvency?
- Counterparty risk — will reinsurers be able to meet their obligations?

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Business Continuity Risk

How will an insurer meet customer needs? During a time when the health system will be overloaded and claims will spike, many employees will also be sick or fulfilling family responsibilities. Field offices will be crippled as companies withdraw temporarily from markets. Schools, day care facilities, places of worship, and malls will all be closed. Employees will need options to balance these additional responsibilities. Telecommuting and split shifts will be among the social-distancing methods utilized. Vendors and other suppliers should be included in these contingency plans to maintain the supply chain for as long as possible. Insurers should also participate in their community planning exercises. A region can materially reduce the impact of a pandemic by working with their local health authorities to strategically send home employees, reducing contact rates and keeping the virus from tipping into a pandemic. Pay policies should be determined in advance for time off, whether voluntary or mandatory. Much as Y2K provided an opportunity to update company technology, a potential pandemic can provide side benefits by driving insurers to improve their Internet and automatic phone-driven systems for customers.

A pandemic has a much different impact on a company than does the loss of a building. Plans should start with previously developed contingency plans, but many issues will not have been previously considered.

Economic Risk

Few companies in any sector will thrive during an influenza pandemic. One realistic scenario has manufacturers of cleaning products and masks among the few economic winners. Reduced demand, along with supply chain breakdowns, is expected to lead to a global recession. Customers will not be able to rely on suppliers located halfway around the world. Food, medicine, oil, and water will be scarce. Providers of infrastructure like electricity and natural gas will find key parts impossible to acquire. Unlike natural disasters, such as earthquakes and hurricanes, that provide a natural boost to the economy through rebuilding, the economy is unlikely to rebound quickly. A recession will lead to unrealized losses on assets just as claims rise, although this is likely to be offset by higher bond prices driven by lower rates. This will lead to a potential cash crunch for insurers, with many taking losses on assets to generate cash to pay claims. It remains unclear who will be in position during a pandemic to purchase these assets. Insurers should create stress scenarios that predict the financial impact of this and other risks.

Insurance Risk

Higher than expected claims is the obvious risk for insurers during an influenza pandemic. Term life product lines are especially vulnerable since premium rates assume few deaths. Health insurance forms vary by country, but policies that do not depend on receiving treatment to pay will have additional claims. Health care systems may actually experience reduced expenses if understaffed facilities run out of supplies to care for the sick. If the virus impacts all age groups, including the elderly, then payout annuities will provide an internal financial hedge for insurers and state run pension systems. Accumulation products will also provide a buffer, since the assets back all general account products and would be available to meet cash flow needs. Annuities providing a wrapper around equities and guaranteeing values at death will provide an interesting case study, as fund values drop and mortality rates rise within a short period of time. Residual morbidity is unknown, but, following the 1918 pandemic, neurological, lung and heart ailments all appeared to increase.

Counterparty Risk

While insurers writing business directly to groups and individuals need to create economic scenario plans to show how they would address a range of potential outcomes, they often have offsetting liabilities and excess capital. Reinsurers rely on having exposure to a large number of insured lives so that their mortality results are close to the expected levels. This allows them to minimize required surplus funds and to maximize their returns. Reinsurer claims will be dramatically higher than expected during a pandemic, and they will be susceptible to insolvency. Direct carriers should expect to be shown the economic scenario plans of reinsurers.

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Summary

There will be influenza pandemics in the future. No one knows when they will occur or how severe they will be. What is clear is that not everyone will receive the desired level of health care and that it will have to be rationed during a pandemic. The health system cannot support the total level of care needed, from beds to ventilators. Who gets to make these life-determining decisions? Will someone be required to pay for unreceived health care? Who will it be?

The insurance industry has built its reputation by providing service during times of need to individuals all over the world. By providing good service during the severe stress of a pandemic, this reputation will be enhanced. Not providing service will destroy years of built-up goodwill and brand development.

Individuals should keep redundant supplies of food, water, cleaning supplies, and medicines at home. A radio that runs via crank power provides assurance that your family will maintain contact with the outside world. In our "just-in-time" global economy, all companies should keep extras of critical parts necessary to provide basic services like heat and electricity. Hospitals and clinics should maintain stores of extra supplies. Chemotherapy patients and pregnant women should have backup plans if hospitals are overloaded.

What's good for humanity is also good for the insurance industry. Proactively making the public aware of common-sense activities, like washing hands, limiting contacts, and checking in on others in your community, saves lives. Honest communication and flexible plans are the keys.

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