

.....CPS BULLETIN.....

The Newsletter of CPS Actuaries and Computer Programming & Systems, Inc.

Volume 3, Issue 3

December, 2002

Introduction

All of us at CPS wish you a happy, healthy and prosperous new year.

This issue of **CPS Bulletin** begins with an article about ways you can speed up your computer. While the cost to purchase a new computer has dropped considerably in recent years, purchasing a new computer may not always be the best option – your current computer may be good enough. This article provides some ideas on how to improve the performance of your current computer.

As available yields on investments have continued to decline in recent months, our second article looks at the impact low interest rates have on fraternal benefit societies and some suggestions to help cope with such low yields. While low rates are great for people that want to get a mortgage, they are not as good for the finances of fraternalists.

CPS is working on a number of new projects, including developing a new administration software system and illustration software. We are also expanding our computer networking consulting services. Please let us know if you are interested in any of our services. ❖

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Is There a New Computer in Your Future?

Many computers are now being sold at very economical prices – as low as \$400 for a well-known maker's machine or even lower if one opts for a no-name brand. If you purchased your machine a couple of years ago and are finding that current or new applications are demanding more than your present machine possesses, you may be asking whether it is worth retiring the computer or whether there are ways to improve its performance.

While a new computer is an attractive idea, it will require effort to set up, assuming you wish to transfer the applications and data from your current machine to the new computer.

To transfer data you will either have to use a specialized program such as Alohabob (discussed in our Newsletter of September 2000) or, if you have access to a network, you may be able to transfer the data from the current computer to the network and then to the new computer. Since applications may not transfer as well as data, you may need your old program set-up CDs or diskettes and will have to go through the set-up process again if these programs were not already installed on your new computer.

An alternative to purchasing a new computer would be to first try to clean up your old machine to see if it can give you more "oomph". The first thing you can try is to use your computer's Disk Defragmenter in order to clean up files and bits of data scattered around your hard drive. To "defrag" you would click the Start button, select run and type defrag in the box. Beware that this can take many hours to complete but it does help to speed up your computer if all of the files are cleaned up on your hard drive.

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Another item to check is to see which programs are running in the background while you are using your applications. You may have loaded some new software and unbeknownst to you the software has loaded, for example, a complimentary copy of AOL onto your computer and inadvertently AOL's Instant Messenger may have started running in the background. Alternatively, if you downloaded QuickTime it may have attached itself to the computer start-up menu so that it activates each time the computer is booted-up. You may find that by shutting down these non-essential programs your computer speed increases measurably. The way to see what is running is to press the CTRL ALT DEL keys simultaneously. A box will appear that shows the programs that are running. You can use the facility provided to shut down the unwanted programs. To make sure that they do not start up again when you reboot your computer may not be as simple and expert advice is recommended.

Extraneous programs (adware or spyware) may also exist on your computer. These programs attached themselves to your computer at web sites you visited. A free utility such as Lavasoft (www.lavasoft.com) can detect and remove such programs.

If you are online a lot and your online speed is the problem, computer speed alone is unlikely to help significantly. However, switching to DSL or Cable is likely to substantially speed up your surfing.

If, after trying out these ideas you are still dissatisfied with your computer's performance, you may obtain a substantial speed increase by adding memory or acquiring a larger and faster hard drive. Increased memory will help with multitasking even if you already have 128 Megabytes (MB) of RAM. This is because, while working, your computer swaps data and software between your hard drive and memory, and more memory will reduce the need for this swapping (which is the slowest part of processing). In order to add memory you must determine from the computer manual the slots you have available for additional memory. Two leading memory vendors are www.crucial.com and www.kingston.com. Prices typically are under \$60 for 128 MB and under \$100 for 256 MB. This is a relatively simple process that many computer users can do for themselves.

Since the objective of an upgrade is to avoid reinstalling your programs and data, you ordinarily will not wish to replace your hard drive. Instead you can add another hard drive, which will then become the subsidiary drive (technically the "slave" drive). An advantage of this arrangement is that you can easily back-up all your data on the slave drive and if the unthinkable happens and the master drive crashes you have an instant backup! Installing an additional hard drive is best done in conjunction with a professional.

The last item you may wish to change for extra performance is the Central Processing Unit (CPU), especially if your current speed is above 300 MHz. If you find that the computer is so old that the CPU speed is below 200 MHz, you may find, like the writer of this article that the motherboard may be of a vintage that does not allow for a change of CPU. This process is best done by a professional, who may then tell you that you also require an extra heat sink or fan to cope with the heat generated by a new CPU. All in all, if you are down to getting a new CPU you may be better off purchasing a brand new computer.

The benefits of a new computer are that you can have all sorts of additional toys to play with. Some of the most worthwhile are

- A CD-RW drive to facilitate back-ups, burn CDs and to download music from the Internet.
- A DVD-RW drive to play DVDs and record them. For example you will soon wish to transfer your worn out videotapes onto DVD for more secure storage.
- An enhanced video card for more vivid graphics.
- A network card is now automatically included in virtually all computers to enable sharing facilities such as data and printers with any other computer you may have or will acquire.
- Digital music and photography software.

In conclusion, before you run out and buy a new computer, you may wish to consider our suggestions to bring your current computer "up-to-speed".

If you would like further information about transforming your computer, the experts at CPS will be pleased to assist you.

Low Interest Rates: Good or Bad for Fraternal?

Regulators, particularly the New York Insurance Department, have recently been concerned with the effect of the current low interest rate environment on fraternal benefit societies. Appointed actuaries have been asked to opine on these effects when submitting the annual statement. Why is this issue so important to the insurance departments when no such submissions were required during the high interest rate environment? This article attempts to answer this question.

Let us initially consider the effect low interest rates have on the annual statement. Low interest rates will have their biggest effect on the asset side of the balance sheet. When interest rates are low, the market value of bonds is usually high. However, since the statement value of bonds is an amortized value, the increased market value of your bond portfolio has little impact on the annual statement.

On the other hand, reinvestment of assets and investment income will now take place at low interest rates so that the future income from current and future investments is not as advantageous. Also, corporations with good credit ratings are able to raise money at lower rates than in the past, thus inviting them to call in any bonds that are callable and replacing them with bonds paying a lower interest rate. Since many fraternal rely heavily on the investment income on their surplus to fund many of their fraternal programs, a decrease in these earnings will have a major impact on the society's finances.

As an example of reinvestment problems, the lack of attractive yields on new bond purchases have caused some societies to see an increase in their cash assets. The yields on cash have been around 1% - 2%. If these funds are not reinvested, this can be a costly mistake especially if rates remain at these low levels for a number of years.

Low interest rates will likely have a marginally beneficial effect on the Interest Maintenance Reserve (IMR) since gains achieved on bonds sold or called before their scheduled maturity date will be amortized at a lower interest rate. This allows for an acceleration of recognizing realized gains.

Low interest rates will also impact deferred annuity business. All societies must have a guaranteed interest rate in their annuity contracts. Some guaranteed rates are as high as 4½% or 5%, which looked pretty safe in previous decades but now look rather significant. Many companies have lowered the guaranteed rate on new business to 3%. It is very difficult to find matching or immunizing investments (see our April 2002 and October 2002 Newsletters) for this business because the term during which the investment will remain with the society is unknown and is at the option of the annuitant. A number of societies have continued to credit high rates on their annuities. First year yields of 6% or more are not uncommon and it is difficult to find first class investments yielding 7% or more to ensure that the society has a reasonable profit margin. Although some societies are earning in excess of 7% on their portfolio, this rate relies on high yield investments made in the past, leading to a subsidy of new entrants by existing members. While it may be reasonable for surplus to be so used for a period of time, if the low rate environment continues this situation will have to be monitored very closely.

A third effect of low interest rates is how they impact the liabilities. Fortunately there is a reduced likelihood of the valuation interest rate dropping to 4% for 2004. This is because the yield differential between corporates and treasuries has widened significantly. The Moody's index on which the valuation interest rate is based was in fact 6.87% for September, 7.08% for October and 7.01% for November – way in excess of the 6.2% 12-month average required for a change.

However, when interest rates are low, features such as conversion options and riders become more valuable. Also, when the economy is in the doldrums, there is a tendency for disability claims to spike so that disability and similar options may become more severe. Finally lapses and surrenders may also grow, leading to larger immediate cash outgo.

What is a society to do?

- Monitor amounts held in low-yielding cash assets and reinvest funds in a timely manner.
- Reduce the guaranteed rates on all future annuities to 3% - the minimum currently allowed by law.

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- Reduce the rates payable on deferred annuities to levels at which the society can still make a profit. Many larger companies have already reduced their rates. As an example, the rate currently offered by TIAA-CREF (the largest annuity issuer in the U.S.) is only 4.1% (reduced from 4.7% as of October 1 of this year).
- Review or perform cash flow projections and use them to optimize your investment strategy in the near term. For example, you should project your cash requirements for 2003 and keep as little as possible in low yielding cash. It is not necessary to ensure that the society has enough cash to meet every contingency – just the expected outgo; a society could always arrange access to a credit line through their broker if the unusual were to occur.
- Implement the matching strategy advocated in our prior newsletters bearing in mind the advantages of fraternal benefit societies discussed therein.
- Review premium rates for life plans and consider increasing them especially for smaller face amounts where expenses bite most sharply.

While it is impossible to forecast how long current conditions will continue, with effective management, fraternal benefit societies should be able to ride out this low interest rate environment and learn from these tribulations how to better manage their organizations.

About CPS

CPS Actuaries and Computer Programming & Systems, Inc.
CPS is an independent company with over 35 years of service to our clients. We offer a wide range of computer and actuarial services. For information regarding our services, please call us at **203-324-9203**, or visit our web site at www.cpsincorp.com. ❖

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Regulation Update

In this section we usually inform you about progress on various regulatory issues. As we get ready for year-end, we decided that for this issue we would instead provide links to web sites that can help you find information easily.

- State Insurance Department Web Sites
The easiest way to find a particular state's web site is to go to the NAIC's web site (www.naic.org), select *State Insurance Regulators*, then *Map of Insurance Regulators* (or type www.naic.org/1regulator/usamap.htm in your browser) and you will see a map. Select a state on the map and you'll be taken to that state's web site.
- State Filing Instructions
The NAIC web site also indicates how you can find each state's year-end filing requirements (including the checklists) once you've accessed the state's home page. From the NAIC home page, select *State Filing Instructions* under the *Filing Instructions* header to find the explanations.
- State Laws and Regulations
One of the easiest ways to find the laws of any state is to go to the Find Law web site (www.findlaw.com). Some of the states have their regulations on-line and they can be found through this site also. From the Find Law home page, select *States* under the *Laws: Cases and Codes* heading, and then select the state you want to find information about.

Interest Rate Monitor

The following are some key interest rate benchmarks:

<i>Benchmark</i>	<i>Current</i>	<i>3 Months Ago</i>	<i>1 Year Ago</i>
Fed Funds	0.75%	1.81%	2.00%
Prime Rate	4.25%	4.75%	4.75%
30 yr mortg	5.62%	5.76%	6.70%

Source: www.bloomberg.com as of 12/25/2002