The Sage of Omaha Says GLWBs Were “Crazy”

By Editor Test *Sun, Jun 7, 2009*

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Billionaire investor Warren Buffett has criticized some life insurers for taking on “crazy” financial risks by selling variable annuities, or retirement products that promised unrealistic guarantees to buyers, Reuters reported.

“I always thought they were crazy when they were doing it,” said Buffett, at a press conference in Omaha, his hometown, because of the financial risks to the insurer. The products are tied to stock market performance and in some cases guaranteed a certain periodic return, while principal could not be eroded by investment losses.

Insurers such as The Hartford and Genworth Financial have been badly burned by over-selling these products, which performed badly as the credit crisis sent markets plummeting. Buffett, chairman and CEO of Berkshire Hathaway, is said to be the world’s best investor.

Roger Lowenstein, one of Buffett’s biographers, wrote that the Sage of Omaha was invested mainly in cash when the 1974-1975 bear market struck, and bought a slew of Fortune 500 company stock at historic discounts.

Of the variable annuity living benefits, Buffett said: “If you buy a policy, you the policyholder get some of the upside, and [the insurers] guarantee you always get your premium back.” From a company’s perspective, “that’s poison.” Life insurers have also lost money on investments securities linked to commercial mortgages, he added.

Berkshire was asked to reinsure variable annuity guarantees, and declined, Buffett said. “Life companies had those two temptations, one on the asset side, one on the liability side, and those that succumbed are in real trouble.”

The Dow Jones U.S. Life Insurance Index (DJUSIL) has fallen nearly 65% since the beginning of 2008, as investment losses, declining revenues from asset-based fees, and rising costs to hedge variable annuity guarantees have decimated many insurers’ profits.

But Buffett predicted the government would assist any major life insurer that was in danger of collapse. The government has already offered Troubled Assets Relief Program (TARP) funds to some U.S. life insurers. Of those offered TARP money, Allstate Corp., has declined it. Prudential said May 15 that it had not yet made a decision.