Taking Stock: When policyholders lose, insurers win

by Malcolm_Berko

Dear Mr. Berko: I need to purchase long-term care insurance for and my wife and myself. We are considering a Conseco policy because the salesperson appears very knowledgeable and the price and coverage seems fair. We've also looked at Genworth Financial but the price is higher. We're impressed with the Conseco person who told us that he owns 250 shares of Conseco and we like the fact that this person owns stock in the company he works for. We will purchase the Conseco policy and we'd also like to buy 300 shares of the stock. What can you tell us about the company and do you think it would be a good investment?

M.R.

Fort Walton Beach, Fla.

Dear M.R.: Conseco Inc. (CNO-$20.16) and its subsidiaries Bankers Life and Casualty and Colonial Penn Life have been writing health insurance, life insurance, annuities, Medicare supplemental policies and cancer policies for almost three decades. And CNO did reasonably well with over $5 billion in annual revenues before collapsing under a mountain of debt and declaring Chapter 11 in late 2002. CNO came out of bankruptcy a year later and is now profitable with expected 2007 revenues of $4.6 billion and projected earnings of $1.54 a share.

Revenue growth since emerging from bankruptcy has been poky, growing less than 1 percent per year. Earnings have been just as dawdling and are lower today than they were in the last few years. Net profit margins are a dinky 2.16 percent, return on equity is a blushing 1.48 percent, the shares trade at 11 times earnings and the debt/equity ratio is just 0.30. However, it is interesting to note that CNO's book value is $31 and CNO shares trade at 70 percent of book. One might suggest that the low share price to book value is an indication of the low esteem in which investors hold the company and its management.

Most of us remember a dozen years ago when health insurance companies purposefully and methodically denied coverage to policyholders for even mundane procedures. And while denying coverage to policyholders they also short-sheeted doctors and hospitals. Those health insurers had a virtual monopoly to print money; they made it hand over fist because huge dollops of lobbyists' dollars guaranteed that state and congressional regulators looked the other way!

Well it seems that CNO has taken a page from the playbook of the mid-1990s. The bottom line is that insurance companies make big bucks when they don't pay claims. According to Mary Beth Senkewicz, who last year resigned as head of the National Association of Insurance Commissioners, "they'll do anything to avoid paying, because if they wait long enough, they know the policyholders will die."

CNO is going to make a bundle of money this year because its management has become expert in denying long-term health-care claims. The volume of complaints against Conseco exceeds by orders of magnitude those of other long-term care insurers. The complaints against Conseco are legion and the resolutions are running 100 percent for Conseco vs. zero for the policyholders. Conseco is turning its "denied claims department" into a profit center. These concerns are ignored by state regulators (some say they are paid to be ignored) and lawmakers.

I'd buy CNO because potential earnings (thanks to superb claims denial) could rise above $2 a share from projected 2007 earnings of $1.54. That 30 percent increase in earnings is anticipated even with flat revenue growth for next year. So with price-earnings ratio of 11, CNO should trade at the $22 to $23 level, which is also a 30 percent increase in share price.

There are four analysts on the Street who closely follow CNO and two of them rate the stock a "strong buy," while two suggest a "hold." And would it surprise you if the two analysts with a "strong buy" were employed by brokerages that had an important advisory relationship with CNO?

So go ahead and buy 300 shares. But hells-bells my friend, Pious Sam wouldn't recommend buying a long-term care policy from CNO. "To be certain of your coverage," says Pious Sam: "it's best to buy long-term care insurance protection from the big, well-known, companies like Met Life, Genworth Financial, Lincoln, Travelers, etc."

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