GCU

Entity: GCU			
Affirmed	**Type**	**Rating**	**Outlook**
GCU	IFSR	BBB+	Positive

Methodology:

Global Insurer & Insurance Holding Company Rating Methodology

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Rating Summary:

The rating and positive outlook reflect the continued favorable trends in the society's surplus and overall capital base, underpinned by its consistent profitability trends. GCU possesses a solid balance sheet and a stable membership base, which is moving in a positive direction relative to its peers. In a challenging interest rate and investment environment, GCU has successfully demonstrated its ability to adjust credited rates to maintain healthy margins through year-end 2020. KBRA continues to view favorably the recent steps the society has taken to improve its corporate governance, investment management and enterprise risk management practices. Lastly, GCU has implemented its new, transformational administrative systems consolidation project which should create longer-term operational efficiencies, enhance the user experience for members and agents, as well as improve ease of business and analytics capabilities.

GCU is the 7th largest fraternal benefit society (based on net admitted assets as of mid-2020) and remains committed to writing annuity and life insurance products. Expanding its life writings is a strategic push for GCU as the company launched a final expense product towards the end of 2020. Annuity writings should be further bolstered by the anticipated launch of a fixed indexed annuity product in the first half of 2021. Although the organization experienced some adversity during the 2009 financial crisis, the society has broadened and refined its product offerings, accumulated surplus, and repositioned the company for profitability and growth. Since year-end 2010, GCU's reported surplus has achieved a compound annual growth rate of roughly 24%, and total admitted assets exceeded $2.2 billion at year-end 2020. In addition, the society maintains a low operating expense profile which is well below industry averages. Moreover, GCU has sound liquidity and good financial flexibility with no leverage and access to low-cost funds through its membership in the Federal Home Loan Bank of Pittsburgh.

Balancing these strengths are GCU's noteworthy exposure to spread compression within its legacy annuity block due to high minimum guaranteed crediting rates. Although manageable, the society's investment portfolio has notable exposure to reinvestment and credit risk in its longer maturity bonds. The society also faces challenges related to expanding its geographic reach and diversifying its business mix to sell more life insurance. GCU's business mix remains relatively concentrated as reserves are almost entirely interest-sensitive.

Outlook

The Positive Outlook reflects KBRA's expectation that GCU will continue to preserve, and improve upon, its current capitalization through continued operating profitability, grow its life insurance business, maintain sound investment portfolio credit quality, avoid significant spread compression through active management of credited rates, retain key members of its management team and successfully launch its fixed indexed annuity product.

Key Credit Considerations	+/−
Continued Growth in Capital Base and Profitability Strong capitalization growth and highly favorable trends in total adjusted capital (TAC). TAC is projected to grow to $191 million at year-end 2020, reflecting almost a 550+% increase since 2010. CAL RBC has settled in the 350-400% range. A CAL RBC of 350% is projected for 2020. The company has recorded over $130 million of net gains from operations for the 2015-2019 period.	+

Expanding Membership Well-established fraternal with roughly 47,400 members, representing a 17% increase from 2010. Most fraternals are experiencing membership declines, so GCU is moving in a positive direction relative to its peers.	+
Strategic Diversification Efforts Explicitly targeting a diversification of its business; plans to grow its life insurance portfolio, optimize distribution, and target new geographies. Estimated life premiums in 2020 ($5.6 million) were up nearly 65% from 2019, although remain just over 2% of total premium writings.	+
Potential for Spread Compression Annuity block susceptible to spread compression (as of 3Q 2020, 63% of annuity reserves are held in products with a guaranteed rate of 3.0% or higher) and disintermediation (69% of annuity reserves have no or minimal surrender charge). However, above-average investment yield, 5.4% in 2019, while maintaining a generally good quality invested asset portfolio (95% of the portfolio is in fixed income securities with 95% held in NAIC 1 or 2 rated bonds) are mitigants.	–
Exposure to Reinvestment Risk Notable exposure to reinvestment risk given product portfolio and required yield to meet guaranteed rates in the annuity block. However, target spreads are still being achieved as the society actively manages credited rates across product offerings and refines asset reallocations to maximize yield.	–
Lack of Business Diversification Business mix lacks true diversification as reserves are almost entirely interest-sensitive (between 95% and 96% as measured at YE 2015-2019).	–

Rating Sensitivities	
▪ Sustained earnings, continued favorable capital trends, stable membership, growth in life insurance sales, maintenance of above-average investment performance without compromising credit quality, and successful launch of its fixed indexed annuity product which materializes in growth without undue negative impacts on surplus.	+
▪ Change in risk profile, decline in earnings, material investment losses, lack of credited rates discipline, failure to execute upon business plans, and/or departure of key members of the management team.	–

ESG Considerations

KBRA's ratings incorporate all material credit factors including those that relate to Environmental, Social and Governance (ESG) factors. Throughout every analysis, KBRA captures the impact of ESG factors in the same manner as all other credit-relevant factors. More information on ESG Considerations for the Insurance sector can be found **here**.

ESG factors did not have an impact on this rating analysis.

Recent Developments

Financials and Operations

GCU continues to remain profitable and bolster its surplus. Through 3Q 2020, GCU's balance sheet continued to strengthen compared with the same period a year prior. Total assets at year-end 2020 are expected to exceed $2.2 billion. Assets are expected to grow by $150 to $200 million annually. NAIC RBC (CAL) for 2019 was 363%. RBC (CAL) for 2020 is estimated to be 350%, which meets GCU's target for this metric.

Net gains from operations projected at year-end 2020 ($29.7 million) are down 6.1% from 2019, primarily reflecting increased annuity benefits paid. However, net income at year-end 2020 is projected to be $12.9 million, a nearly 53% decline from 2019 which reflects primarily the write down of OTTI credits in the amount of approximately $16 million coupled with the challenging business environment in 2020 in the wake of COVID-19 pandemic.

Both life and annuity premiums for 2020 were down compared to budget, which GCU primarily attributes to the pandemic, but favorable compared to 2019. Life premiums of $5.5 million increased 62% year over year. GCU also launched a final expense product in the fourth quarter of 2020. Annuity premiums of $215 million increased 1.1% year over year.

GCU plans for continued, sustained, and disciplined growth of annuity sales in the coming year, especially with the development and introduction of its fixed indexed annuity product. The product is anticipated to launch in the second quarter of 2021. GCU will continue to focus its effort on the distribution of its life products and the recruitment of more IMO's.

In late 2020, GCU completed the strategic roll-out and implementation of its new, modern policy administration system which will offer an enhanced digital experience and support GCU's overall efforts towards efficiency and automation over the long term.

Active rate management by GCU resulted in average crediting rates which trended downward in 2020. Full year 2020 average crediting rates were 3.16%, down 29 basis points from 2019. Average spreads earned by GCU in 2020 (1.97%) were down 7 basis points.

Investments

GCU remains primarily invested (95%) in fixed income corporate securities ($2.2 billion invested assets as of 3Q 2020). Its investment guidelines are reviewed annually. Allocation shifts and diversification on the margins for 2020 include alternative assets, private credit and equity funds. GCU plans to increase allocations to alternative assets from $30 million (currently 1.4% of assets; limited to 2.5%) to $60 million through 2022. Further, $10 million (less than 1% of assets; limited to 1%) was invested in a low volatility/high quality public equity strategy. Net investment income for 2020 is estimated to be $103.4 million, an increase of 1% year over year.

COVID-19 Pandemic

The COVID-19 pandemic had a minimal impact on operations. The majority of staff transitioned seamlessly to a work from home environment and operations continue to function normally. There is a small number of essential staff which maintained an office presence. The pandemic did have a meaningful impact on new business as both life and annuity premiums for 2020 were significantly under budget. At the onset on the pandemic, GCU's actuary performed a generic pandemic shock analysis on GCU's life portfolio which elevated claim volume activity by as high as 20 times (nominally, an 1,543% increase of claims paid from 2019 amount of $2.6 million). This scenario had a modest pro forma effect on GCU's RBC ratio and surplus (RBC ratio decreased 55 points and surplus decreased $30 million in this severe scenario). However, a material increase in claims experience did not occur. Projected life claims for 2020 of $2.6 million increased 22% from a year prior but remained under budget.

Background and Organizational Structure

GCU is a Pennsylvania-domiciled, fraternal benefit society founded over 125 years ago.

The society is licensed in 31 states and Washington D.C. to sell a full range of annuity and life insurance products to meet its members' financial needs. In addition to annuities and life policies, the society also sold Medicare supplement products. However, as of January 1, 2020, GCU ceased sales of Medicare supplement products; hence, the business is now a closed block. Currently, the society has roughly 47,400 members nationwide with over 75,000 active policies. The majority of GCU's business is generated from Pennsylvania (40% of direct written premiums/deposits through 3Q 2020) and Wisconsin (10%).

GCU has roughly 1,200 independent general agents selling and marketing its products. These agents are located primarily in Pennsylvania, Wisconsin, Ohio, Minnesota, California, Michigan, Illinois, Indiana, Arizona and Florida.

Corporate Governance

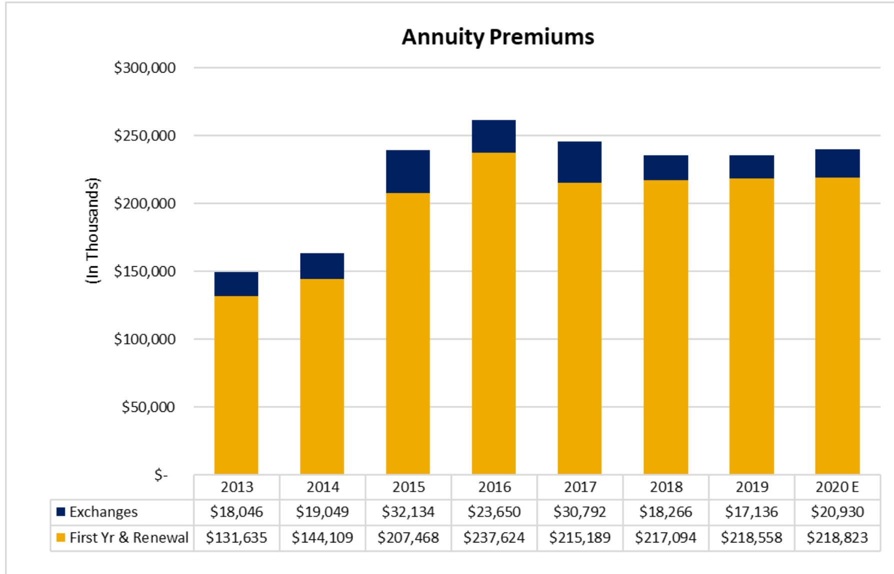
Historically, the society's supreme legislative and judicial authority was the national convention which was held every four years. Revised bylaws for the society that eliminated the national convention and made the board of directors the absolute governing body and ultimate decision maker became effective in November 2018. In addition to reducing corporate expenses, this move fosters greater accountability and flexibility across the organization. KBRA views this as a credit positive, as the supreme council system that is common in many fraternals frequently hinders management and fosters an expensive and inefficient decision-making process.

GCU's board of directors has 11 members. The society's bylaws grant the board authority to appoint up to 4 benefit members to serve as voting directors for a term to be determined by the elected directors. The elected directors each have 4-year terms; all board positions were up for reelection in 2020.

Product Overview

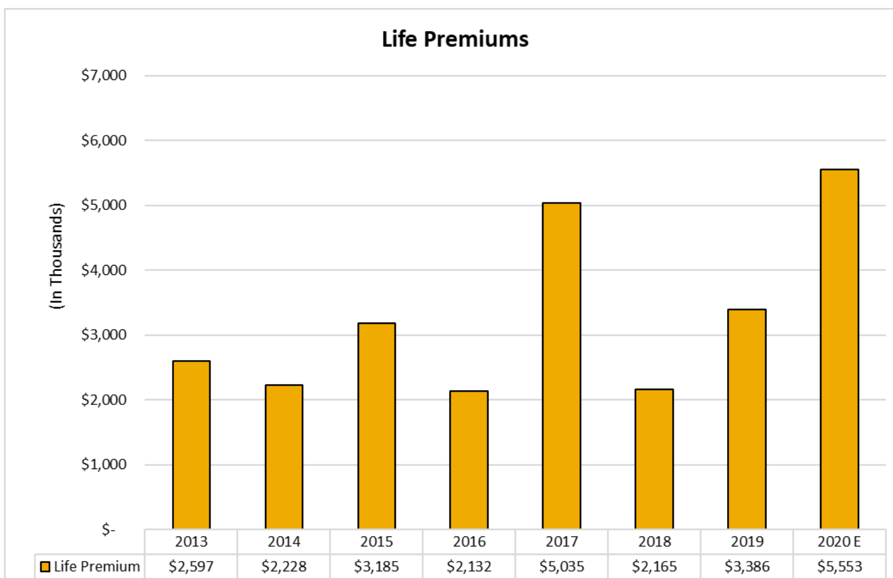
GCU offers fixed annuities and life insurance, whole life and term, actively in 26 states.

GCU's primary offering is deferred and immediate annuities. GCU does not offer variable annuity products. GCU plans to launch an indexed annuity product in the first half of 2021.



Consistent with many fraternals, the guaranteed minimum interest rates (and credited rates) on GCU's annuity offerings have been higher than those of commercial carriers' products. Current spreads on the society's annuity products remain in the range of 150-200 basis points across the various offerings but have declined from 2019 levels. This is primarily attributed to lower investment yields. Throughout 2008 to 2012, GCU underwent a product transition; in doing so, the society began to remove its longer duration and higher minimum guaranteed rate products in favor of a newer suite of products. GCU projects continued growth across its annuity products. Through 2020, the society generated $219 million in first year/renewals and processed roughly $20 million in conversions.

GCU's life insurance offerings include both whole life and term products. The life products have recently been repriced, with pricing assumptions and product specifications developed by Allen Bailey & Associates, to incorporate the 2017 CSO mortality tables. GCU projects considerable growth in this line of business due to the society's recent introduction of a final expense life insurance product.



In 2015, GCU commenced selling Medicare supplement products supported by a quota share reinsurance contract with Aetna Life Insurance Company (Aetna). The society retains a small exposure (5%) of claims and expenses and the rest is assumed by Aetna. The society historically offered these products to meet member needs and further enhance the fraternal relationship. The product was underwritten and manufactured by Aetna, including guidelines and pricing. As of January 1, 2020, GCU placed this line of business into runoff. The closed block will take several years to run off; results from the Medicare supplement product line are immaterial for GCU.

KBRA KROLL BOND RATING AGENCY

Insurance Entity Financials

GCU	3Q 2020	2019	2018	2017	2016	2015
BALANCE SHEET						
Total Admitted Assets	2,166,526,579	2,052,334,084	1,890,844,697	1,712,285,488	1,549,960,643	1,354,927,436
Surplus	174,597,665	162,741,532	154,269,000	133,042,421	108,531,975	90,739,736
Asset Valuation Reserve (AVR)	6,290,461	18,746,796	19,311,098	18,662,238	17,556,902	13,217,553
Total Adjusted Capital (TAC)	180,888,126	181,488,328	173,580,098	151,704,659	126,088,877	103,957,289
Chg in TAC from Prior Period	NA	4.6%	14.4%	20.3%	21.3%	24.5%
Surplus to Liabilities (excl. Separate Accts)	8.8%	8.6%	8.9%	8.4%	7.5%	7.2%
NAIC RBC (CAL)	NA	363%	379%	390%	277%	380%
BIG Bonds/TAC	51.9%	37.3%	56.8%	74.1%	160.5%	76.4%
High-Risk Assets/TAC	104.5%	80.0%	102.8%	125.8%	214.4%	114.8%
PROFITABILITY						
Net Gain from Operations	21,079,821	31,685,738	25,596,181	28,455,531	23,705,811	22,039,996
Net Income	3,079,065	27,712,797	22,182,737	25,707,763	20,636,081	22,061,922
Net Investment Yield*	5.0%	5.4%	5.3%	5.4%	5.6%	5.9%
1 Yr. Operating ROE*	16.7%	20.0%	17.8%	23.6%	23.8%	27.1%
Return on Admitted Assets*	0.2%	1.4%	1.2%	1.6%	1.4%	1.7%
Key Insurance Metrics						
% Annuities w/o Surrender Charge	NA	64.1%	61.8%	61.1%	71.0%	65.1%
Avg. Face Amt. of Life New Business	NA	26,612	35,480	58,438	36,912	28,950
% Interest Sensitive Reserves	NA	96.3%	95.9%	95.5%	95.3%	94.8%
Life Ins as % of Total Reserves	NA	3.9%	4.1%	4.5%	4.7%	5.3%
Lapse Ratio	NA	1.1%	1.9%	3.3%	0.7%	2.8%
Current Liquidity	105.7%	105.9%	106.3%	105.7%	105.0%	105.0%
General Ins. Exp. to Total Admitted Assets	0.3%	0.4%	0.4%	0.4%	0.5%	0.5%

Stress Testing

KBRA employed a stress testing approach to attempt to quantify the impact of adverse economic scenarios on GCU's balance sheet. Specifically, a material decline in the equity markets, higher credit defaults, and volatility in interest rates were considered. Because GCU's liability profile is almost entirely interest-sensitive and its investment portfolio is conservative and "plain vanilla" (95% fixed income securities, and over 90% in corporates), KBRA believes the society's most significant exposure is to changes in interest rates. Hence, the stress testing entailed a detailed examination of GCU's cash flow testing process.

The analytical team reviewed GCU's year-end 2019 asset adequacy analysis required by state regulators. GCU's appointed actuary, Allen Bailey, utilized seven deterministic interest scenarios (typically described as the New York 7) as well as four sensitivity tests based on the level scenario (NY1): (1) a 10% increase in expenses; (2) a 10% decrease in lapses; (3) a 10% increase in lapses; and (4) a 10% increase in mortality. In aggregate and by product line, all scenarios and sensitivities projected a positive present value of 40th year ending value of surplus based on both book value and market value. There were no interim periods in the projections where surplus became negative.

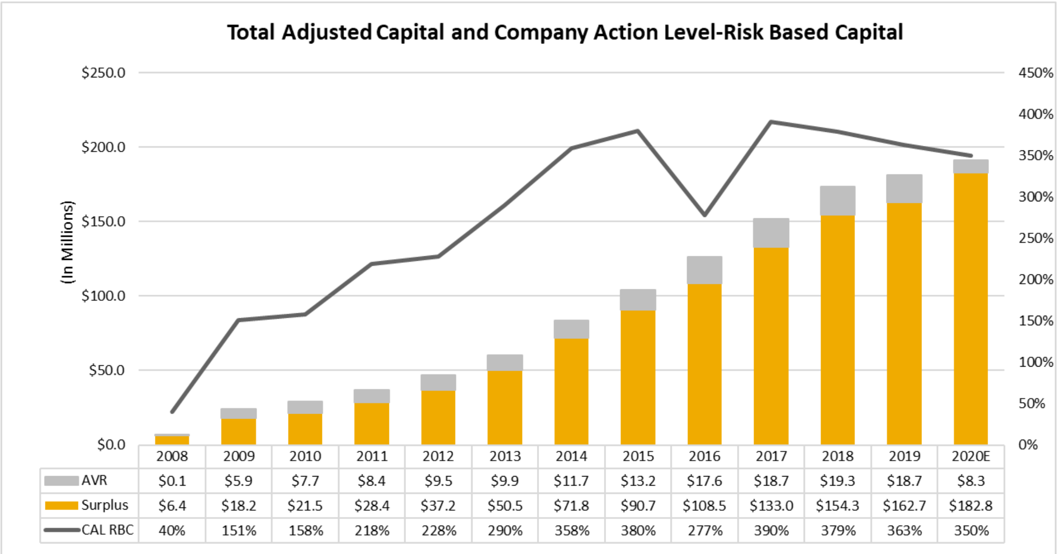
KBRA examined the preliminary results for 2020 cash flow testing conducted by Allen Bailey. All seven scenarios projected a positive present value ending value of surplus, increased from the 2019 results.

The analytical team also performed an asset credit stress test on GCU's fixed income portfolio. The results were consistent with GCU's current IFSR.

Qualitative Rating Determinants (QRD)
Balance Sheet Management
Operating Fundamentals
Company Profile & Risk Management

QRD 1: Balance Sheet Management

Quality of Capital



	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020E
AVR	$0.1	$5.9	$7.7	$8.4	$9.5	$9.9	$11.7	$13.2	$17.6	$18.7	$19.3	$18.7	$8.3
Surplus	$6.4	$18.2	$21.5	$28.4	$37.2	$50.5	$71.8	$90.7	$108.5	$133.0	$154.3	$162.7	$182.8
CAL RBC	40%	151%	158%	218%	228%	290%	358%	380%	277%	390%	379%	363%	350%

GCU suffered a severe setback in its investment portfolio that led to a 76% decline in surplus during 2008 (CAL RBC of 40%). The drivers were decreases of $9.8 million and $8.2 million in the valuations of common stock and bonds, respectively. Since 2009, GCU has exhibited exceptionally strong and consistent growth in total adjusted capital and operating results have been favorable. GCU has been able to successfully leverage new distribution platforms and has revitalized products to drive growth in annuity sales. The sizeable income generation exhibited in recent years has fostered substantial surplus and balance sheet growth. The society's surplus is up over 900% since the end of 2009, projected to reach a new high of $183 million at year-end 2020. This equates to a 10-year compound annual growth rate of nearly 25%.

GCU currently holds a sufficient level of risk-adjusted capital (CAL RBC 379% and 363% as of YE 2018 and YE 2019, respectively) which is sound, but somewhat below the industry median of 450%. A CAL RBC of 350% is projected for 2020. This measure is also slightly below that of similarly rated fraternal peers. Nevertheless, KBRA is comfortable with GCU's current level of risk-based capital given (1) the society has consistently added to capital over the last several years and has a very low expense base which will facilitate continued growth; and (2) the society's investment portfolio is primarily focused on lower risk assets.

Driven by solid asset performance, steady annuity and life (albeit small) premium flows, and favorable earnings trends, GCU grew its asset base to over $2.2 billion as of year-end 2020. This increase can be attributed to continued positive cash flows from strong annuity sales and growth in investment earnings. KBRA further notes that GCU continues to maintain a conservative asset makeup on its balance sheet with no financial leverage.

Asset Quality and Investment Risk

GCU currently has three investment advisors who manage its bond portfolio: Northern Trust (about 42% of invested assets as of year-end 2019), PNC (33%), and Prosperity Capital Advisors (24%), with all managers operating under the same recently revised guidelines.

GCU maintains a conservative portfolio with a focus which remains on fixed income securities. The investment portfolio, consisting primarily of investment grade corporate bonds, increased to $2.1 billion at September 30, 2020. Bonds make up 95% of GCU's assets, with an average maturity of over 20 years and an option adjusted duration of just under 12 years. The society maintains high bond quality with 95.4% of the bonds in the two highest NAIC rating classes and an overall average rating of BBB+.

Bond Portfolio Quality						
(In Thousands)		2019 BV	%		3Q20 BV	%
NAIC 1	$	595,572	31.0%	$	497,291	24.6%
NAIC 2	$	1,259,400	65.5%	$	1,429,756	70.7%
NAIC 3	$	37,126	1.9%	$	67,279	3.3%
NAIC 4	$	20,574	1.1%	$	25,532	1.3%
NAIC 5	$	9,893	0.5%	$	-	0.0%
NAIC 6	$	100	0.0%	$	1,087	0.1%
Total Bonds	**$**	**1,922,665**	**100%**	**$**	**2,020,944**	**100%**
BIGs/TAC		**37.3%**			**51.9%**	

The below investment grade portion of the fixed income portfolio has been reduced considerably from historical levels – less than 52% of total adjusted capital as of September 30, 2020. However, this increased from 37.3% at year-end 2019 which was largely driven by downgrades related to the global COVID-19 pandemic. Public corporates are GCU's largest allocation and are diversified by sector. The most significant concentrations are in financials (24% of total bond holdings), consumer-noncyclical (18%), communications (11%), and energy (9%). The portfolio remains diverse as no single credit exposure is greater than 2% of the portfolio.

Additional assets are in preferred stocks (2% of invested assets as of 3Q 2020), other invested assets (1%) and common stocks (1%, although $10.9 million or 43% of the common stock holdings are investments in affiliates). The asset classes serve to provide diversity and balance to the portfolio, as well as provide the benefit of higher growth potential. In 2020, GCU invested $10 million in a high quality/ low volatility equity strategy. Previously, its legacy equity portfolio had a market value of approximately $3 million.

(BV In Thousands)		3Q 2020	%
Bonds	$	2,020,944	94.5%
Preferred Stock		40,562	1.9%
Other Invested Assets		29,220	1.4%
Common Stock		25,421	1.2%
Cash & Cash Equiv.		17,601	0.8%
Mortgage Loans		3,462	0.2%
Other Assets		1,027	0.0%
Total Invested Assets	**$**	**2,138,237**	**100%**

GCU also has a small alternative/Schedule BA allocation with notable investments in a Washington Alliance Fund ($15.7 million as valued on 9/30/2020; real estate fund). Management expects that allocations to its alternative investment strategy will grow to $60 million through 2022.

Furthermore, since 2008, GCU has persistently outperformed its peers in net investment income due to its growing invested asset base as well as an above-average pre-tax investment yield. Despite the continued depressed interest rate environment, net investment yield on the portfolio in recent years has been in the range of 5-6%. With tighter credit spreads in an anticipated prolonged low interest rate environment, active management of credited rates will be necessary in order to maintain margins.

Bond Portfolio Maturity			
(In Thousands)		3Q20 BV	%
Less than 1 Year	$	10,793	0.5%
1 to 5 Years	$	50,178	2.5%
5 to 10 Years	$	270,319	13.4%
10 to 20 Years	$	658,940	32.6%
Over 20 Years	$	1,017,148	50.3%
No Maturity Date	$	13,566	0.7%
Total Bonds	**$**	**2,020,944**	**100%**

In 3Q 2020, GCU recognized OTTI expense which totaled $16.3 million from bonds related to three old field companies. A handful of other corporate exposures remain on the watchlist as of November 2020, which totals just over $11 million in book value (0.5% of invested portfolio).

Financial Flexibility and Access to Capital

GCU has favorable financial flexibility given its recent profitability and revenue generation. GCU's operating performance and internal capital generation allows for financial flexibility in funding its own initiatives in addition to meeting the needs of any current expenses. Currently, GCU maintains no debt and all financial obligations are supported by operations. Investment income is primarily reinvested.

GCU is a member of the Federal Home Loan Bank of Pittsburgh (FHLBP), which provides the society with access to a secured asset-based borrowing capacity for funding agreements and backup liquidity. The society has a maximum borrowing capacity of approximately $15 million. As of 3Q 2020, GCU has borrowed $12 million via a funding agreement (below 2% cost of borrowing) to enhance earnings.

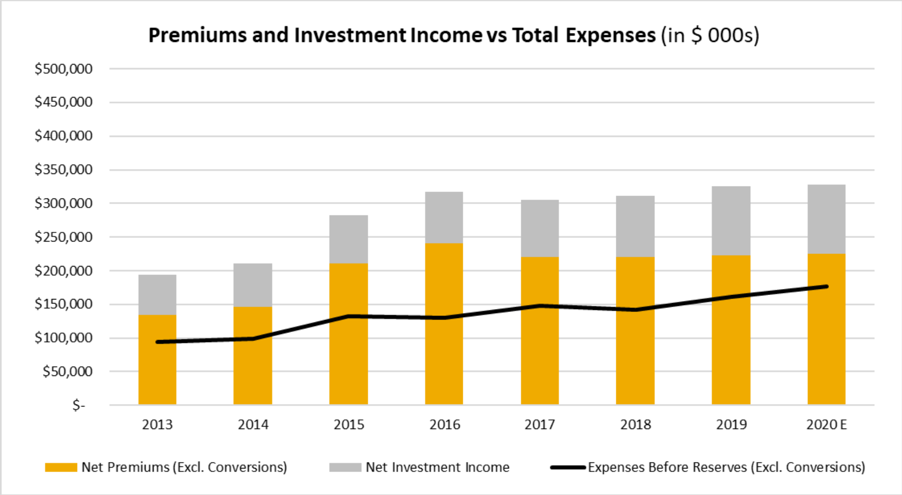
KBRA expects GCU to maintain sufficient financial resources to fund any planned initiatives and cash requirements in the near to medium term.

Liquidity and Asset/Liability Management

GCU's liability structure is heavily weighted in annuity reserves — 96%. Upon issue, products are protected with surrender charges. In addition, the society, like many fraternals, benefits from low lapses/withdrawals due to the strong affinity relationships that members have with the societies. However, KBRA believes that disintermediation risk would still be heightened if interest rates were to rise. KBRA notes that 69% of GCU's annuity contracts have less than 5% surrender charge with 48% without any charges. This particular concern is somewhat mitigated by the fact that many of these contracts have guaranteed minimum interest crediting rates of 3.0% or higher (63% of fund value of annuities).

The life insurance block, largely whole life, provides a steady source of earnings for the company. While small compared to the annuity products, it is a highly creditworthy product built on the cash value of the account. Additionally, the society's lapse ratio, 1.1% for 2019, remains low.

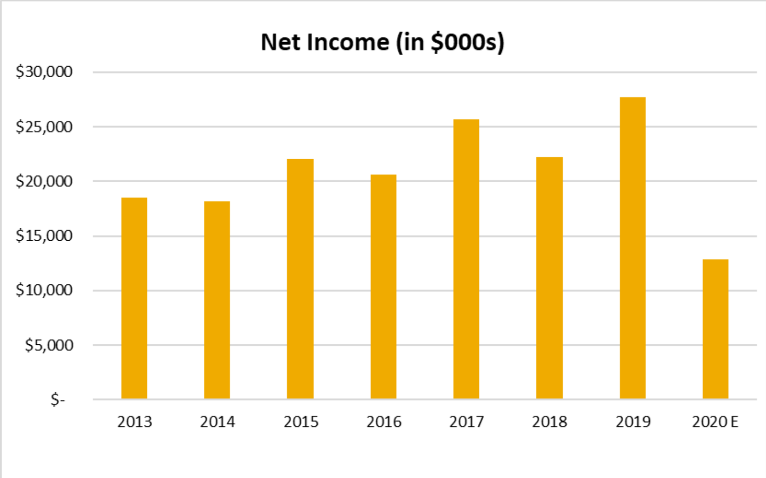
The company's current revenue stream (excluding conversions) – expected to approach $225 million in 2020, and net investment income, to exceed $103 million – compares favorably to current benefits paid.



QRD 2: Operating Fundamentals

Current Year, and Consistency of, Profitability

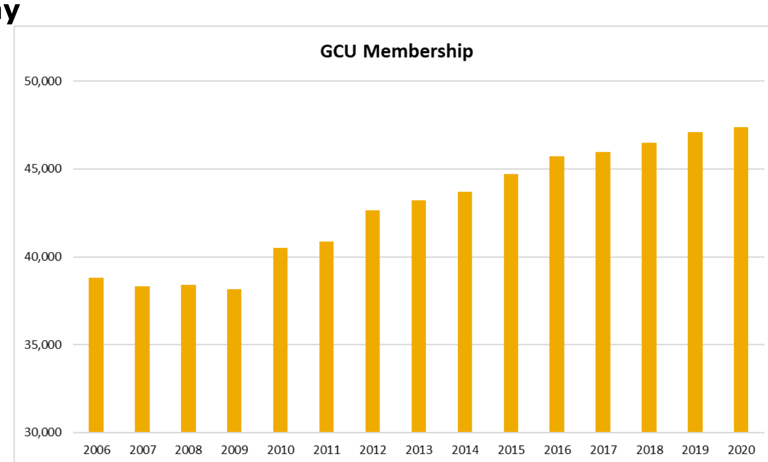
GCU has successfully grown its net gain from operations over time, with $31.7 million in 2019 and $29.7 million estimated for 2020. The society has been able to maintain top line growth by expanding its membership base along with penetrating its existing membership with its new (more conservative) product offerings.



Net income at year-end 2020 is projected to be $12.9 million, which would represent a nearly 53% decline from 2019. The difference was mostly attributable to approximately $16.9 million of realized losses due to the OTTI expense related to certain energy bonds.

In order to sustain its current level of profitability – above 16% return on capital – GCU will need to continue monitoring its crediting rate strategy on its annuity programs to maintain its target spreads. KBRA notes that GCU's crediting rate strategy needs to exhibit like-responsiveness in both up and down rate environments. Paired with continued success in its annuity book, successful growth of the society's life insurance portfolio will provide further stability to its operating results. GCU's targeted spreads are 150-200 basis points. Average spread for 2020 (197 basis points) was within GCU's targeted range but down 7 basis points from 2019.

Earnings Diversification: Product/Geography



KBRA notes that GCU's membership has been on a slight upward trajectory since 2009. Management acknowledges that it had historically employed a strategy to sell annuities at credited rates above the commercial market; hence, at lower spreads. This strategy has since been abandoned in favor of maintaining healthy margins in the persistent low interest rate environment via active management of credited rates. Nevertheless, it is important to highlight that GCU has been successful in growing membership within the products it is actively marketing, and that this trend that stands in stark contrast to the declining membership trends of many other fraternals.

GCU has a regional geographic spread with the majority of its business written in mid-Atlantic and mid-western sections of the United States. KBRA believes GCU's geographic distribution sufficiently supports the business strategies and continued stability in its core membership. KBRA notes that GCU's top 2 states (PA and WI) account for approximately half of its direct premiums written, ranging from 55% to 62% since 2012 (down to 50% through 3Q 2020).

Exposure to Event Risk

Given its sound capitalization, conservative investments and broad membership, KBRA believes GCU is well-positioned to withstand an economic downturn and has not experienced significant financial strain during the COVID-19 crisis. Nevertheless, as noted previously, GCU's balance sheet profile exposes the enterprise to significant interest rate movements. GCU does not sell variable products and, as a fraternal, benefits from the affinity relationship of its member policyholders. Credited rates are generally higher than commercial carriers; hence, it is not as likely for a fraternal to experience a "run-on-the-bank" scenario.

QRD 3: Company Profile and Risk Management

Management Profile and Strategy

For fraternal organizations, it is critical for management to be engaged and closely associated with their members. GCU's management expertise is concentrated within several key persons who collectively have extensive experience in the society's products, operations, and historical events. In the past, KBRA has noted that GCU would benefit from a deeper bench of senior and mid-level managers to supplement and support the current team. The society has hired several officers over the last 12-18 months to round out its management team. A recently hired technology director should further enhance GCU's strides in leveraging technology for efficiency and automation on a go forward basis.

Market Position

GCU has little market penetration in even its largest territories, and commercial carriers are looking for more and more ways to broaden sales – product innovation, strategic relationships, cross-selling, worksite strategies, and disintermediation of agents, to name a few. GCU has contracted with new distribution platforms, discussed in the following section, in addition to revitalizing its brand image.

Distribution

GCU distributes its products through independent marketing organizations (IMO), managing general agencies (MGA), and select field marketing organizations (FMO). This strategy was implemented in 2013 to maximize the efforts of a small home office sales team and give higher value to the GCU contractual relationship. This distribution strategy has greatly increased GCU's access to target growth states through its working relationships with experienced, producing agents.

GCU has recently been focusing on distribution management initiatives such as gaining stronger commitment from its top producers, capitalizing on opportunities to diversify and recruit distribution from a regional and national perspective, as well as redefining and implementing agent productivity measures.

Risk Management

GCU established a formal enterprise risk management (ERM) program in 2017, which is detailed in its ERM Policy and incorporates an annual risk appetite statement. The key objective was to develop, and implement, an overall risk and control framework, including the key financial reporting controls for GCU and its subsidiaries.

GCU's board of directors and Risk Committee board representatives are ultimately responsible for the approval and establishment of the ERM policies for the society, including reviewing and approving the reports from the Enterprise Risk Committee (ERC). The Risk Committee is comprised of five members of the board of directors and four representatives from the executive management team (the same four who are on the Executive Finance Committee). Members of the Risk Committee are appointed by the chairman of the board of directors and serve for a four-year period.

The ERC is delegated by the Risk Committee to oversee risk management activities, manage day-to-day risk decision-making, review and assess risk management reports from all areas of GCU, and approve of appropriate risk management procedures and measurement methodologies. The president and chief executive officer of GCU selects the chief risk officer (CRO) to serve as the head of the ERC. The current CRO is Tim Demetres, who also serves as the society's chief financial officer. The CRO is responsible for the management and supervision of the ERC and implementation of the ERM Policy. The CRO reports directly to the Risk Committee at least semi-annually to review the decisions made by the ERC and to give a transparent report of ERM activities including the results of any risk assessments performed across GCU.

Reinsurance Utilization:

GCU's life product reinsurance program remained largely unchanged in 2020. GCU has relationships with two insurers: Optimum Re Insurance Company (Optimum) and Aetna Life Insurance Company (Aetna), respectively, provide reinsurance to the various policies, life and Medicare supplement, offered by the society. The reinsurance coverages in place do not have any third-party guarantees. All treaties are solely between GCU and the reinsurers. As of January 1, 2020, GCU's Medicare supplement block was placed into run-off. Hence, no new business is being written. Equitable Life & Casualty (Utah) administered all Medicare supplement policies through October 2020 in its capacity as a third-party administrator. Equitable announced it was discontinuing its administrator services after 2020 which provided GCU an opportunity to appoint a new administrator at a lower cost.

External Considerations

Since GCU is the top company in the structure and the subsidiaries are strategic and risk-neutral, the analytical team has determined that no rating enhancement or drag on GCU's ICA is warranted.

Impact of Transfer Risk

As GCU is domiciled in the United States (AAA rated by KBRA), only writes business in the United States and only has USD denominated securities in its asset portfolio, there is no currency transfer risk.