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Annuity Market Update

ACA Conference – Francis Fernandes & Colin Parnell

6 February 2015

65 Gresham Street London, EC2V 7NQ
t 0207 709 4500

For Professional Clients Only

Your speakers

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Agenda

- Recap on Buy-ins / Buy-outs
- The Market
- Areas for discussion
  - The future: impact of 2014 Budget
  - Market trends: trend to larger transactions?
  - Medical underwriting: the biggest area for growth?

Buy-in versus Buy-out

Before

- Scheme invests its assets and uses the proceeds to pay pensions to its members

Buy-in versus Buy-out

Buy-in

- Typically covers part of the membership
- Perfectly matching asset
- Sponsor covenant risk vs Insurance counterparty exposure
- Policy in name of Trustees

Buy-in versus Buy-out

Buy-out

- Typically covers full membership
- All assets transferred to insurer
- Individual policies issued
- Scheme wound-up

Annuity purchase – arguments for

Managing risk

Interest rates and inflation	Duration and inflation matching cashflows
Asset Generation	Insurers capture corporate bonds
Living longer	Protection against increasing longevity
Covenant	Additional support for other risks
Hassle free	Reduce / eliminate governance burden

Annuity purchase – arguments against

Managing risk

Overall risk reduced?	Has overall liability matching improved?
Lost investment return	Growth potential diminished?
High current price	In absolute terms, prices are high
Inflexible	No turning back, DIY alternative
Optimal strategy?	Pensioners may be the least risky

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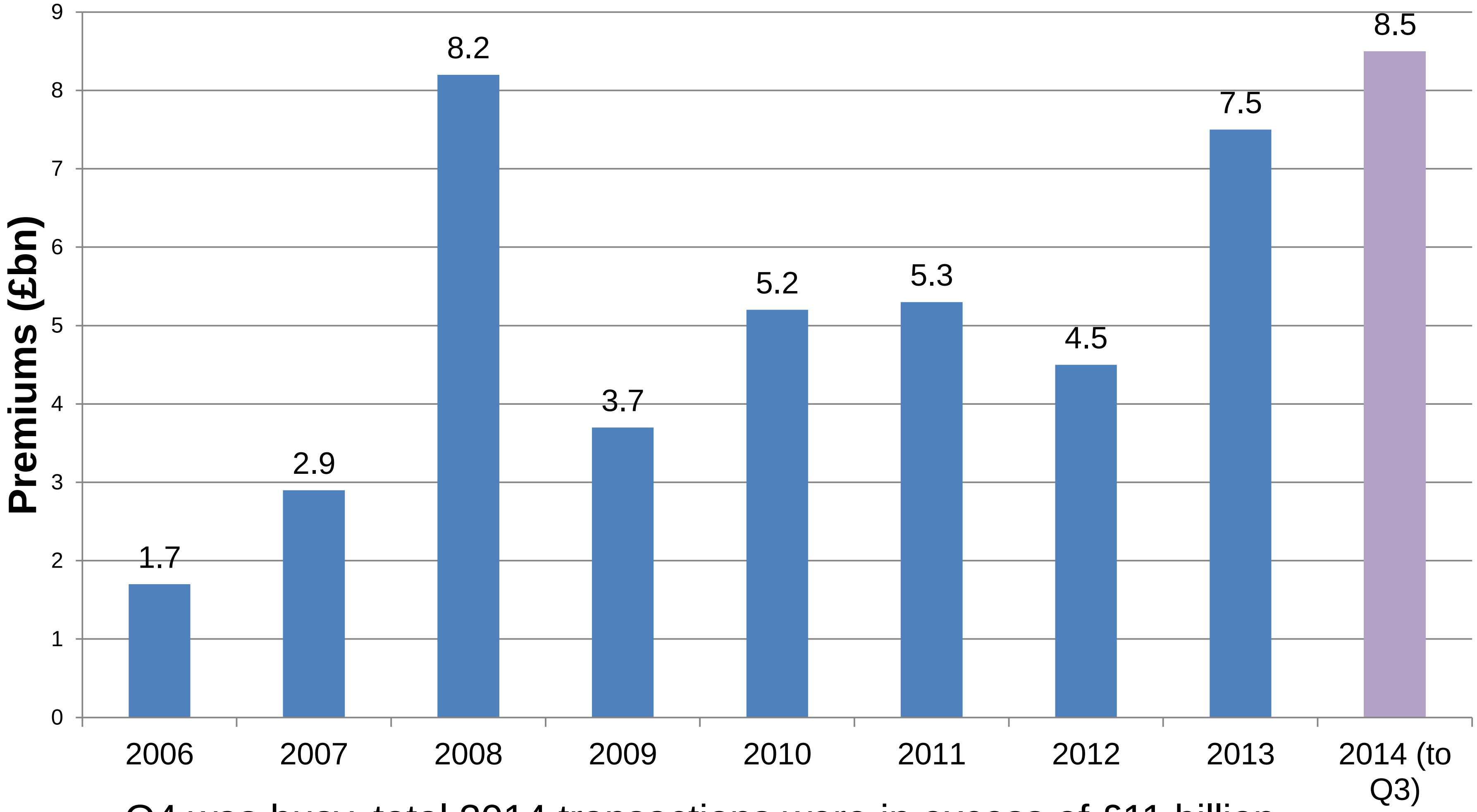
The Market

Total bulk annuity transactions over the last 9 years



Q4 was busy, total 2014 transactions were in excess of £11 billion

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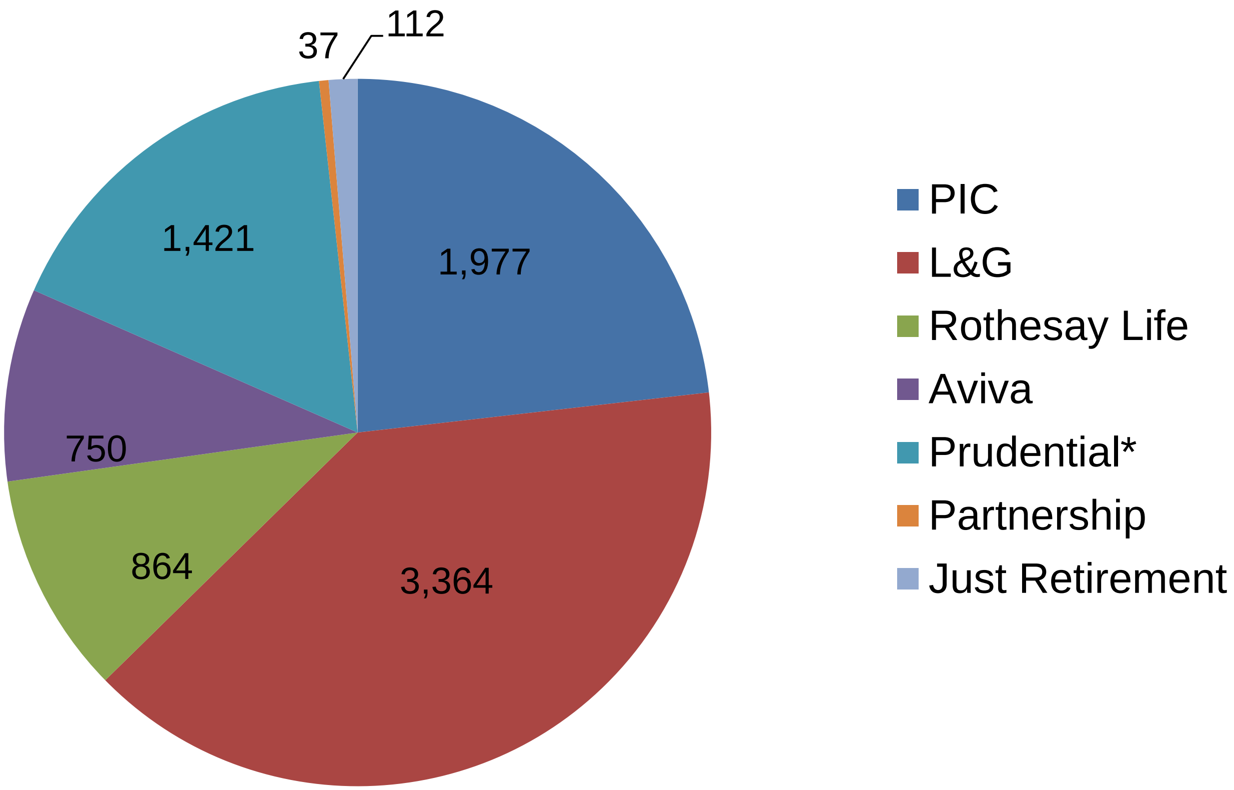
Longevity swap transactions well over £20 billion (2013: £8.9 billion)

What transactions happened in 2014?

Value of deals by provider in 9 months to Q3 2014



Initial Q3 2014 figures for Prudential – final figures are TBC
Excludes Q4 £200 million transaction for Partnership
Excludes Q4 £2.5 billion transaction for L&G (TRW Automotive)

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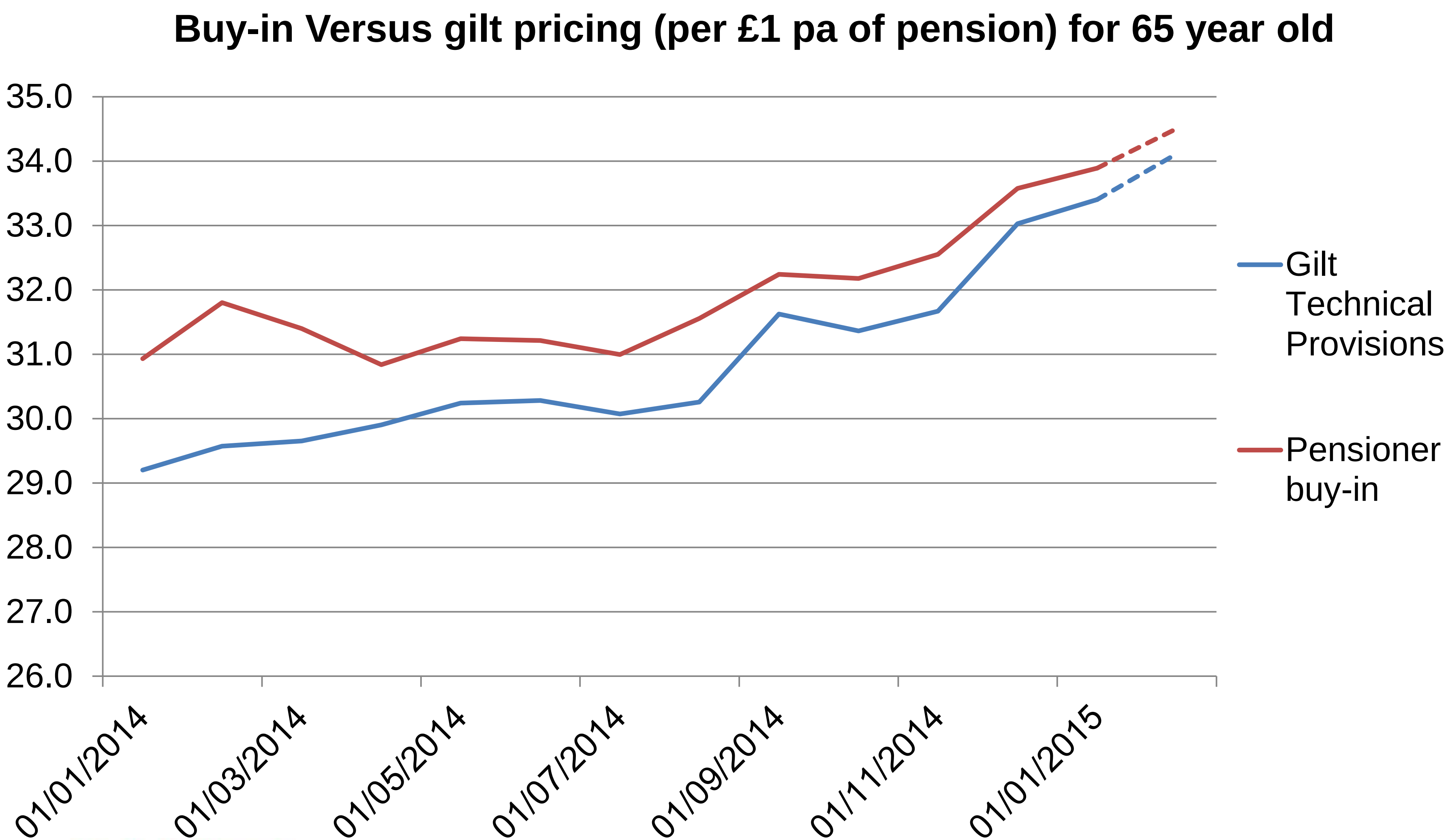
Key recent bulk annuity transactions

Company	Insurer	Size	Comments
ICI	L&G and Prudential	£3.6bn	Buy-in
Unknown	Partnership	£200m	“Top slice” buy-in
TRW	L&G	£2.5bn	Pensioner only buy-out

Annuity Cost Versus Technical Provisions



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Discussion topics

Discussion 1 – the future

1. 2014 Budget impact
   i. Will there be a rush to transfer into Defined Contribution pensions?
   ii. Will insurers affected by the Budget continue their keen pricing?

2. Insurer price monitoring
   i. Live indicative pricing feeds from insurers – where is this headed?

3. Gilt yields outlook
   i. Will yields go lower?
   ii. Worth delaying a transaction?

4. Solvency II insurer pricing and process implications

Discussion 2 – market trends

1. Competition
   i. Short term capacity constraints and selective insurers?
   ii. New entrants to the market?

2. Deferred premium buy-in (spread premium payments)
   i. First deal of this structure with L&G (2013), but others offer this
   ii. All scheme members insured, paving the way for solvent wind-up

3. Advisor trends
   i. Buy-out funding and investment targets?
   ii. Allowance for GMP equalisation and wind-up expenses?
   iii. Effective legal and data preparation

Discussion 3 – Growth of medical underwriting

Stage 1

Risks communicated, decision to underwrite, indicative quotes.

Stage 2

Questionnaires, Interviews, GP reports, shared with several insurers.

Stage 3

Underwritten quotes, best and final prices.

- Opportunity now?
- Exclude traditional providers?
- Cost savings?
- Data Protection
- Competition
- Selection risk
- Split the market?
- Insurer strength
- Timescale
- Recent innovations
- Top slicing

Typical Process: Adjusting to reflect Medical Underwriting?

Typical Timeline and 3-stage process for non-underwritten policies

Early December
Agreement between Trustees and Company

Mid December
Request for quotes issued

January and February
1st Round of quotes

Mid March
Short-List Insurers and Final Bidding

End March
Selection of Preferred Insurer

Mid April
Structuring and Execution

Summary

How you can avoid the traps

- Planning
- Data
- Consider wider issues
- Investments
- Improve knowledge and understanding
- Build relationships with insurers

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Questions and Discussion

Regulatory Statement

The information contained within this presentation does not constitute financial advice.

The information provided is based on our understanding of current law and taxation as at 3 February 2015.

HMRC policy, practice, and legislation may change in the future.

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