LET'S TALK

BUYOUTS POST BUDGET

AN OPPORTUNITY WORTH EXPLORING?

BUDGET RECAP

George Osborne's recent Budget announcements, aimed at giving individuals more flexibility over how they use their defined contribution retirement savings, have caused quite a stir. Within hours we saw insurers' share prices sliding, as investors predicted a dramatic decline in the individual annuity market. In retrospect this was an overreaction, but insurers have seen volumes of individual annuity business fall and are looking for ways to replace this.

WHAT DOES THIS MEAN FOR BULK ANNUITIES?

Whilst insurers who've lost individual annuity business scramble to develop innovative new at-retirement products, those also active in the bulk annuity (buy-in/buyout) market are looking to these parts of their businesses to absorb immediate spare capacity. So, the Budget has created opportunities for trustees and sponsors of UK pension schemes looking to insure all or part of their defined benefit liabilities.

Insurers, keen for bulk annuity business, are becoming more flexible in the types of solutions they will offer. For example, allowing sponsors to spread policy premium payments over an agreed recovery period rather than paying the full amount up front. In addition, we believe other insurers, not currently offering bulk annuities, are taking steps to enter this market place in order to recover some of their Budget driven losses in the individual annuity space.

Some insurers seek to acquire and hold higher yielding assets than those traditionally found in annuity portfolios, e.g. equity release mortgages or private finance initiative investments in addition to traditional corporate and government bonds. In the past these have been used to help reinforce the healthy margins secured against individual annuities. In some cases insurers are now offering to use these assets to support bulk annuity pricing, allowing them to give schemes of their choosing, e.g. those with a higher chance of transacting, lower quotations. Such opportunities are limited - a given asset can be used to support enhanced pricing on only a limited number of deals, i.e. it cannot be redeployed.

SHOW ME THE NUMBERS

Chart 1 shows levels of bulk annuities written since 2004. At £7.45bn, 2013 was the second highest year on record, but we've already seen over £6bn of deals announced up to early June 2014 - more than 80% of last year's total. Market commentators have recently revised up their predictions for the 2014 finishing position - from around £10bn to over £20bn. We've also seen some record breaking deals in the mix, including a £3.6bn buy-in for the ICI Pension Fund (split between two insurers). This marks a shift in larger schemes' long term goals from self sufficiency to buyout. Overall, insurer appetite is increasing across the spectrum.

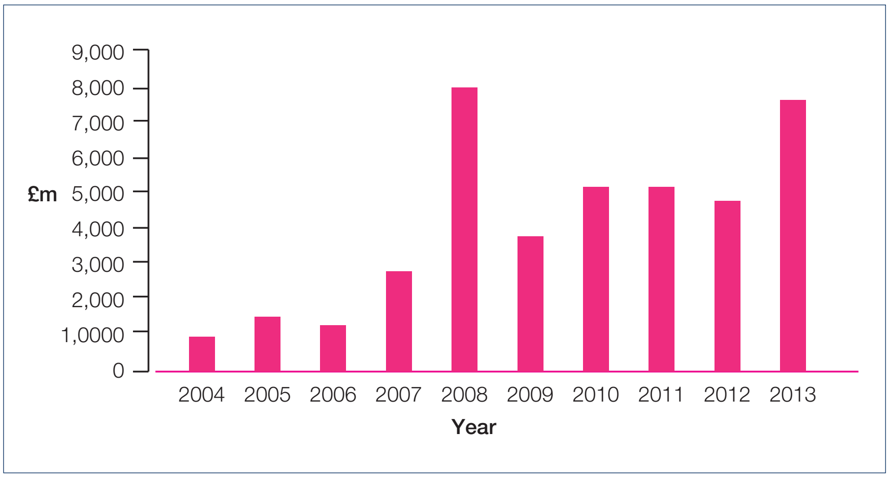

Chart 1: Bulk annuity business written since 2004

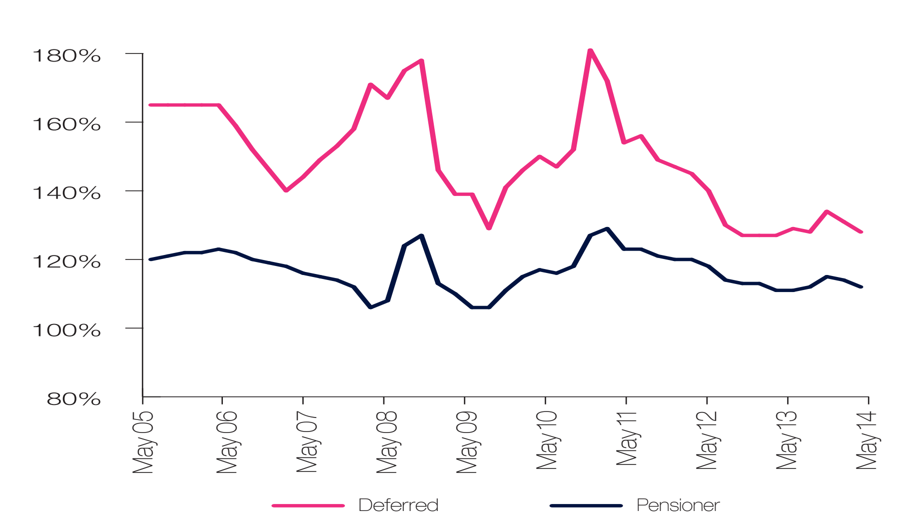

Chart 2: JLT affordability index

Market conditions also play a role. Chart 2 shows JLT's affordability index, which tracks prices in the buyout market against company accounting liabilities. A general trend of improving buy-in/buyout affordability for both pensioners and deferred members over the last 2-3 years, against a backdrop of improving funding levels, have combined to increase sponsor and trustee demand for bulk annuity solutions. The Budget creates opportunities for them to realise this.

HOW LONG WILL IT LAST?

We believe there is an immediate opportunity for schemes to benefit from the conditions described above, arising from the March 2014 Budget announcements. Insurers are reporting high demand for quotations, confirming that many trustees and sponsors are already seriously considering a bulk annuity purchase. We expect insurer appetite to persist into the second half of 2014, although this will continue to be limited by the number of quotations and transactions they can physically process.

WHAT SHOULD I DO NEXT?

Many trustees still regret missing the chance to purchase an annuity in 2008. To best position your scheme for a 2014 trade, the first step is to understand whether this is affordable and the second is to be in the market, to ensure that when an opportunity does arise, your scheme can take advantage of it. By providing some straightforward data in respect of your current pensioners, JLT can do a quick initial assessment using up-to-date rates from insurers to estimate the range of current market pricing for your scheme and compare this against your funding liabilities. This will help you to understand at what price a transaction makes sense. We can also obtain indicative quotes for deferred members, if required.

If initial results are positive, we have efficient, fixed fee processes that will allow you to transact a pensioner buy-in in as little as eight weeks. For further information, please refer to our Buy-inSure brochure. A similar approach for schemes who feel they can benefit from medical underwriting is also available.

With full commitment from scheme sponsors and trustees, transactions in Q3 and Q4 2014 are readily achievable.

WHERE CAN I GET HELP?

Your usual JLT contact can refer you to our dedicated Buyout Team. Alternatively email buyouts@jltgroup.com.

The JLT Buyout Team completed 30 bulk annuities for our clients over 2013, over 15% of total market deals transacted last year. Our deal conversion rate, measured at c. 60% by one leading insurer in a period up to July 2013, is significantly ahead of the industry average (which regular market speculation and commentary put at around 20%). The Team are able to advise on a wide range of transaction types, varying in size from below £1m to in excess of £1bn, covering deal structures from conventional bulk purchase annuities to fully bespoke de-risking solutions.

This Let's Talk does not constitute advice

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