

Risk Settlement: UK market update

March 2018

Headlines

- Spare capacity for both pensioner buy-ins and full scheme deals not utilised
- Aon predicts record £30bn bulk annuity market in 2018 as schemes become live to favourable pricing period for annuities
- Longevity swap interest rising following market re-pricing

Bulk annuities – scope to use more market capacity

In 2017, the bulk annuity market took over £10bn of bulk annuity business from pension schemes for the fourth consecutive year, but did not see a new record size despite attractive pricing and increased capacity.

The bulk annuity providers did not write substantial new insurance company back-book deals in the year, in contrast to 2016 (when Rothesay Life and L&G absorbed £9.5bn of back-books) and now in 2018 (with Rothesay Life taking on £12bn of Prudential back-book business).

For 2018, the overall volume of bulk business written by the market is on course to match our prediction of £30bn, including back-books. 2017 instead stands out as a year of some missed opportunities.

Better pricing was realised through insurers using a wider set of income-bearing assets to generate a competitive yield. This was supported by strong competitive market pricing and a more stable regulatory environment than in past years. This was further augmented by improvements in longevity reinsurance pricing as the year progressed.

While 2016 bulk business was dominated by repeat buyers, some of these schemes had run out of pensioners to secure for the time being. There was insufficient demand from other schemes that would have found a transaction to be feasible, leaving spare capacity.

This delay to further market growth looks temporary, with a substantial number of large auctions already in progress in 2018. This has left insurers managing their workload by declining some auctions, favouring well-defined decision-making processes from established broking teams.

Breakdown of bulk annuities by provider

The table below summarises bulk annuities secured by pension schemes over 2017 compared with 2016:

2017 rank	Bulk annuity providers	2017		2016	
		Value (£m)	Market share	Value (£m)	Market share
1	PIC	3,704	30%	2,529	25%
2	Legal & General	3,405	28%	3,339	33%
3	Aviva	2,045	17%	1,477	14%
4	Just Group*	998	8%	620	6%
5	Rothesay Life	960	8%	-	-
6	Scottish Widows	645	5%	943	9%
7	Canada Life	544	4%	145	1%
	Phoenix	-	-	1,181	12%
	TOTAL	12,301		10,234	

*On 4 April 2016, a merger resulted in Just Retirement Group plc and Partnership Assurance Group plc becoming part of what is now Just Group plc. The figures are on a combined basis, reflecting business written into both life companies. The table excludes back-book transactions. It reflects an Aon survey of the providers.

Recent volumes have been mainly concentrated in two providers, PIC and L&G, leaving substantial scope for business growth for some of the other providers. Aviva in particular has increased its volume placed substantially and is aiming to increase it further in 2018.

Scottish Widows and Canada Life have become established in the market following 2015 launches. The Phoenix Group, which previously negotiated a transaction involving one of Phoenix's own pension schemes, is understood to be about to write its first external bulk annuity. This has increased the number of active bulk annuity providers in the market to eight, and most auctions are hence seeing competitive pricing.

Number of transactions

The table below shows the deals completed in the market.

This shows L&G, Aviva, and PIC securing most individual deals, writing across a wide range of sizes and transaction structures, with Just Group writing a substantial number of the market's pensioner buy-ins outside of the largest auction processes.

Other providers have focused on a narrower range of auction processes, with some providers preferring larger or less mature liability profiles, to suit their asset sourcing capabilities and target volume, as well as the relative competitiveness of different areas of the market.

The majority of deals remain focused on pensioners, but the substantial improvements in scheme solvency positions over 2016-2017 make buy-out more attainable than before for a substantial number of schemes. Providers are reporting a much increased pipeline of full scheme buy-out enquiries in 2018.

Larger recent transactions

2017 saw no individual deals over £1bn, with the largest disclosed transaction being a £725m PIC annuity to secure the liabilities of the Dockworkers Pension Scheme. Other large disclosed deals for 2017 included:

- Two £600m pensioner buy-in deals for Pearson with each of Aviva and L&G;
- A £590m pensioner buy-in for Ferguson (formerly Wolseley) with PIC;
- A £570m pensioner buy-in for the Plumbers pension scheme with L&G;
- A £490m pensioner buy-in for the Merchant Navy pension scheme with L&G, as a repeat annuity buyer;
- Smiths Group securing a further £337m of their two main pension arrangements with transactions with PIC and Canada Life; and
- Rothesay Life transactions to secure all liabilities in pension schemes of Royal Mail (£450m) and Tullett Prebon (£270m), in bespoke transactions with residual risk cover.

2017 H2 Rank	Bulk annuity providers	H2 2017		H1 2017		H2 2016	
		Cases written	Value (£m)	Cases written	Value (£m)	Cases Written	Value (£m)
1	Legal & General	16	1,901	15	1,504	8	2,698
2	PIC	16	1,829	10	1,875	15	1,632
3	Aviva	23	1,719	11	326	28	549
4	Just Group	15	703	7	295	15	779
5	Rothesay Life	2	555	3	405	-	-
6	Canada Life	3	268	3	276	3	110
7	Scottish Widows	3	240	5	405	1	592
-	Phoenix	-	-	-	-	1	1,181
	TOTAL	78	7,215	54	5,086	71	7,541

The table excludes back-book transactions implemented by Legal & General and Rothesay Life. It reflects an Aon survey of the providers.

Longevity swaps

2017 was a period of adjustment for the longevity market. Better pricing emerged as the year progressed, and to a level where we became satisfied that the longevity market offered good value again.

During 2016, we had raised concerns about a 'dislocation' in longevity pricing, before the reinsurance market had reflected the marked slowdown in UK life expectancy improvements.

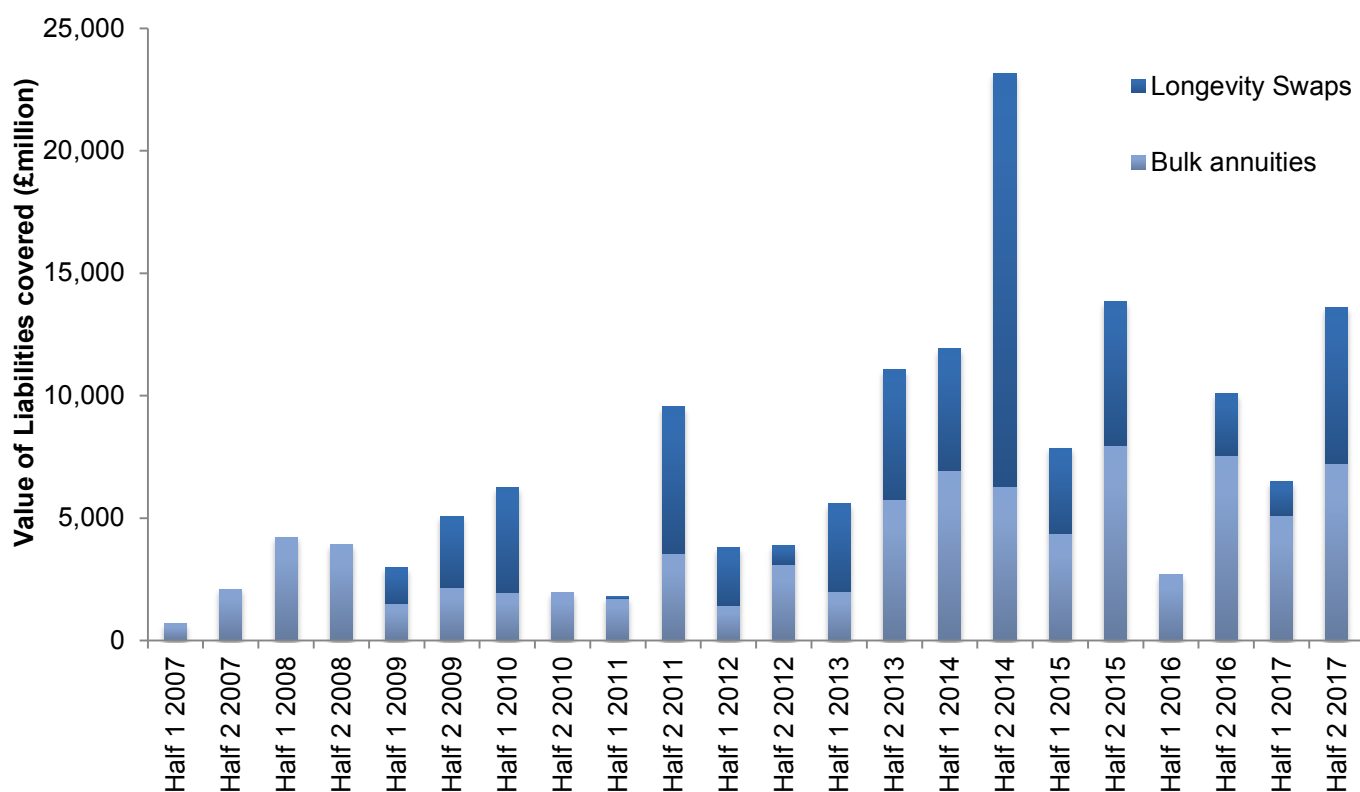
As the table below shows, the deals that did occur in 2017 reflected a variety of structures to pass risk onto the reinsurance market. The L&G transaction in particular was unusual in passing on longevity risk directly to the reinsurance market, limiting the cost of cover. At present, the market is continuing to see a variety of structures proposed for new transactions.

We expect 2018 to be a very busy year for the longevity market, both in servicing reinsurance for a substantial volume of new bulk annuities, and in supporting a larger volume of longevity deals from pension schemes.

Date	Pension scheme	Size	Structure	Insurer/ Reinsurer
Sept 2017	British Airways	£1.6bn	Captive (Guernsey)	N/A / Partner Re and Canada Life Re
Sept 2017	MMC UK Pension Fund	£3.4bn	Captive (Guernsey)	N/A / Prudential Insurance Company of America
Aug 2017	Scottish Hydro-Electric Pension Scheme	£0.8bn	Pass-through	L&G / SCOR
June 2017	Skanska Pension Fund	£0.3bn	Fully intermediated	Zurich / SCOR
Mar 2017	Anon	£0.3bn	Fully intermediated	Zurich / SCOR
TOTAL		£6.4bn		

Long term market development

This graph shows the overall volume of risk settlement transactions disclosed for company pension schemes in the UK. The bars show the volume of bulk annuities and longevity swaps.



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