


Medically underwritten buy-ins - market insights

April 2015



I am delighted to present Hymans Robertson's annual report on medically underwritten buy-ins - providing an insight into the medically underwritten buy-in market.

Over the past two years, the market for medically underwritten buy-ins has grown significantly to the extent that they represented over 10% of all bulk annuity transactions that took place during the fourth quarter of 2014. With this growth we're also seeing more competition, as new insurance companies enter this market.

We expect the pricing for medically underwritten buy-ins to remain attractive for 2015 – often over 5% cheaper than traditional buy-ins, providing pension schemes with a window of opportunity to take advantage of the competitive pricing during 2015. Longer term, we expect demand to outstrip supply with pricing expected to harden.

If you would like more information on medically underwritten buy-ins or would like to discuss this report in more detail, please contact me or your usual Hymans Robertson consultant.

James Mullins



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Background – what is a medically underwritten buy-in?

A medically underwritten buy-in differs from a traditional buy-in because it takes account of individual members' health status, initially by asking members to complete a short questionnaire. Having the additional information enables insurers to refine their pricing which can be particularly beneficial if the members being insured have health or lifestyle conditions. However, by just going through the process of collating health information, it allows the insurance companies to have the best possible understanding of the risk that they're taking on. This allows the insurers to remove unnecessary prudency margins (which are needed when there's more uncertainty) and so provide the most competitive pricing for pension schemes.

Top slicing

In nearly all pension schemes a few pensioners (typically former executives and senior managers) account for a large proportion of the liabilities. This represents a significant concentration of risk for the pension scheme because if this small group of pensioners live longer than expected, then there's a disproportionate impact on the scheme's financial position. Medically underwritten buy-ins are currently the most cost effective way of removing this concentration of risk, associated with the pensioners with the highest individual liabilities. Such transactions are referred to as 'top sliced, medically underwritten buy-ins'.

Traditional buy-in pricing for high value pensioners reflects the fact that affluent individuals are likely to live longer. By gathering data on their health and lifestyle it's more likely than not that some health conditions will be present which reduces the cost of insurance.

For these reasons, well over 50% of the medically underwritten buy-ins to date (by value) have been top sliced buy-ins. We expect this trend to continue.

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Attractive medically underwritten buy-in pricing remains

In our experience medically underwritten buy-in pricing remains over 5% cheaper than traditional pricing, often close to a pension scheme's technical provisions reserve.

This means that pension schemes can exchange gilts (a broad matching asset) for a medically underwritten buy-in (a perfect matching asset, including protecting against life expectancy and proportion married risk) without any cost implications nor any need to increase company contributions.



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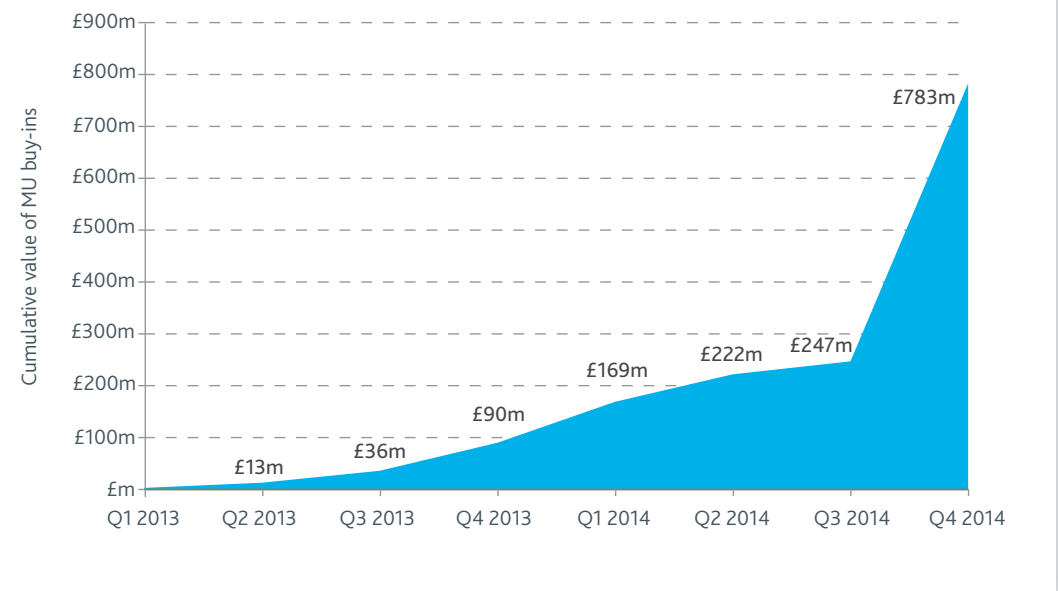
Insurance Companies who offer medically underwritten buy-ins

- ◆ Just Retirement and Partnership are driving this market, each with close to 50% market share (by value) of all medically underwritten buy-ins. Aviva has also completed one medically underwritten buy-in.
- ◆ Given the rapid growth in this area, other insurers are increasingly active and interested in this part of the market. We expect to see other insurance companies offer medically underwritten buy-ins during 2015.

Headlines for the medically underwritten buy-in market to date

- ◆ From a standing start in 2013, 43 pension schemes have now completed medically underwritten buy-ins covering almost £800m of liabilities.
- ◆ The popularity of medically underwritten buy-ins has grown to such an extent, that they represented over 10% of all bulk annuity transactions during the fourth quarter of 2014.
- ◆ Given the attractive pricing, medically underwritten buy-ins have very wide appeal and conversion rates from obtaining a quotation to completing a transaction are very high – we estimate conversion rates are around 75% for the market as a whole and currently stand at 100% for Hymans Robertson clients.
- ◆ MorganAsh are the market-leading company for gathering health information from members and providing this information to insurance companies to refine their pricing.

Figure 1 – the rapid growth of medically underwritten (MU) buy-ins:

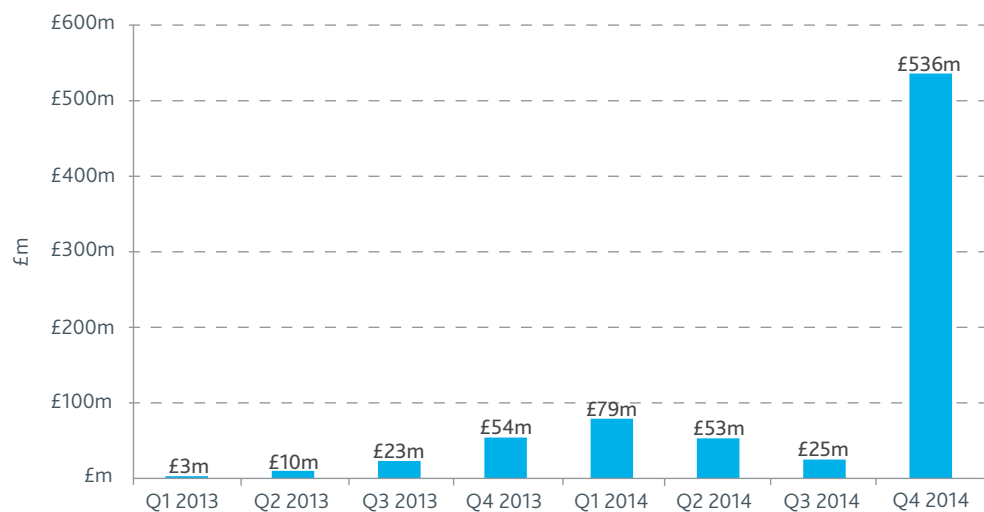


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Headlines for the outlook in 2015

- ◆ We expect to see between £500m and £1billion of medically underwritten buy-in deals to be completed during 2015, taking total market volumes to in excess of £1.5 billion by the end of 2015.
- ◆ Insurer pipelines are stronger than ever and Hymans Robertson is currently working with over 15 pension schemes who are either in the process of completing a transaction or obtaining medically underwritten buy-in quotations.
- ◆ We expect medically underwritten buy-in pricing to remain highly competitive during 2015, but to increase into 2016 as pension scheme demand grows further. This means pension schemes have a window of opportunity during 2015.
- ◆ The medically underwritten buy-in market will continue to be dominated by 'top sliced' transactions. These top sliced transactions are becoming increasingly popular with larger pension schemes and, given the attractive pricing, we expect this trend to continue. The largest deal in 2014 was a £206m 'top sliced' buy-in with Partnership covering the largest individual liabilities in a multi-billion pound scheme.
- ◆ Average deal sizes more than tripled from 2013 (£7m) to 2014 (£27m) and we fully expect this trend to continue in 2015 as more larger pension schemes recognise the significant benefits of medically underwritten buy-ins.
- ◆ We expect medically underwritten buy-ins to represent around 10% of all buy-ins (by value) during 2015.
- ◆ 2014 saw the first medically underwritten buy-out covering deferred members, as well as pensioners and we expect to see further medically underwritten buy-outs in 2015.

Figure 2 –medically underwritten buy-in transaction values, by quarter:





For all these case studies, prices were close to Technical Provisions reserves (in some case cheaper) and close to 10% cheaper than traditional buy-in pricing.”

Medically underwritten buy-in – case studies

	1	2	3	4	5
Scheme size	£150m	£200m	£120m	£150m	£150m
Number of pensioners covered by “top slice” buy-in	18 (average liability of £1.2m)	20 (average liability of £1.2m)	34 (average liability of £0.6m)	50 (average liability of £0.65m)	40 (average liability of £0.8m)
Buy-in transaction date	Sep 2013	Feb 2014	Dec 2014	Dec 2014	Mar 2015
Assets exchanged for buy-in	Gilts and corporate bonds	Corporate bonds and cash	Gilts	Gilts and corporate bonds	Gilts and cash
Price	Prices were all close to Technical Provisions reserves (in some case cheaper) and close to 10% cheaper than traditional buy-in pricing. On average, equivalent to an implied return of gilts + 0.3% p.a.				
Positive impacts for the pension schemes	<ul style="list-style-type: none"> Removed significant concentration of risk associated with highest individual pensioner liabilities; Exchanged broad matching assets for a perfect matching asset, including protecting against life expectancy and proportion married risk <p>All without any need to increase company contributions.</p> <p>In fact, in several of these cases, the scheme’s overall best estimate asset returns actually increased, despite the material risk reduction.</p>				



The Trustee is delighted to have been able to manage its Fund’s concentration of risk with this tailored and cost effective solution. Hymans Robertson’s impressive process, Club Vita’s market leading longevity analysis and the insurance company’s competitive price has allowed the Fund to remove this risk at a cost close to our technical provisions reserves – a great outcome for everyone associated with the Fund.”

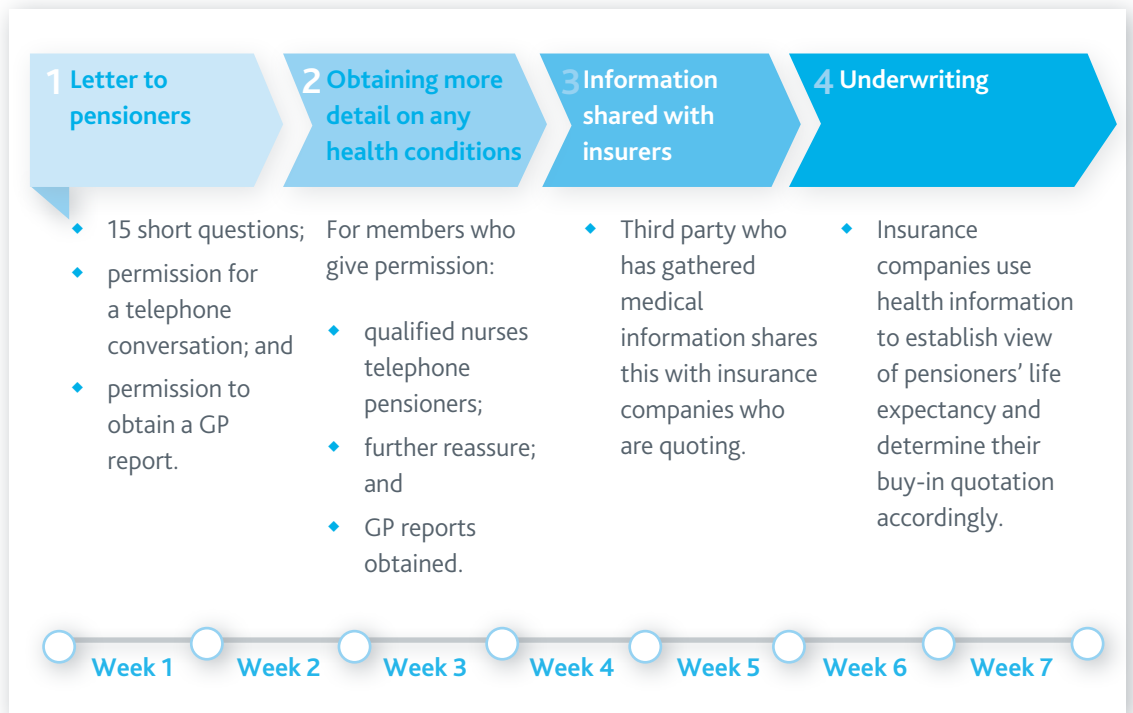


Many thanks for this good news and for all the help you have given to the Trustees to enable this investment to be made. It went very smoothly from our point of view.”



Many thanks to the Hymans team. Very efficient.”

How the health data gathering process works



- ◆ 15 short questions; permission for a telephone conversation; and
- ◆ permission to obtain a GP report.
- ◆ For members who give permission:
 - ◆ qualified nurses telephone pensioners;
 - ◆ further reassurance; and
 - ◆ GP reports obtained.
- ◆ Third party who has gathered medical information shares this with insurance companies who are quoting.
- ◆ Insurance companies use health information to establish view of pensioners' life expectancy and determine their buy-in quotation accordingly.

- ◆ To some peoples' surprise, our experience is that most pensioners are happy to actively help with the data gathering process, provided that it's well communicated;
- ◆ We typically see pensioner response rates of between 70% and 80%;
- ◆ This is great news for pension schemes as it provides the insurance companies with a lot of additional information about the risks they are taking on, which allows the insurers to remove unnecessary prudency margins (which are needed when there's more uncertainty) and so provide the most competitive pricing; and
- ◆ Pensioner feedback on the data gathering process has consistently been positive.



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If you would like to discuss this quarterly update in more detail please contact your usual Hymans Robertson contact or:



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