Bulk annuity briefing, Quarter 2 2024

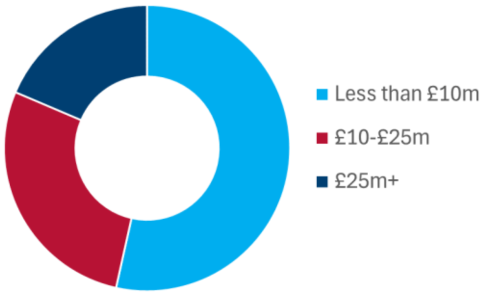
In this briefing, we look back on a busy year so far for First Actuarial's risk transfer team, and provide three recent mini-case studies. We also discuss the latest update to the First Actuarial Bulk Annuity Index, which monitors pricing trends in bulk annuity transactions relative to self-sufficiency liabilities.

A milestone for First Actuarial

In our last update, we announced that our risk transfer team has now led on more than 40 transactions, settling c.£500m of liabilities.

At First Actuarial we understand the complexities and nuances of the sub-£100m market. Take a look at our track record:

Proportion of First Actuarial-led transactions by size



Market update

Smaller schemes continue to hit the headlines as one of the fastest-growing market sectors.

Concerns over capacity (in particular during the buy-in to buy-out phase) are balanced by optimism regarding recent new entrants M&G and Royal London. Utmost and Brookfield are also expected to officially enter the UK bulk annuity market in the coming months.

While financial capital appears readily available where required, what remains unclear is how easily human capital will be acquired by new and existing insurers.

Case study 1

The challenge: The trustees of a scheme with an existing insurer relationship were keen to buy-in with that insurer. However, the scheme benefits did not fit the insurer's streamlined template.

The solution: *"Working closely with the scheme's legal adviser and the Scheme Actuary, we reviewed the areas where the scheme benefits didn't match the template. For example, certain membership categories varied in their ill-health benefit entitlements. Our solution harmonised this and other benefit complexities, so the transaction could go ahead without disadvantaging members."*

Declan Keohane, Head of Risk Transfer

Case study 2

The challenge: A small scheme faced uncertainty over its solvency position due to its size.

The solution: *"We arranged for an indicative quotation to be provided by an insurer, and helped the trustee and sponsor understand what this meant for them. Once all stakeholders were comfortable, we helped the scheme get 'buy-out ready'. The transaction went ahead without the need for additional employer contributions."*

Steve Higginbottom, Senior Risk Transfer Consultant

Case study 3

The challenge: A buy-in was jeopardised when an important deed which influenced pension increase rates couldn't be located.

The solution: *"The missing deed could have derailed the entire project at the eleventh hour. However, we negotiated with the insurers and arranged for the potential additional premium value to be carved out of the contract's 'material change' clause. This gave the trustees and sponsor the time required to assess the potential financial impact of the missing deed, and the breathing space either to locate it or adjust members' benefits."*

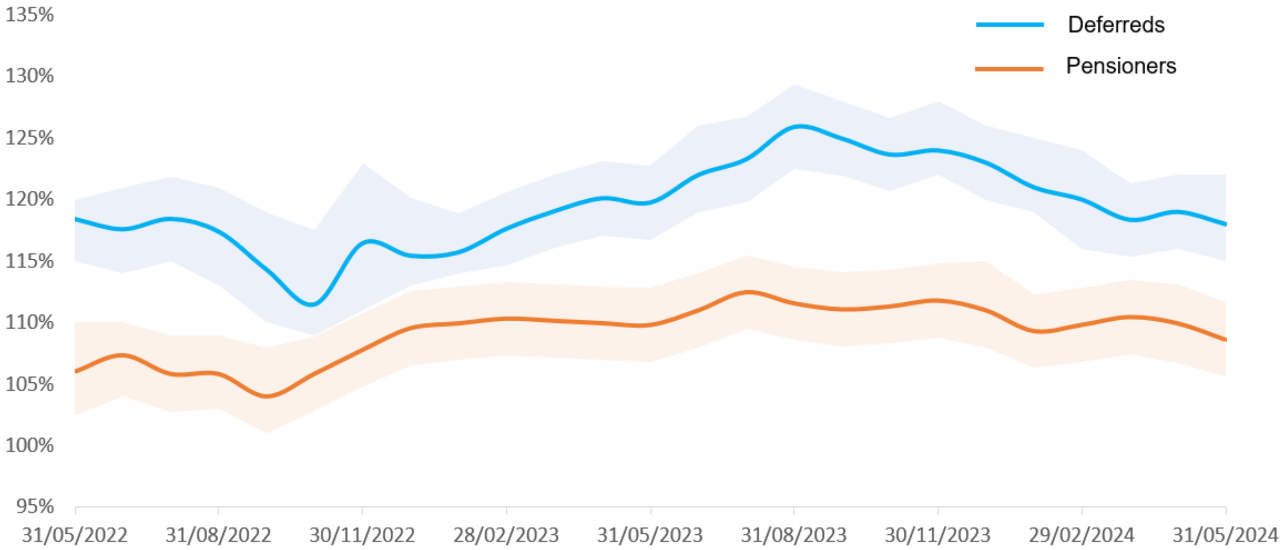
Phil Kelly, Senior Risk Transfer Consultant

First Actuarial Bulk Annuity Index

The chart below shows the average price of a £50 million bulk annuity transaction (with a mixture of fixed and inflation-linked liabilities) as a percentage of the liabilities measured on a self-sufficiency basis, using a discount rate of 0.5% pa above gilt yields.

The solid lines represent our estimate of the average price relative to self-sufficiency liabilities. The shaded area shows the range of sample pricing received from different insurers.

First Actuarial Bulk Annuity Index (£50 million transaction) – Pricing relative to self-sufficiency liabilities



Insurers charge a higher premium for deferred members than for pensioners of the same age. This is because it's harder to predict the benefit outlay. Deferred members are entitled to exercise options around when to retire and whether to take part of their benefits as a tax-free cash lump sum. For many schemes, the cost of a full buy-out can be prohibitive. But generally, as schemes mature and approach a self-sufficiency target, the extra funding required to reach buy-out decreases.

The increase in gilt yields has materially reduced the cost of buy-out and increased demand. However, buy-out pricing is also affected by other variables such as credit spreads, competition, insurer capacity and reinsurance pricing. The net effect of changes to these other variables has been to increase the cost of buy-out relative to gilts-based liabilities over the last 18 months. Towards the start of 2024, an increased appetite for schemes at the smaller end of the market led to a slight weakening of insurer pricing relative to self-sufficiency liabilities.

As at 31 May 2024, we estimate that the average price of a bulk annuity covering pensioners will be 9% higher than the equivalent self-sufficiency liabilities. In other words, for a scheme that is 100% funded on a typical self-sufficiency basis, we estimate that for every £10m of pensioner liabilities, an additional £0.9m of funding will be required. However, for every £10m of deferred liabilities, we estimate an additional £1.8m of funding will be required.

Further information

Over the past 12 months, First Actuarial has helped schemes secure bulk annuities with each of the insurers operating at the smaller end of the market. We believe that we are ideally placed to help smaller schemes under £100m navigate the bulk annuity market.

[Find out more about our risk transfer services]().

To discuss how we can help your scheme with a potential bulk annuity, please contact your usual consultant or [email our risk transfer team]().