Bulk annuity briefing, Quarter 3 2023

In this briefing, we consider activity in the bulk annuity market during the year so far and discuss how the market may develop over the coming years.

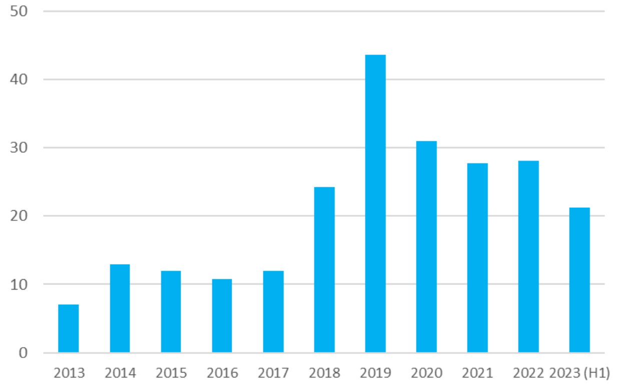
We also take a look at the latest update to the First Actuarial Bulk Annuity Index, which monitors pricing trends in bulk annuity transactions relative to self-sufficiency liabilities.

The story of 2023… so far!

With higher gilt yields forecast to be here to stay, many schemes have capitalised on the opportunity, and de-risked through the use of insurance.

Transactions for the first half of 2023 – totalling over £21bn – have set the stage for a potentially record-breaking year. As the weeks roll by, the question on our consultants' minds is: will this be the year that the market hits £50bn?

Total value of bulk annuity transactions (£bn)



New entrants…

M&G, via its wholly-owned subsidiary Prudential, announced its re-entry into the market with two deals totalling over £600m. Initially, M&G is likely to consider 'mid-market' schemes – particularly those where they can use their investment expertise to offer innovative solutions to issues like illiquid assets.

Elsewhere in the market, Canada Life, previously a pensioner-only insurer, has completed its first full scheme buy-in with a £58m transaction. They continue to have an appetite for smaller schemes.

… and leavers

After three unsuccessful attempts to complete the regulatory authorisation process, The Pension SuperFund, one of the proposed new consolidator vehicles, has been 'mothballed'.

Clara-Pensions, currently the only consolidator to have completed The Pension Regulator's assessment process, announced its first transaction in November. The £590m transaction aims to secure a full buy-out with an insurer in the next five to ten years.

Smaller schemes

Aviva, Legal & General and Just continue to write the most deals for smaller schemes.

For some time now, exclusivity has been a common pre-condition for the smallest schemes. This is set to continue, with a marked increase in the minimum deal size for which insurers will consider quoting competitively.

With the arrival of new entrant Canada Life, smaller schemes that have worked with their advisers to maximise their attractiveness can expect to have a wider choice of insurer.

Looking forward

Industry expectations for 2023 range from around £45bn to £55bn. Whether actual figures reach the top of this range will depend on whether several 'mega-transactions' expected over the coming months fall into the current year.

Also in the pipeline are potential new insurers – several new entrants are expected to announce their propositions in 2024. What this means for smaller schemes remains to be seen; it's not yet known which areas of the market these insurers will target.

First Actuarial expands its risk transfer team

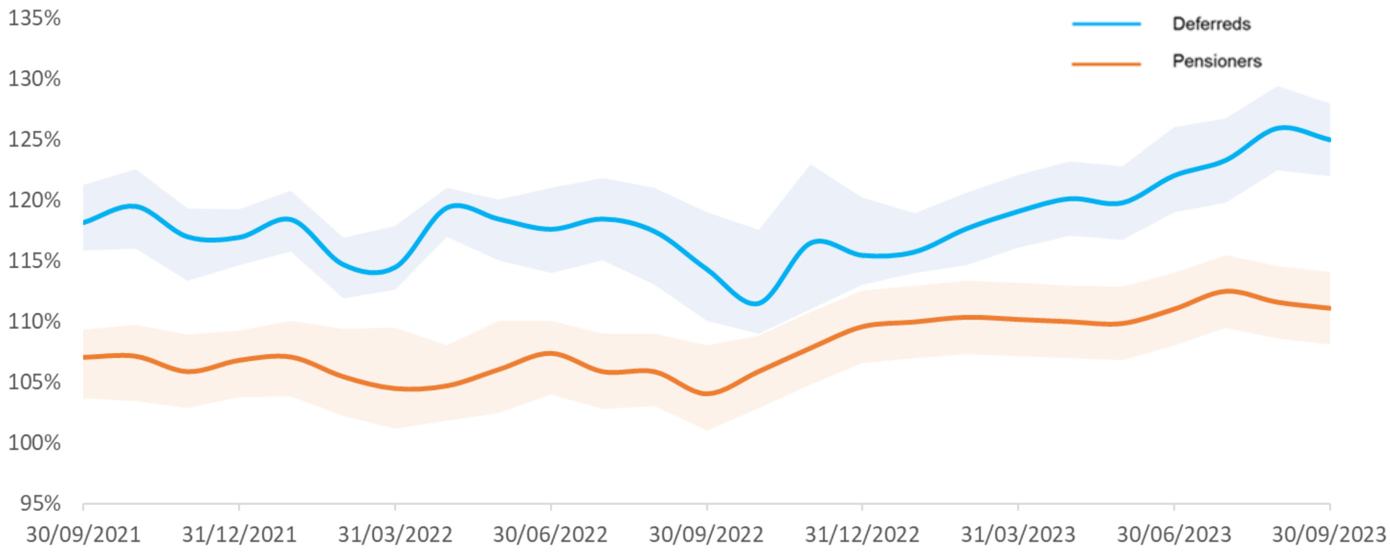
Reacting to our clients' needs, at First Actuarial we've expanded our risk transfer team – by recruiting externally and also drawing on our existing talent.

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 in these other variables has been to increase the cost of buy-out relative to gilts-based liabilities over the last 12 months.

As at 30 September 2023, we estimate that the average price of a bulk annuity covering pensioners will be 11% 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 £10 million of pensioner liabilities, an additional £1.1m of funding will be required. However, for every £10 million of deferred liabilities, we estimate an additional £2.5m 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 **First Actuarial's 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**.

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