2016 in reflection: solvency, sovereignty and solutions

Frankie Borrell reviews the developments that have occurred in the bulk annuities market throughout 2016

A quiet year in the pensions bulk annuity market is a rare thing and 2016 was in no mood to dial down the volume. The year started with the much-anticipated introduction of Solvency II, a piece of legislation almost 15 years in the making. We saw the de-risking landscape evolve: one insurer withdrawing, two settling in and a further two merging. The seven active providers drove innovation to meet the needs of an ever-more sophisticated market place. And of course, all of this was set against the backdrop of an unsettled political environment, not least the UK voting to leave the EU.

A new regulatory framework

Whilst Solvency II held the promise of an even more robust framework for trustees, the potential for higher premiums – in particular for deferred pensioners – was a hot topic in 2015. As such, we saw many schemes accelerate their de-risking plans ahead of the new regulations coming into force. Some £5.4 billion of business was written in the last quarter of 2015, the largest quarterly volume ever recorded in the UK.

Concerns around the impact on premiums have ultimately proved unfounded, with attractive pricing levels retained across 2016. Moreover, full scheme buyouts – including deferred pensioners – have been a regular fixture. One consequence of Solvency II though has been greater pricing variation transaction-to-transaction between insurers. This has reinforced the need for trustees to be well advised, well prepared and nimble.

An evolving supply side

In the 30 years since Legal & General entered the bulk annuity market the supply side has evolved considerably. A healthy level of competition has been maintained across 2016, with seven insurers driving value for trustees and their corporate sponsors. With contracts often running for upwards of 50 years, trustees are naturally keen to understand their chosen counterparty's commitment to the market.

Solvency II's reverberations also drove another theme of 2016: non-active providers looking to offload their annuity back books. Whilst this does bring additional competition for trustees when seeking to attract insurers' best terms, we believe that this demonstrates that overall market capacity could soon reach up to £20 billion a year.

Quality over quantity

The significant flurry of business written at the end of last year meant that demand was slower in early 2016, but this began to pick up considerably as the year went on and despite the market volatility following the EU referendum in June.

This year has seen several headline-grabbing transactions, not least the £1.1 billion buyout between Legal & General and the Vickers Group Pension scheme, and a further five buy-ins from the ICI Pension Fund totalling £2.7 billion. The ICI transactions leveraged the fund's umbrella contract structure, allowing quick and streamlined transactions, a framework that's expected to become a blueprint for schemes of all sizes.

Macroeconomic driven opportunities

The UK's vote to leave the EU and last month's US election has driven volatile financial markets. Well-prepared schemes that are able to move swiftly have found that market fluctuations often create opportunities to secure favourable pricing. This serves to highlight the importance of robust yet agile governance, and the rewards to be had if schemes can be manoeuvred into a transaction-ready position. The second half of this year has also seen many trustee boards with overseas parents move quickly to explore locking into favourable terms supported by the depreciation of sterling.

Looking ahead to 2017

So what do the next 12 months hold?

A key theme that has emerged and is expected to develop in 2017 is one of increasingly examining what sits behind an insurer's price. There is a growing focus from trustees' on the variation between insurers in the areas of flexibility, innovation, service standards and perhaps most importantly financial strength.

We anticipate innovation accelerating to further meet need. One such example is the development of solutions to better cater for underfunded schemes. The days of a one-size-fits-all solution are long gone; insurers are looking to evolve their offering to meet the unique circumstances of each scheme.

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