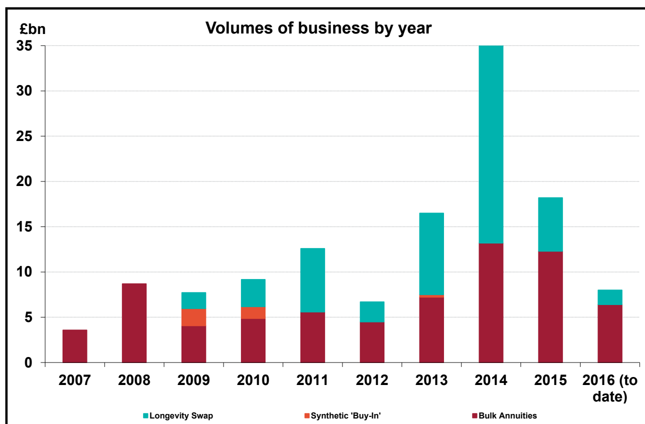
**Summary**
• The bulk annuity transfer market had a quiet start to 2016 due to the introduction of Solvency II regulation for insurers and political uncertainty.
• The second half of the year has seen an upswing in the number of deals, attributed to Brexit uncertainty and for some, improved funding positions thanks to favourable asset holdings post-Brexit market volatility.
• For trustees who are looking to enter a bulk annuity contract with an insurer, it is recommended that they are thoroughly prepared in advance and are ready to act quickly when pricing looks attractive.

**Louise Farrand explains why, following a slow start to the year, the bulk annuity market is starting to pick up pace**

You could call it the calm before the storm. On the whole, the bulk annuity transfer market had a quiet start to 2016. However, the word among insurers and consultants is that despite recent enormous political uncertainty and regulatory change, activity in the second half of the year is picking up. Trustees who are looking to pass on their defined benefit pension scheme liabilities are proceeding undeterred with buy-ins and buyouts.

Perhaps a slight lull at the start of 2016 was inevitable. With Britain's referendum on membership of the European Union on the horizon, it's no great surprise that some trustee boards preferred to watch and wait. Meanwhile, EU regulation in the form of the Solvency II introduced more stringent capital requirement for insurers, leading many industry commentators to predict that bulk annuity transfers would get more expensive for schemes.

That said, a quiet start to the year is quite common, as Willis Towers Watson observed in an August briefing note. In March 2016, the same consultancy projected that around £12 billion of liabilities would be transferred to insurers over the course of the year. When *Pensions Age* asked them to revisit their projection in November 2016, they revised this sharply downwards to £9 billion. Pension Insurance Corporation head of business origination Jay Shah estimates a similar figure of £8-9 billion.




Graph supplied by Willis Towers Watson

If Willis Towers Watson and Shah's predictions come to pass, it would mean that 2016 would not hit the highs of 2015 and 2014, but it would be a steady year for insurers *[see graph]*.

Not every insurer saw a lull at the start of 2016. "It hasn't been quiet for us," qualifies Shah. "I think it was quieter in the market in the first half of the year, for two reasons: Solvency II was going to be implemented and there was uncertainty as to what that might mean for pricing in 2016. A lot of the transactions that would normally have happened in the first quarter were accelerated into 2015. We saw a bit of a rush in the final quarter of last year and saw a little bit of a lull in the first quarter of this year. In the second quarter, some decisions were put off ahead of the referendum vote."

Legal & General's director of strategic transactions within its pension risk transfer business, Ashu Bhargava, says: "It was a quiet start, but as the year has progressed, insurers have become much more confident. At Legal and General, we have written £5.8 billion of *[bulk annuity]* premiums. Even though there have been tough circumstances because of Solvency II and uncertainty in the market because of political events, there are opportunities. Where trustees are prepared, and have the governance to take advantage of opportunities, they are available. Trustees who are ready are able to transact."

**Ready, steady, go**

Sometimes, uncertainty causes paralysis. Conversely, political uncertainty has been spurring trustees and scheme sponsors on, reports JLT Employee Benefits head of buyout Tiziana Perrella. "I don't think that trustees feel they can afford to take risks. The more uncertainty

there is, the more they feel they must hedge their exposure. We are seeing an acknowledgment that if you can pay your full liabilities you should do so. It just becomes difficult to assess the right time and value for money. The discussion is around that, rather than about whether it is the right thing to do. It's a matter of timing."

Both Willis Towers Watson and JLT Employee Benefits, consultants with a broad perspective on market happenings, report an uptick in activity, the former noting that following Brexit: "We are still seeing considerable activity in the market, including advising on several transactions that have completed in recent weeks."

Further fuelling the fire is the fact that politically-induced market volatility hasn't been bad for every scheme. Perrella says: "After Brexit, prices did go up but depending on whether you had the right assets, you might find your position as a scheme has not worsened, and may even have actually improved. It's about what assets you've got, what positions you have and where your sponsor is located. Sponsors with foreign parents have seen that the depreciation of sterling has been positive for them."

Bhargava agrees: "There's a lot of doom and gloom around the aggregate size of deficits, but within that aggregate, there are schemes that are better funded and schemes that are worse funded."

Schemes who held certain assets will have seen improvements in their funding in the aftermath of Brexit. For instance, gilts rose in value after the vote.

Meanwhile, Brexit has affirmed the likelihood that interest rates are likely to stay lower for longer. "Trustees and sponsors are accepting there isn't going to be a miracle solution to deficits. Low interest rates are here to stay and it is going to be quite difficult to earn your way out of deficits. There is a greater propensity to accept that pension schemes have to be de-risked. If a cheque has to be written, it has to be written," says Shah.

**Two new de-risking trends**

**1. The incremental buy-in**

In the past, most trustees took the view that if they weren't well-funded enough to enter a buyout, they wouldn't look at insurance transactions. There has been a huge move away from that, according to Legal & General's Ashu Bhargava. "It's not about getting fully funded before doing an insurance transaction. Now, it's about looking for opportunities in the market, taking advantage and de-risking incrementally. That's a huge trend. It's easier to get value for a smaller transaction than one that is 10 times the size. When opportunities present themselves, you can transact quite quickly."

To facilitate incremental buy-ins, trustees are signing master contracts with insurance companies, which then only need a couple of extra pages of legal details added when they are ready to de-risk another tranche of scheme liabilities, adds Bhargava.

**2. Deferred payment structures**

A little-known guarantee that schemes can agree with an insurer, JLT Employee Benefits' Tiziana Perrella is surprised that deferred payment structures are not more popular. "Effectively, you fix the terms *[with an insurer]* now; you pay a proportion of the premium, and pay the rest over a period of time. It's like a recovery plan but you know at the end of it you will be rid of the scheme," she explains. "If I were a sponsor, at the least I would want to know what that figure is. By paying an agreed sum plus a 10-15 per cent premium on top, the sponsor has certainty."

She continues: "An even better idea is, if you have good credit lines, to borrow from your bank, wind up straight away, and save yourself 10 years of accounting fees, Pension Protection Fund levy, and extra management time. We have had a few cases that have transacted on this basis – but I am surprised that more sponsors haven't investigated."

**Time to act**

For trustees who are looking to enter a bulk annuity contract with an insurer, the first thing to do is to get ready to move quickly when pricing looks attractive.

"There is always good day pricing but if you are not in the market, you can't take advantage of it. Equally, you can't go to the market unprepared," says Perrella. "For smaller schemes especially, they have to make themselves as attractive as possible. There are various aspects to it – data work, legal work, evidence you have had conversations with the sponsor, and potentially a very robust trigger. You don't need a lot of good quotes to transact, you just need one good quote. We don't have a problem with approaching one insurer if we know they are interested in a particular type of scheme of a specific size."

There's good news for schemes. Changing dynamics in the insurance market mean they are competing harder for business. "There has been some jostling for positioning. The market has been quite dynamic and there is quite a lot of competition," says Shah.

This is certainly backed up anecdotally by Perrella: "Some insurers are not making as much business and they are proactively approaching us to say, 'we have good pricing if you are ready to transact now'. I am having quotations turned around in two weeks from some insurers – but that is for schemes that have done all the preparation. I am waiting to do between four and nine transactions by mid-December."

With insurers and consultants predicting a flurry of transactions before the end of the year, the calm before the storm is truly over for insurers, schemes and consultants.

**Written by Louise Farrand, a freelance journalist**