Bulk annuities: Sustainable growth

Despite the understandable challenges of 2020, Aviva maintained its focus on investing responsibly within its bulk annuity portfolio, leaving it well placed to drive the agenda in 2021

The bulk annuity market has remained surprisingly resilient to the turmoil of the past year. While the 'jumbo deals' that characterised the market in 2019 did not appear for 2020, the market continued to grow in line with the underlying trend and will likely reach £28 billion by the end of the year.

Aviva has been very active throughout 2020, having written £5 billion of bulk annuities by the end of Q3, compared to £2.1 billion in the same period last year. "We continue to support schemes of all sizes and needs with their de-risking ambitions – with the largest completed transactions being over £1 billion and the smallest being under £5 million", Aviva annuity asset origination director, Marcus Mollan, says.

According to Mollan, 2020 has been an interesting year for investment markets. The year started with relatively low yields, tight credit spreads and equity highs, and the end of the year looked much the same. But that's only half the story.

"If you just looked at market conditions at the beginning and end it would look like a very boring year, but between March-May we saw equities falling, spreads widening, and consumer behaviour dramatically changing.

"This created a brief period where investors such as insurers and pension schemes could take advantage of very attractive investment opportunities. This rewarded schemes that had been invested conservatively and were able to move quickly to adjust their investment portfolios or to execute an annuity transaction," he explains.

Just as the volatile market conditions provided opportunities for nimble investors, they also brought the sustainability of investments more sharply into focus.

"At a macro level, the experience of Covid-19 focused everyone's minds on the delicate state of the world," Mollan says. "Far more investors have now recognised that we are seeing dramatic changes in climate, and that such changes will have significant market implications.

"Investment markets have always looked ahead of what's happening in the real world, aiming to predict what's coming next and trying to price that in. The markets have recognised there is a real and emerging dynamic. Environmental, social and governance (ESG) issues will be the most pressing topic on investors' agendas to respond to once we are past the current Covid-19 crisis."

Having been actively prioritising ESG investments for many years, Aviva has long been at the forefront of responsible investing, and it intends to remain so even as others wake to it and competition for assets increases.

At the start of the year, prior to the pandemic really taking hold, Mollan explains, Aviva had completed a significant volume of annuity transactions and had money available and ready to invest. The private asset market was significantly quieter than normal and in response Aviva switched focus to public assets, particularly finding good opportunities in US corporate bonds.

The second half of the year saw a real change, with private asset markets being much more active. "There was a thawing of the market and a lot of opportunities that had been put on hold came back to life, many of them with a green or sustainability focus," Mollan explains.

Notable 2020 examples include, in May, Aviva announced it had supported a UK renewable energy project with a £131 million loan to finance offshore transmission assets for a wind farm off the Suffolk Coast.

Each year, the Galloper Offshore Wind Farm's 56 turbines generate enough green electricity to power the equivalent of more than 380,000 British homes.

Its financing of the Galloper deal builds on Aviva's existing portfolio of offshore wind assets and renewable energy investments, having provided £400 million to help fund the construction of the world's largest offshore windfarm, Hornsea 1, in 2018.

Real estate opportunities also figured within Aviva's responsible investing deals in 2020, with the company investing £35 million in debt financing in April to support the Big Yellow self-storage company, and £154 million in debt financing for CLS Holdings, a property investment company, in September.

As part of the Big Yellow financing, Aviva included a green clause in the transaction subject to the sponsor installing solar panels on additional security properties, as it expects the addition of solar panels to result in an even lower-emission portfolio, whilst reducing ongoing running costs of the underlying assets. The CLS transaction also embedded sustainability-linked incentives.

In July, Aviva also entered into a £60 million corporate debt facility for a not-for-profit housing association, Coastal Housing Group, which has 6,000 homes under management in South Wales. Coastal will use the proceeds from the financing, the largest it has undertaken to date, to secure its long-term business plans by expanding its operations and delivering additional housing across a range of tenures.

The following month, Aviva also completed a £75 million private placement with Settle, the not-for-profit housing association that manages over 9,000 properties across Bedfordshire and Hertfordshire. This facility will help Settle in advancing its environmental, social and governance agenda, including the commitment for all properties to meet 'EPC C' standards or better by 2025.

The financing will also help the group meet its 2024 goal of at least 1,500 new homes, including a targeted focus on shared ownership to meet the current supply shortage of affordable homes in the region.

Aviva was able to lean on the £47.3 billion Real Assets business of Aviva Investors to access these markets, drawing on its expertise across the infrastructure, real estate and private debt markets to assess opportunities that could meet long-term investment objectives.

Looking forward, while the first half of the year is usually a quieter time for private asset investments, the backlog from 2020 will likely result in a busier H1 for 2021 than would be the norm, meaning there should be plenty more deals to see this year.

The focus on ESG will also certainly continue through 2021 and well beyond for Aviva, its shareholders and its customers, as Covid-19 has made people even more aware of the need to address climate change.

Thanks to the amazing work done to develop and roll out vaccines, we're hopefully turning the corner on the Covid-19 health crisis.

"In contrast", adds Mollan, "the challenges facing our society on climate change are an order of magnitude greater. The world hasn't been as swift to embrace this challenge, but that's changing. We're starting to see significant movement at a policy level and renewed focus on climate change in the US.

"Aviva will continue to lead from the front, as responsible investing is in our DNA. It's central to all our annuity asset investment decisions and as our annuity business continues to grow, we have the incentive and leverage to make a positive difference for our annuity customers and for future generations."

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Aviva annuity asset origination director, Marcus Mollan

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