Summary
• The bulk annuity markets have seen record volumes in recent years as schemes seek to de-risk.
• Some question, however, whether this will continue.
• Funds looking to be bought out should look for, and minimise, the gaps in their data.

Coming along nicely

Bulk annuity transactions have hit record levels in recent years. Peter Carvill asks whether the trend will continue and what schemes can do to look more attractive to insurers

The bulk annuities market has seen tremendous growth in recent years. Last year, according to figures from Barnett Waddingham, the market for buy-in and buyout transactions exceeded £24 billion. That comes after annual volumes over previous years that had hovered between £10 billion and £13 billion.

The outlook for this year appears equally rosy. In December 2018, Willis Towers Watson predicted that the number of deals involving bulk annuities would be up to £30 billion in 2019, with longevity swaps set to double to over £10 billion. And as JLT's *Buyout Market Watch* stated in March: "We expect 2019 to be at least as busy."

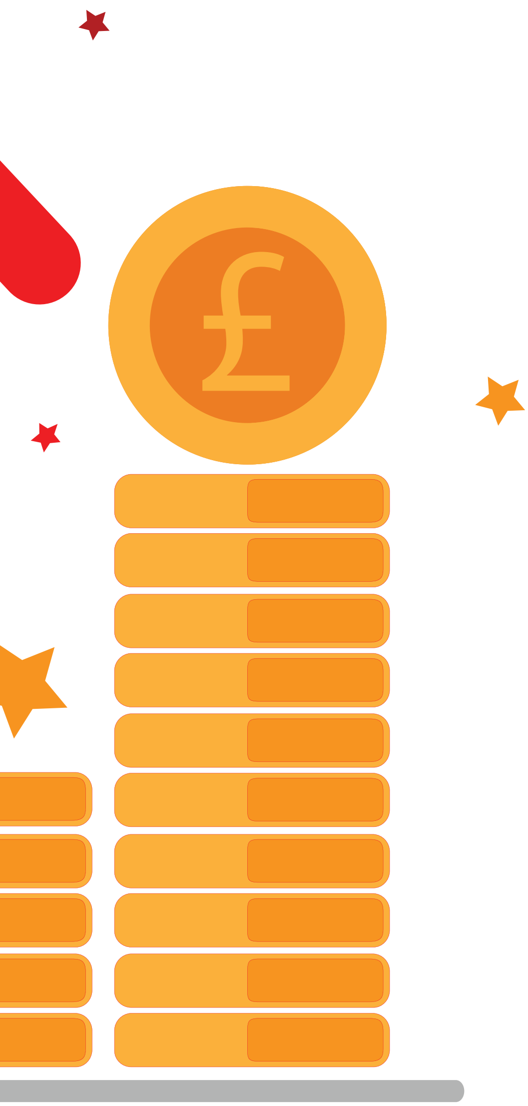
Buyout Market Watch outlines three reasons for this. The first is the competition between eight insurers, alongside the 'most-attractive' pricing seen in 10 years, aligned with a strong trend from trustees and sponsors for de-risking, improved funding levels, and the rapidly ageing demographics of scheme members.

The market appears to be remaining strong. According to figures from JLT, there have been 80 buy-in, buyout, or longevity swap transactions over 2018 and 2019 (50 buy-in, 22 buyout, eight longevity swap). And as this article was being written in mid-August, we were seeing buy-in transactions involving Cadbury Mondelez Pension Fund and British American Tobacco for sums involving £520 million and £3.4 billion, a buyout of PGL Pension Scheme by Phoenix for £1.1 billion, and a longevity swap for HSBC Bank (UK) Pension Scheme by Prudential Insurance Company of America for £7 billion.

Mercer's partner for risk transfer Suthan Rajagopalan says that the company is "definitely confident that the market will reach £30 billion in 2019". He adds: "I don't think it'll be double or treble, but we're looking at £20-30 billion on a bulk annuity basis. In terms of longevity swaps, it will be a multiple of last year, say £5-10 billion."

Others believe it could surpass the £30 billion figure. Aon's senior partner and head of risk settlement Martin Bird says there had been internal debates of whether the market would go beyond £40 billion this year due to the number of large schemes and projects that are in play. He refers specifically to the Rolls-Royce deal, valued at £4.6 billion, that was announced in June. "It only takes one or two deals like that. I don't like to speculate, but we think the right number is over £35 billion. But £40 billion wouldn't surprise me."

However, others are more sanguine and feel that what we are seeing is merely a blip in the market. In this camp are Willis Towers Watson's senior director Shelly Beard. She doubts that the current pattern is one that will be sustained. "Firstly, there's a lot of large transactions at the moment. The ability to do that is due to a fall in life expectancy and a positive equities market. This means funds have better funding positions than they expected. They're taking the opportunity to complete transactions. I think it's a one-off bulge, for want of a better term."



Market trends

With such movements, the industry is seeing, in some respects, its limitations. Anecdotal evidence suggests that there is a limit to the capacity of insurers to handle the amount of new transactions. In fact, says Bird, this is the biggest trend in the market.

He explains: "It's not that the insurers have limited bandwidth in terms of the balance sheet. It's the human bandwidth needed to process that work. The whole market is struggling a little bit there, and it's been a limiting factor this year."

Another trend in the market has been a predicted increase in longevity swaps. In December, Willis Towers Watson predicted that the £5 billion in this product in 2018 would double the next year.

This surge may be driven by a stagnation in UK life expectancy improvements. Office for National Statistics figures show that male life expectancy rose from 78.91 years between 2011-2013 to 79.07 between 2012-2014, and continued to rise very gradually in the following periods from 79.09 years to 79.17 years to 79.18. For the female population, these numbers began at 82.71, rising then to 82.81, 82.82, 82.86, and then remaining at that value for 2015-17.

Rajagopalan says: "Some schemes have an inherent level of longevity risk because they have higher pensions and more affluent people who are going to live longer. We saw improvement rates in longevity tail off between 2016 and 2018. There's been no improvement on a national level, which led to a deprioritising in thinking about longevity swaps. This year, we've seen a turnaround – a 4 per cent improvement. This may just be a blip or a turn in the market, and it may lead to a resurgence."

Rajagopalan says that the driving factors in 2019 have been improved data governance and simplified transactions. This is backed up by Mercer's *Pension Risk Transfer Market Watch*, published in July. There, the company's head of UK bulk annuities David Ellis wrote: "Getting your house in order (data, assets, and governance are good examples) before you go to market has always been good advice, especially where your potential counterparties are busier than ever."

As Bird notes, it takes only one or two big deals to boost the numbers and it is not uncommon now for the industry to see large deals valued in the billions. In previous years, these types of deals had been much smaller. But since last year, we have seen deals (the aforementioned British American Tobacco and Rolls Royce, plus the Airways Pension Scheme, a transaction of £4.4 billion with L&G; the Dresdner Kleinwort Pension Plan, £1.2 billion with PIC; and Rentokil Initial, £1.5 billion with PIC) that would have been the exception a few years ago.

As Beard puts it: "People thought once that some deals were too big, but insurers are now more comfortable with them." She adds: "In the context of what's going on, £500 million is now considered small."

Preparation

While the market seems in good shape, schemes should not be resting on their laurels. Bird says that there are many things that they can do in order to prepare for a buyout. He says that while they are not exciting, they are crucial.

He explains: "Schemes can get properly prepared by working through their data and understanding the gaps. They're not a problem, but schemes may not have everything there in order to get a buyout price. Pension schemes often don't ask about spouses and their ages. You need to know which benefits you're going to insure. That's usually a lengthy process."

Written by Peter Carvill, a freelance journalist