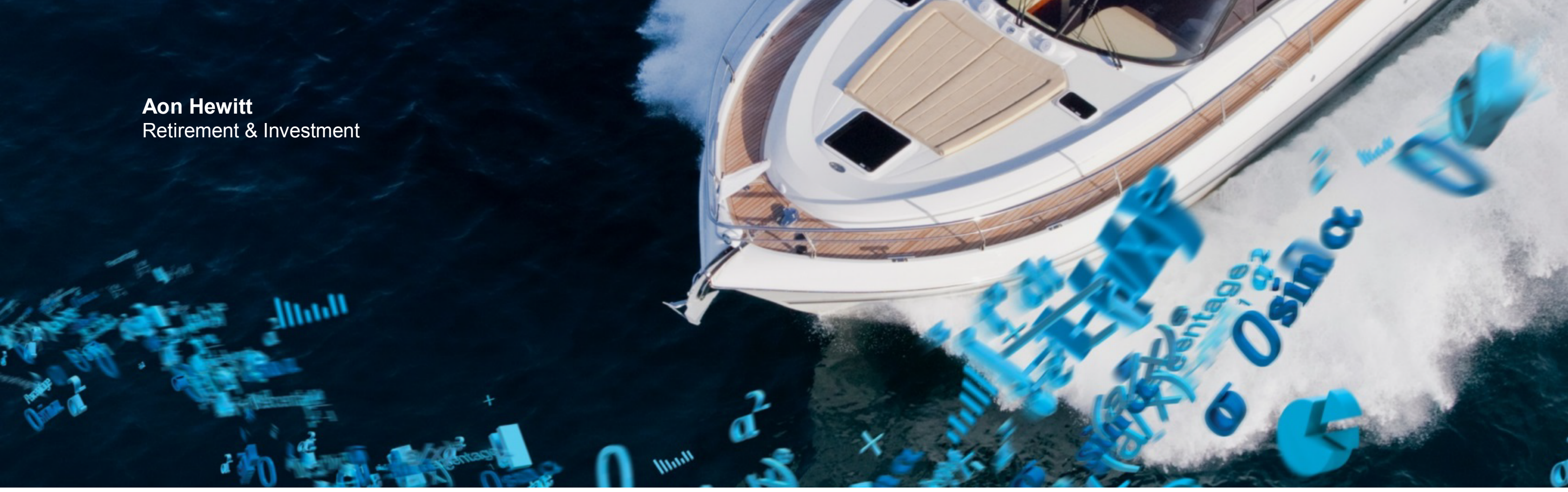


UK Risk Settlement

January 2018

2017 bulk annuity market: the year before the peak

The bulk annuity market ended 2017 in a particularly busy state, with schemes reacting to price improvements witnessed over the course of the year (as reported in previous bulletins) and eight active insurers all seeking to write material business.

We estimate that £12-13bn was placed in 2017, with market leaders PIC and Legal & General so far announcing £6.8bn of business between them, and most other insurers seeking to increase their volumes, most notably Aviva. Unusually there were no individual bulk annuity deals close to or above £1bn, partly reflecting the trend to secure schemes in tranches over time, and partly from the magnitude of price improvements taking buyers by surprise. We estimate that around 75% of deals were pensioner only transactions, with improved scheme funding likely to lead to more buyouts into 2018 and beyond.

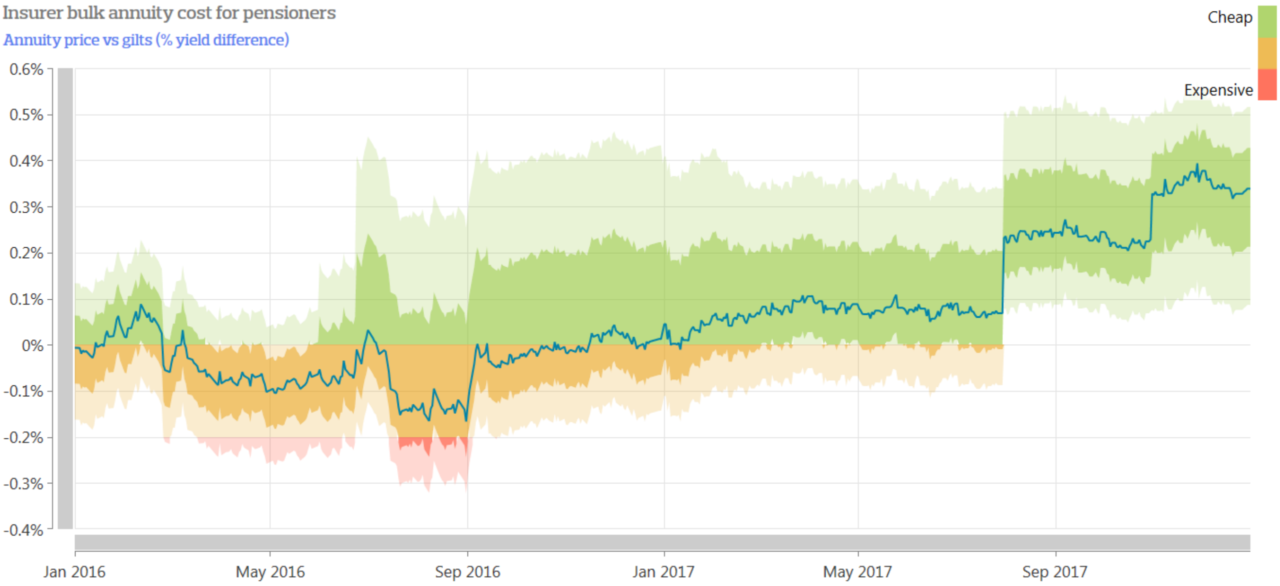
This left spare capacity unused and 2018 is now expected to see record volumes, with annuities from company schemes exceeding £15bn for the first time. There is potential for the total volume including back-book opportunities (notably from the Prudential annuity book) to reach as high as £30bn if all providers' appetite is well sated.

Strong pricing opportunities are continuing to arise, for well-positioned auctions, as the increase in demand has been pre-empted by provider planning to develop their origination teams and asset sourcing for this year.

The graph on the next page illustrates the continuing price opportunity to transfer assets from other low-risk strategies such as gilts, LDI and high-quality corporate debt, and invest in annuities. At current pricing this often gives a materially better yield and considerably enhanced risk-reduction properties, so a significantly improved risk-return trade-off.

The graph on the next page illustrates the typical yield improvement under annuity purchase compared with investing in gilts. In practice the yield gain will be more pronounced than shown in some auctions, when considered on assumptions consistent with the market.

Bulk annuity pricing



How to read this chart

- This shows the return from a bulk annuity for pensioners, relative to the yield on a comparable gilt portfolio
- Annuities shown as 'Cheap' if giving a better return than gilts
- This comparison ignores the material value from annuities giving a better hedge including longevity cover
- Expected pricing for a typical scheme is shown by the blue line
- Best prices typically fall in the darker shading, some auctions fall in the lighter shading. Pricing outside the shading typically represents an unusual liability profile

Chart sourced from Aon's Risk Analyzer

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