For Professional Clients Only

UK Risk Settlement Market Update

October 2022

- £18bn of bulk annuities and longevity swaps disclosed in first half of 2022
- Bulk annuities amounting to £12bn in HY1 reflect a typically quiet start with market gathering pace over HY2
- Expectation that 2022 will be fourth successive year to surpass the £25bn mark for bulk annuities

Building blocks laid for busy end to 2022

In the first half of 2022, the UK bulk annuity market saw £12bn of business written across 78 transactions, marking a strong start to the year. As in most years, a higher volume is expected for the second half, albeit this will be tempered by further yield rises in HY2 which have reduced the value of any individual transactions.

The first half of 2022 still marks a significant step-up from the first half of 2021, when 60 transactions were written covering £7.7bn of liabilities, as the market recovered from the effects of prolonged lock-downs and the resulting economic uncertainty.

A number of transactions in the market are particularly complex in terms of the risks being transferred, which is taking up significant insurer resource. This is influencing short-term case selection, with many insurers seeking to add simpler cases in what remains of 2022.

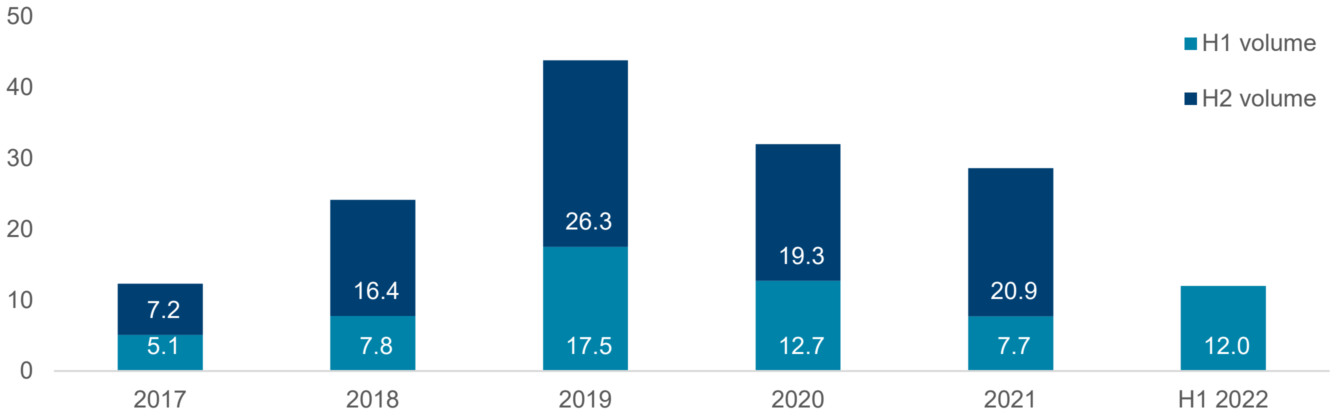
Most new auctions arriving in the market are for full scheme transactions (as opposed, for example, to, a pensioner only buy-in), and 75% of all deals written in the first half of 2022 were full-scheme deals. This has been driven by rising funding levels across schemes as gilt yields continue to rise, noting that the schemes approaching the annuity market still tend to be those that are better funded or more mature.

Funding improvements for schemes reflect positive investment experience overall in 2020-21 and improved annuity pricing, with some schemes able to de-risk and largely lock down their position ahead of the more turbulent stock markets this year.

While pricing is generally at a favourable level compared with the recent past, the continued market volatility can make it harder to capture and so, as ever, the best prepared schemes are most likely to take advantage of attractive pricing.

We expect 2022 to be the fourth year in a row that the market surpasses the £25bn mark for bulk annuities. As mentioned below, recent increases in yields have reduced the pound amount of scheme liabilities and hence annuity deal sizes, which constrains total volumes for 2022. The volatility seen since 23 September could impact transaction volumes to an extent – in particular perhaps pausing some pensioner buy-ins where the level of available assets for de-risking is temporarily more uncertain. It may also (from market yield movements) reduce their values. At present we are expecting most processes to conclude, but in some cases to reset timings.

Bulk annuity volumes split by half year (£bn)



Totals	**£12.3bn**	**£24.2bn**	**£43.8bn**	**£32.0bn**	**£28.6bn**	**£12.0bn**

Source: Aon's Insurer Due Diligence team

Fall in deal sizes from rising yields

Trends across the market in 2022

In the first half of 2022, the average transaction size was c.£150m, compared to c.£180m in 2021. In practice, this average represented a significant number of sub-£100m transactions and a handful of larger deals.

The chart below shows the number of bulk annuity transactions by size, demonstrating the slight uptick in sub-£100m deals so far this year.

We expect that an increased number of smaller transactions will continue to be seen throughout the rest of 2022. As mentioned above, increases in yields have led to a sharp fall in pension scheme liabilities, and a corresponding fall in the size of each bulk annuity deal.

With scheme liabilities, and hence deal sizes, falling, it may be that insurers do not have sufficient human resource to meet their appetite for transactions, increasing expectations for a strong start to 2023.

These factors are likely to be the main headwinds that prevent the market from challenging the record of £43bn set in 2019.

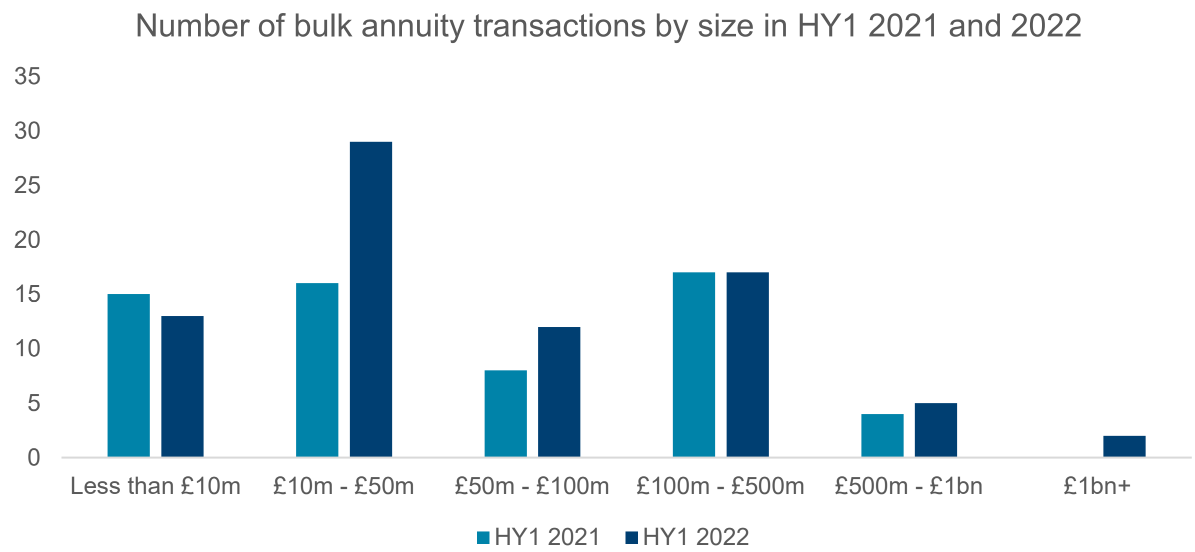
Outlook for 2023

Bulk annuity pricing remains attractive, despite the volatility of the economic environment creating more challenges to locking into a good price.

In 2022, to date, only two transactions in excess of £1bn have been disclosed (amounting to £3.4bn), following four such transactions in 2021 (amounting to £6.6bn).

By contrast, we are aware of a strong pipeline of multi-billion-pound cases either already in or approaching the market and looking to transact in 2023. If these all come to fruition, we expect that next year's market volume will pass the 2019 record.

The increased level of demand could put upward pressure on pricing levels given limited asset availability and insurer resource. However there are also positive headwinds for pricing, including the UK reforms of Solvency II potentially coming into force, although we will have to wait and see the detail to be sure of the impact on the market.



Source: Aon's Insurer Due Diligence team

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Big players continue to dominate

The total volumes and numbers of deals completed by each insurer are summarised in the table below.

Although volumes are led by the five insurers who express the largest appetite, their relative positioning may not be meaningful until the full year data is available, as all of them were working on substantial transactions going into the summer.

Similar to 2021, Legal & General lead the way, having written £3.7bn across 20 transactions – which represents an average deal size of £185m.

Just Group continue to operate at the smaller end of the market, writing 14 transactions covering £588m of liabilities. This gives an average deal size of £42m, the lowest across the market, and showcases Just's flexibility to take on sub-£100m buyouts (with Aviva and L&G the main rivals in that sector).

Scottish Widows and Canada Life have so far focused mainly on pensioner transactions, while building the ability to write other deals.

Deals disclosed for the second half-year include Just Group's largest to date, a £484m full scheme buy-in for Barloworld, and a £1bn Standard Life full-scheme buy-in for WHSmith.

Insurers calm despite financial uncertainty

Insurers have proved resilient to the economically and politically challenging conditions that have developed across the world in 2022, including rising inflation and the impacts of the Ukraine conflict.

Insurer solvency positions have held up, rising this year as a result of improving yields. Insurers are well hedged to changes in inflation and took other protectionary measures to mitigate risks during the pandemic.

Capital supply is hence not a current notable market constraint for annuity providers.

Insurer	H1 2022		H2 2021		H1 2021	
	Deals	Volume (£m)	Deals	Volume (£m)	Deals	Volume (£m)
Legal & General	20	3,715	28	3,275	17	2,965
PIC	10	2,371	13	4,315	1	385
Aviva	18	1,860	23	4,543	22	1,622
Standard Life	6	1,639	5	5,040	2	430
Rothesay	4	1,015	4	1,379	7	1,621
Just Group	14	588	20	1,382	9	553
Scottish Widows	2	430	0	0	1	80
Canada Life	4	343	4	956	1	52
Total	**78**	**11,961**	**97**	**20,890**	**60**	**7,708**

Source: Aon's Insurer Due Diligence team

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Growing competition fuels longevity swap market

In the longevity swap market, 2022 has seen a similar first half to 2021, with £6bn of publicly announced deals, covering two transactions with two reinsurers:

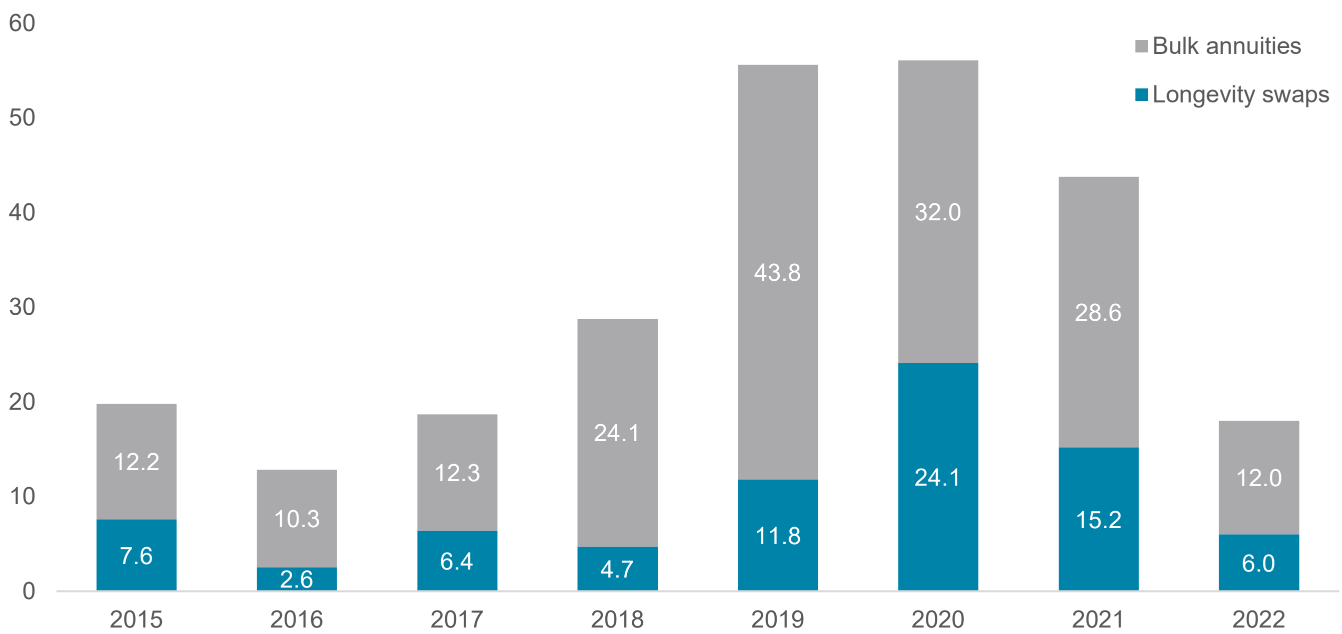
- £5.5bn with SCOR (Lloyds Banking Group Pension Scheme)
- £500m with Canada Life Re (UBS Pension Schemes)

The graph below shows the volume of longevity swap and bulk annuity transactions since 2015.

We expect more longevity swaps to be disclosed for 2022, and we are aware of some completed transactions not yet in the public domain.

This reflects a heightened competitive environment in the market during 2022 with a number of reinsurers actively seeking new business. This has resulted in greater competition which has driven down pricing.

Volumes of risk settlement transactions (£bn)



Source: Aon's Insurer Due Diligence team

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