MILLIMAN RESEARCH REPORT

Single premium immediate annuities

2018 survey

June 2019

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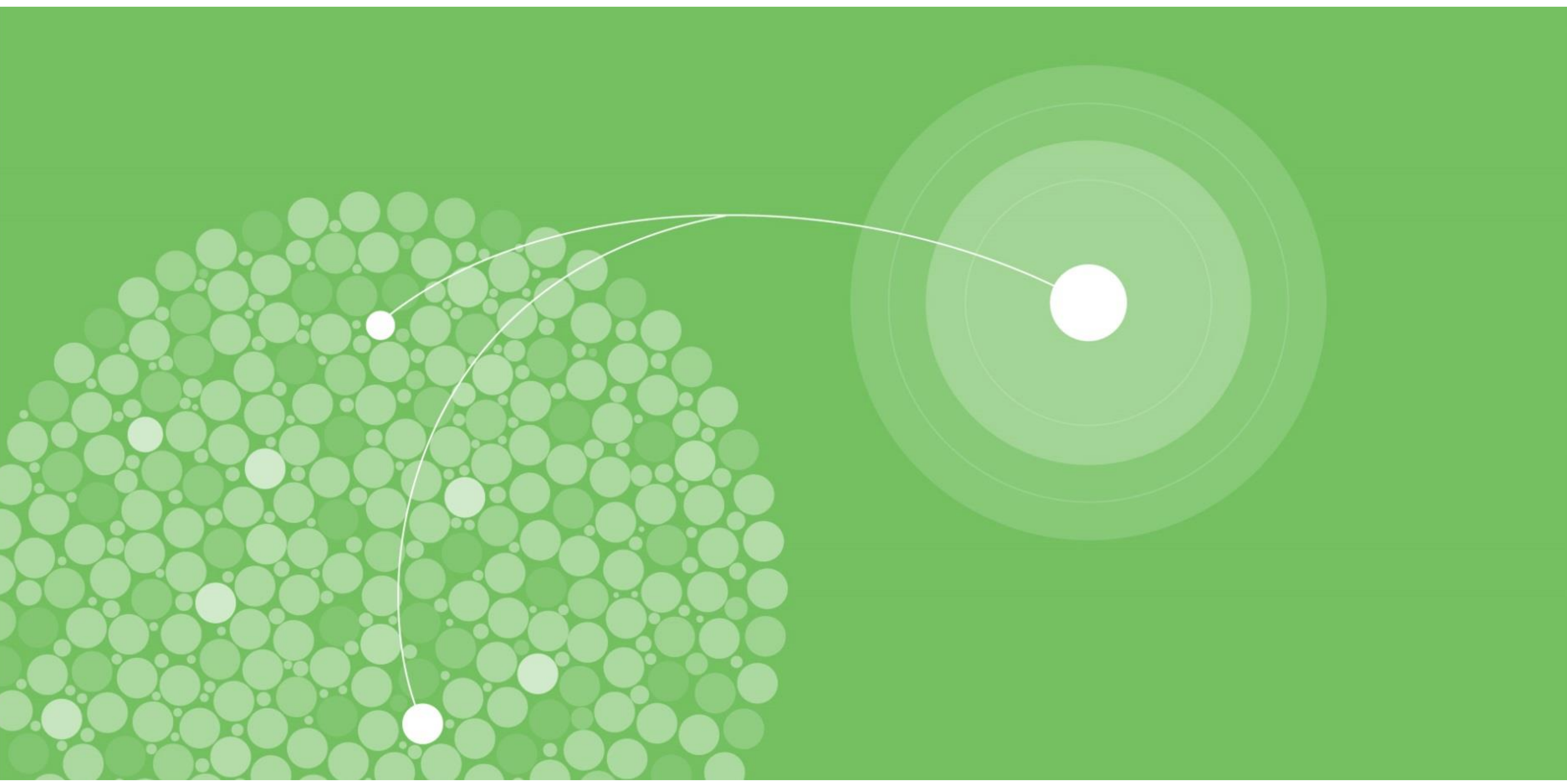

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Background

Milliman conducted a broad-based survey on single premium immediate annuities (SPIAs), capturing historical data for key industry competitors, as well as company perspectives on a range of issues pertaining to these products into the future. Survey topics and questions were determined based on input from a group of cosponsors of the survey as well as Milliman consultants. This survey summary provides carriers with competitive benchmarking to evaluate where they stand relative to their peers.

The survey was sent via email to SPIA companies on April 10, 2018; 28 companies submitted responses. According to Beacon Research, these companies represent almost 94% of the SPIA industry, based on 2017 sales. This figure does not include sales of five survey participants that either did not participate in the Beacon study or did not report SPIA sales in the Beacon study.

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Executive Summary

Survey responses included information about the following five key drivers of SPIA pricing:

1. Investment yields
2. Mortality
3. Profit targets
4. Target surplus
5. Expenses

INVESTMENT YIELDS

The following table in Figure 1 shows a summary of the gross yields assumed in SPIA pricing as of April 1, 2018.

FIGURE 1: YIELD ASSUMED IN SPIA PRICING

YIELD	YIELD ASSUMED IN SPIA PRICING AS OF 4/1/2018				
	Number of Responses	Average	Median	Minimum	Maximum
Gross	28	4.25%	4.23%	3.27%	5.29%

The underlying investments for the SPIA product portfolio are primarily in investment-grade corporate bonds (39.0%), commercial mortgages (13.5%), and private placements (12.5%).

The majority of survey participants assume that reinvestment rates remain the same as initial rates in pricing SPIAs.

MORTALITY

For benefit determination assumptions used in SPIA pricing, the majority of survey participants use some form of the 2012 IAM Basic mortality table, with most using projection scale G2. This is also true for mortality experience assumptions used by survey participants.

PROFIT TARGETS

The most common profit target used by survey participants for SPIA pricing is a statutory return on investment (ROI)/internal rate of return (IRR) target. The average, median, minimum, and maximum ROI/IRR targets are shown in Figure 2, as well as the actual ROI/IRRs reported by survey participants.

FIGURE 2: STATUTORY ROI/IRR

PROFIT MEASURE	AVERAGE	MEDIAN	MIN	MAX
ROI/IRR Target	8.97%	8.50%	5.00%	14.00%
Actual ROI/IRR	8.27%	7.44%	5.00%	13.00%

TARGET SURPLUS

The average level of National Association of Insurance Commissioners (NAIC) risk-based capital (RBC) reported by survey participants is 339%, with a median of 350%, and a range from 100% to 674%.

EXPENSES

SPIA participants allocate expenses on a number of different bases, so a direct comparison of expenses on a component-by-component basis is difficult. Expense assumptions were converted to dollars of expense for a sample policy, assuming a $100,000 average size. Figure 3 shows statistics relative to dollars of acquisition and maintenance expenses for the sample policy.

FIGURE 3: DOLLARS OF EXPENSE

EXPENSE TYPE	EXPENSES ($)			
	Average	Median	Min	Max
Acquisition	1,254	1,180	289	3,516
Maintenance	128	122	25	281

Fully allocated expenses are reflected in pricing by 17 of the 27 responding survey participants, and are not included by the remaining 10.

The distribution of pricing expenses was reported by expense type. Over 61% of acquisition expenses were reported in the distribution category, with 10% in the marketing category, and 8% in the other direct/allocated expenses category. For maintenance expenses, 23% of expenses were reported under corporate overhead, another 23% in technology/systems, and 17% in the other direct/allocated expenses category.

REGULATORY ISSUES

The survey also included questions about the implementation of recent regulatory changes relative to SPIAs.

The changes in the valuation interest rates required in Valuation Manual (VM)-22 have been implemented by 17 of the 28 survey participants. The impact of VM-22 changes to monthly benefits, pricing returns, statutory reserves, and pricing rates were reported by survey participants. (Pricing rates refers to the net interest rates used to determine payout amounts.) A variety of impacts were reported by participants.

Fifteen survey participants have implemented the changes included in the Tax Cuts and Jobs Act (TCJA) of 2017. The majority of those implementing the change did not adjust SPIA profitability targets as a result of tax reform. The tax rate assumed in SPIA pricing was reported to be equal to 35% by 11 participants and equal to 21% by 15 participants. Twelve participants assume 100% of statutory reserves are deductible, nine assume 92.81% are deductible, and four assume 100% for non-life contingent options and 92.81% for life contingent options.

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