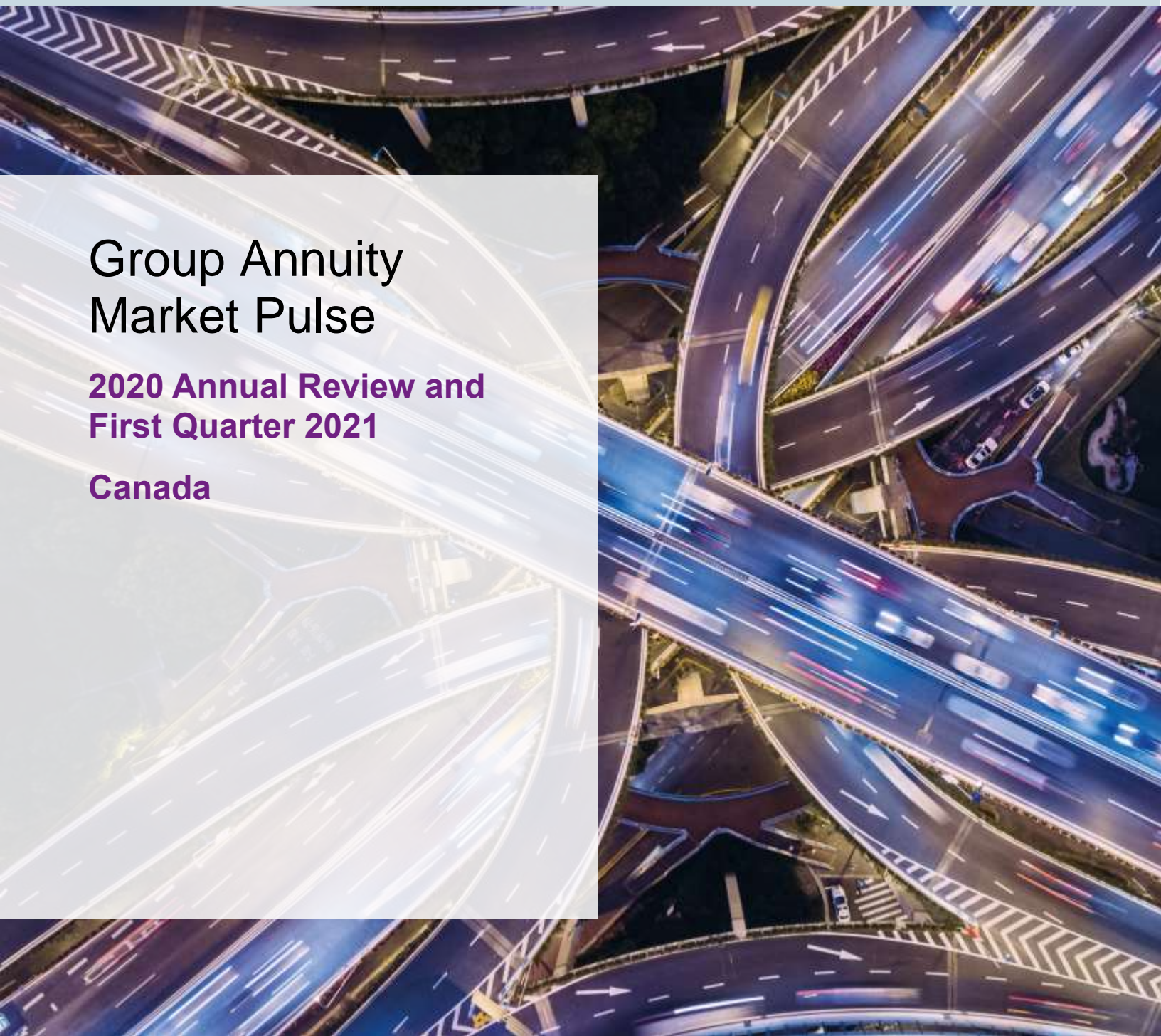


Group Annuity Market Pulse

**2020 Annual Review and
First Quarter 2021**

Canada



Welcome

We are now entering the 8th year of publishing our *Willis Towers Watson Group Annuity Market Pulse* bulletin and are pleased to release the 2020 Annual Review and First Quarter 2021 edition. Despite the disruptions caused by the pandemic during the first half of 2020, we witnessed the third best year in the Canadian annuity market, fuelled by the strongest second half ever witnessed, confirming that pension risk transfer remains top of mind for many plan sponsors.

On the following pages, we will provide an overview of current market players and group annuity sales volume. We will then provide comments on the recently announced \$1.8 billion transaction by GM – *the largest in Canadian history!* This will be followed by an overview of key highlights of 2020 in the US and the UK. Finally, we will have a look at annuity pricing and conclude the report with what's trending in 2021.

Since 2013, Willis Towers Watson's group annuity team has been offering extensive expertise and experience in Canadian group annuities to provide the best outcomes for our clients. We are proud to have advised over 175 clients across the country in assessing whether a group annuity purchase was the right solution for their pension plans. We have innovative tools and experience advising on all sizes of transactions, from the microtransactions (less than \$1 million) to jumbo ones, including the one recently completed by GM for \$1.8 billion.

We would be pleased to discuss this topic with you in more depth and explore risk transfer opportunities for your pension plans.



Willis Towers Watson Canadian Group Annuity Purchase Team Success Measures

60%

Willis Towers Watson advised on ~60% of total volume of transactions in Canada during 2020

175+ \$9B+

Clients advised in developing a group annuity purchase strategy since 2013

of liabilities transferred through group annuity purchases since 2013

Innovation

2014: \$500M pension risk restructuring using a self-insurance **captive solution**

2015: First “**bridge buy-in**” solution

2017: First annuity buy-in deal for **active members** covering future benefit accruals

2018+: Strategic advisor to a large organization to **establish a life insurance company** and reinsure its pension risks

2020: launch of the Willis Towers Watson **Annuity Pricing Tracker** and **Postal Code Mortality Tool**

2020: Completed the **largest annuity transaction** in Canadian market history (\$1.8B)

Ongoing discussions with insurers to be aware of **opportunities**

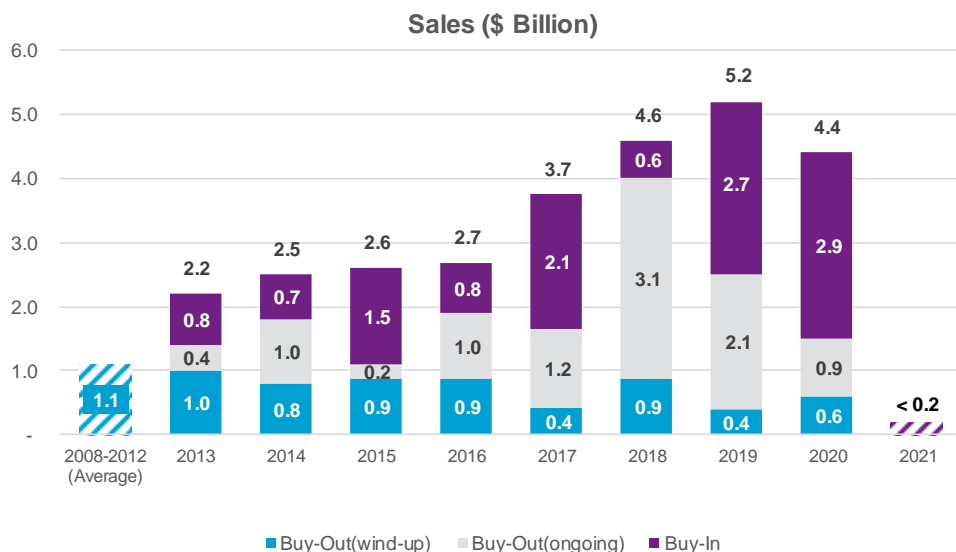


Assurance of **best practices** and use of **innovative tools**



Willis Towers Watson Annuity Purchase Index

Despite the pandemic, the volume of group annuity purchases during 2020 reached \$4.4 billion and over 100 transactions, the third best year ever!



Key Observations:

- The last quarter of 2020 was very active with over 35 transactions completed, representing \$1.6 billion.
- Over 85% of 2020 volume was for ongoing plans.
- One \$660M longevity insurance transaction occurred in 2020 - not included in the graph - [CSS longevity insurance](#).
- Despite a slow start for 2021, we expect the annuity market to be very busy for the rest of the year.

Notes:

- For 2008 to 2012, the breakdown of sales between buy-in and buy-out for terminated plans and buy-out for ongoing plans is not available.
- Excludes longevity insurance agreements.
- Sources of data: LIMRA, Beneva, BMO Financial Group, Brookfield Annuity, The Canada Life Assurance Company, Co-operators Life Insurance Company, Desjardins Financial Security, iA Financial Group, RBC Insurance and Sun Life Financial.

Willis Towers Watson advised on ~60% of transactions (in dollars) during 2020



Who are the players?

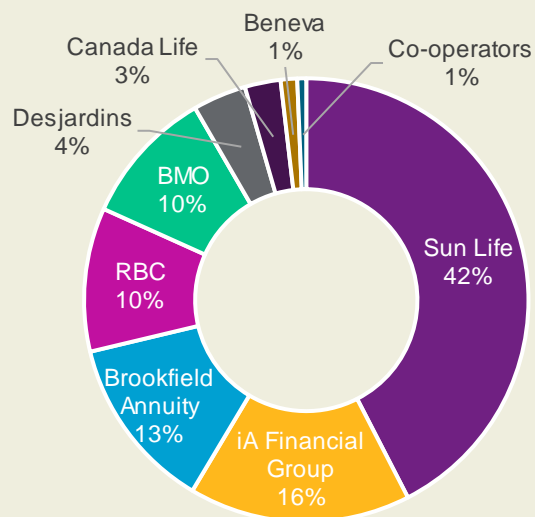
BMO
Brookfield Annuity
Canada Life
Co-operators
Desjardins

iA Financial Group
RBC
Beneva*
Sun Life

5 insurers recorded a volume of sales greater than \$400 million in 2020, contributing to a healthy competitive landscape while keeping pace with the growing demand

* The coming together of La Capitale and SSQ Insurance

2020 Sales Breakdown



Record Canadian CA\$1.8B annuity transaction

We are proud to have been the actuarial advisors to GM Canada on the biggest buy-out annuity purchase transaction ever completed in Canada!

What? A ground-breaking annuity transaction worth \$1.8 billion to transfer the pension liabilities for over 6,000 retirees for the salaried pension plan who retired prior to June 1, 2020.

Who? The deal was secured with Sun Life, iA Financial Group and Brookfield Annuity, with Sun Life acting as the primary insurer.

How? A 12-month engagement process with the insurers and reinsurers was instrumental to create a competitive environment for this jumbo transaction. In addition, the ready to transact investment strategy maintained the plan in a very good financial position as it navigated the financial volatility caused by the pandemic during the first half of 2020. Clients who were able to transact in 2020, when others were not, benefited from a positive financial outcome.

So What? In the past, purchasing annuities in a single day at a competitive price for a block of more than \$1 billion would have been challenging and costly due to the limited capacity from insurers and the challenges to source high-yielding assets in the Canadian market. This transaction is ground-breaking as it demonstrates that the Canadian insurers can now effectively meet plan sponsors' needs for jumbo transactions.

The transaction in figures

- ✓ **\$1.8B:** Largest Canadian transaction
- ✓ **\$1.1B:** Largest Canadian transaction with a single insurer
- ✓ **\$1.4B:** Largest asset in-kind transfer
- ✓ **6,000+:** Retirees annuitized

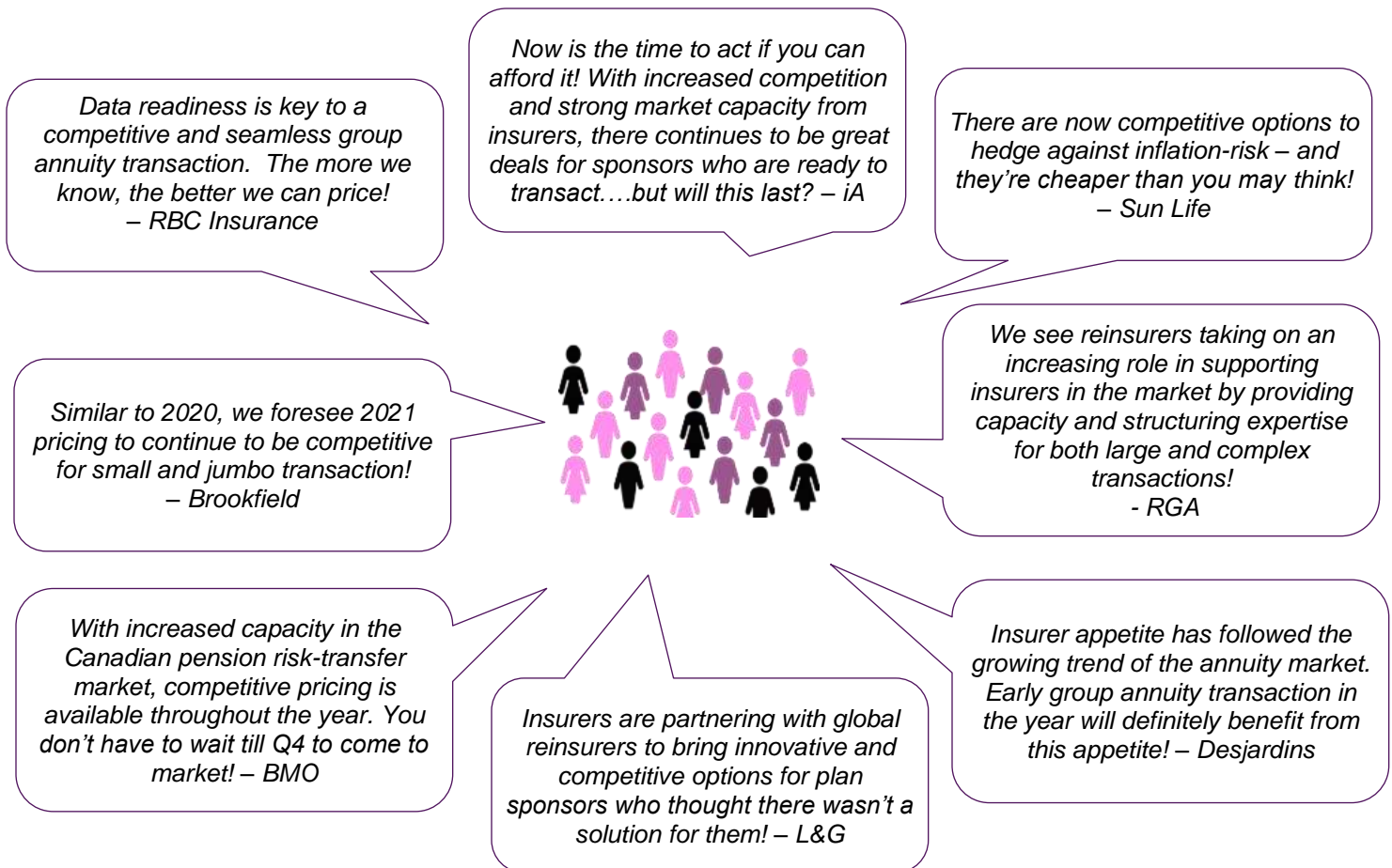
The end results

- ✓ **Transactional and governance readiness** once again paid off
- ✓ **A milestone** in the evolution of pension risk transfer in Canada



Insurers' Pulse

We reached out to insurers and reinsurers in the market to ask them for their view, tips or insights that would help plan sponsors achieve the best outcome as they prepare to purchase annuities in the near future. Here's what they had to say:



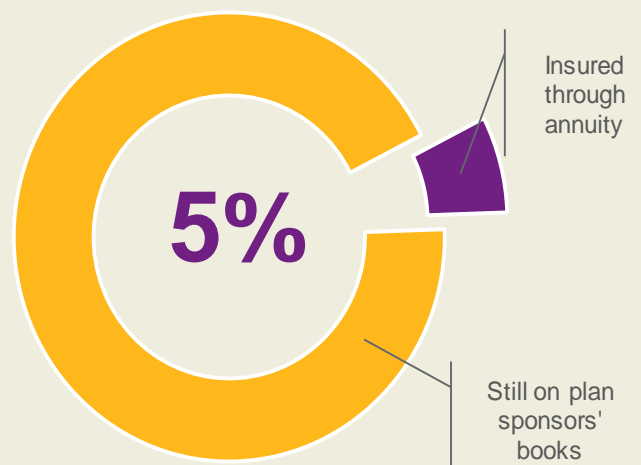
Prevalence of annuity purchases in Canada?

Although we have recently observed increasing volumes of annuity purchase transactions, approaching \$30B in the last decade, we have only started to scratch the surface of Canadian pension liabilities in the private sector.

As a matter of fact, we estimate that only 5% of private enterprise defined benefit liabilities have been insured through annuity purchases through the end of 2020. So far, insurers' capacity has outpaced plan sponsors' demand.

As we turn our attention to 2021 and beyond, we believe the proportion of annuitized liability will continue to slowly but steadily grow as the Canadian group annuity market evolves.

Canadian DB Liabilities (private sector)



What's Going on Elsewhere?

There has been a lot of activity in other key group annuity markets around the world.



United States

While the pandemic slowed down the market during the first three quarters of 2020, activity picked up at the end of the year with more than half of the volume settling in the fourth quarter. The US market continues to be driven by small pension retiree annuity purchase deals, with many sponsors executing a second or third transaction. We expect high activity during 2021 as insurers continue to expand their capacity and the recent rebound in funded status enables plan sponsors to explore further de-risking activities. Increased innovation for large transactions, such as buy-ins and advanced commitment arrangements, are likely to grow in popularity over the coming years.

- ✓ Total 2020 activity at **USD \$27B**
- ✓ **USD \$15B** settled in Q4 2020
- ✓ Since 2017, the United States has been averaging over **USD \$25B**, with WTW advising on more than 50% of that volume
- ✓ Total of **18 insurance companies**, with **10** new insurance companies offering capacity since 2014



United Kingdom

Despite the challenges of COVID-19, 2020 was another incredibly busy year for bulk annuities and longevity hedging, in part due to attractive pricing and improvement in funding levels. In fact, it was the second busiest year on record. Schemes that were ready to transact were able to take advantage of some fantastic pricing. We expect 2021 to be another busy year. Plans in surplus position have almost tripled in the last 5 years and volatility will present attractive pricing for pension schemes that are transaction ready. While activity is expanding, topics such as third-party capital solutions and Environment, Social and Governance (ESG) factors are gaining momentum in the U.K..

- ✓ Total 2020 activity estimated at **£50bn**
- ✓ **£26bn** settled through a buy-in or buy-out arrangement
- ✓ **£24bn** settled through a longevity swap
- ✓ **5 transactions over £1bn** settled during 2020
- ✓ Since 2017, the U.K. has been averaging over **£38bn**, with WTW advising on more than 50% of that volume
- ✓ Total of **8 insurance companies** offering capacity

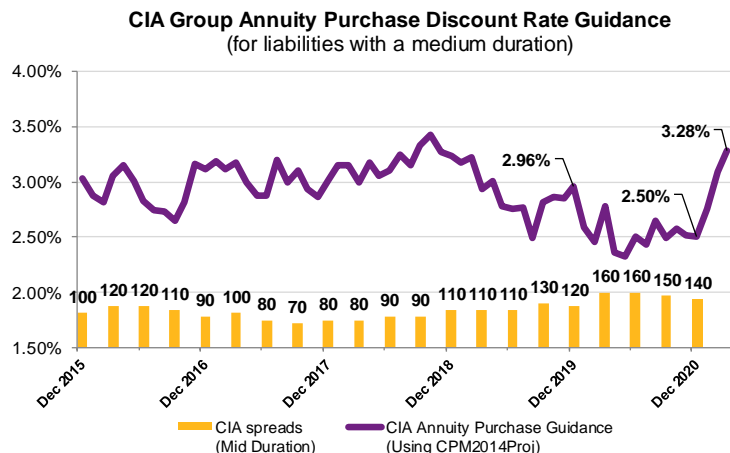
More information on the UK can be found [here](#).



A Look at Group Annuity Pricing

CIA Annuity Purchase Guidance

- The Canadian Institute of Actuaries (“CIA”) annuity purchase discount rate guidance (“CIA guidance”) supports actuaries in selecting actuarial valuation assumptions, without having to request annuity quotes from insurers, by providing market pricing for blocks of business of three different durations at a given date.
- The most recently published CIA guidance indicates annuity pricing at unadjusted long Government of Canada (GoC) marketable bond yields (CANSIM V39062) plus a spread of **140 basis points** (using the CPM2014Proj mortality table) for non-indexed pensions with a medium duration, resulting in a discount rate of **2.50% as at December 31, 2020** (down from 2.96% as at December 31, 2019).
- The **46 basis points decrease** in the CIA guidance since the beginning of the year can be attributable to the decrease in GoC bond yields (66 bps), partially offset by the 20 bps increase in the CIA guidance spread for non-indexed pensions with a medium duration.
- Rates have since increased during 2021 by **~80 basis points** as at March 26, 2021.



Were annuities expensive in 2020?

Price of annuities can be looked at from two different angles – in **absolute terms** or in **relative terms**.

The **absolute level of annuity cost** is determined by the implied gross rate offered by insurers and it is illustrated by the purple line in the above graph. In absolute terms, the cost of annuities in 2020 reached an all-time high as the interest rates reached historical lows due to the massive injection of government spending.

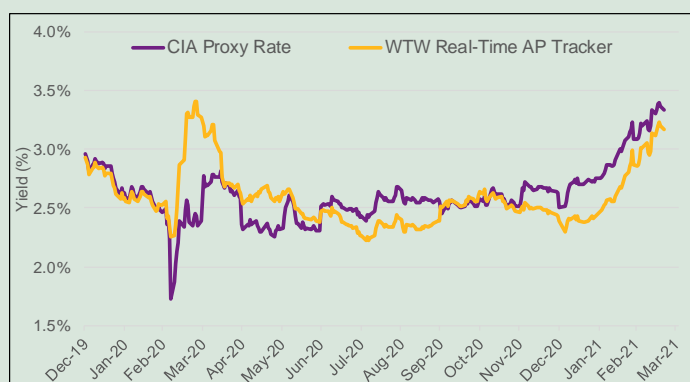
The **relative level of annuity cost** is determined by the level of spread offered by insurers in excess of long-term risk-free rates and is illustrated by the gold bars in the above graph. In relative terms, the spreads offered by insurers during 2020 were the highest of the last decade as the credit spreads on corporate bonds and private placements increased while the market supply was higher than the demand, contributing to a more competitive environment.

During 2020, out of the \$2.4 billion of transactions WTW advised on, \$2.3 billion were sourced from bonds of similar duration, allowing us to draw the conclusion that **2020 offered the most favorable pricing of the last decade** as the average spread above risk-free assets received by plan sponsors was above 150 bps.

How to track the price of annuities in real-time? Use our WTW Real-Time Annuity Tracker

WTW Real-Time Annuity Tracker allows plan sponsors to track the cost of annuities (shown as the yield in the chart) and assess the true competitiveness of quotes received from insurers by reflecting the evolution of credit spreads in real-time.

In addition, the WTW Real-Time Annuity Tracker reflects the mortality profile of specific cohorts based on socio-economic factors obtained from an analysis of the members' data and postal codes using the WTW Postal Code Mortality Tool.



Predictions for 2021

With 2020 in the rear-view mirror, the focus shifts to 2021. Below are our predictions.

A record year? The market is ready to witness another record-breaking year during 2021 as many pension plans' funded status rebounded to pre-pandemic level, leaving several plans with the financial ability to transact. In addition, on the heels of the GM \$1.8 billion transaction completed in 2020, the trend to see larger transactions is expected to continue which will drive the annual annuity market volume higher.

A buyer's or a seller's market? We do not foresee reaching the tipping point where demand reaches levels preventing plan sponsors from transacting due to limited supply. With new insurers entering the market, existing insurers expanding their capacity and the presence of global reinsurers, the supply will continue to expand in the foreseeable future. However, it would not be surprising to eventually see lower levels of spreads offered by insurers as we move from a buyer's market to a seller's market. A CIA guidance spread below 100 bps could be a first sign that the tipping point is approaching.

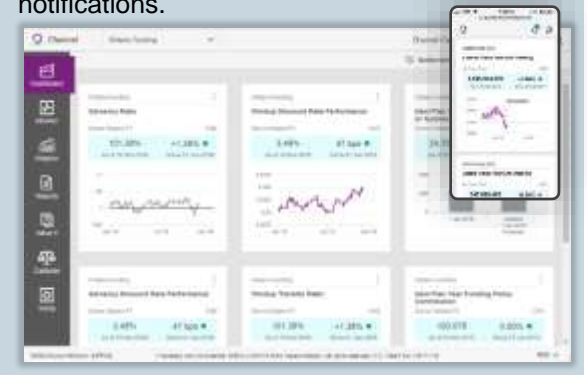
Impact of COVID-19 mortality on annuity costs? With the second wave of COVID-19 upon us, we once again surveyed the pension risk transfer players and their mortality outlook seems to have not changed. For now, the conclusion remains that there is insufficient data to support a change in their mortality assumptions used to evaluate the cost of annuities. The key rationale conveyed being insufficient data, the displacement of deaths, the vaccination campaigns and potentially lower mortality for those not impacted by COVID-19.

Less attractive pricing? As explained in this document, annuity pricing can be assessed in absolute or relative terms. In absolute terms, we all know that future levels of interest rates are very difficult to predict. But with potentially higher inflation as we approach a post-pandemic reality, it is possible that interest rates may go up making annuities less expensive. However, the most important measure for sponsors is the relative measure, or the level of spread offered by insurers above long-term risk-free rates, since bonds are often sold to source the annuity premium. From that perspective, with credit spreads contracting at the end of 2020 and continuing into 2021, and with plan sponsors' demand expected to increase, will we witness less favourable pricing in 2021 compared to 2020?

WTW Monitoring Tool: Channel

Holistic monitoring of a plan's key financial metrics is crucial in the current economic environment. For example, plan sponsors waiting to hit their solvency funding triggers before de-risking should closely monitor financial market movements and annuity purchase pricing in real-time.

Willis Towers Watson's **Channel** can help track the funded status of a plan using daily market data with embedded user-friendly features such as setting triggers and push-notifications.



Want more information?

This document is not intended to constitute or serve as a substitute for legal, accounting, actuarial or other professional advice. For information on how these issues may affect your organization, please contact your Willis Towers Watson consultant, or:

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About Willis Towers Watson

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