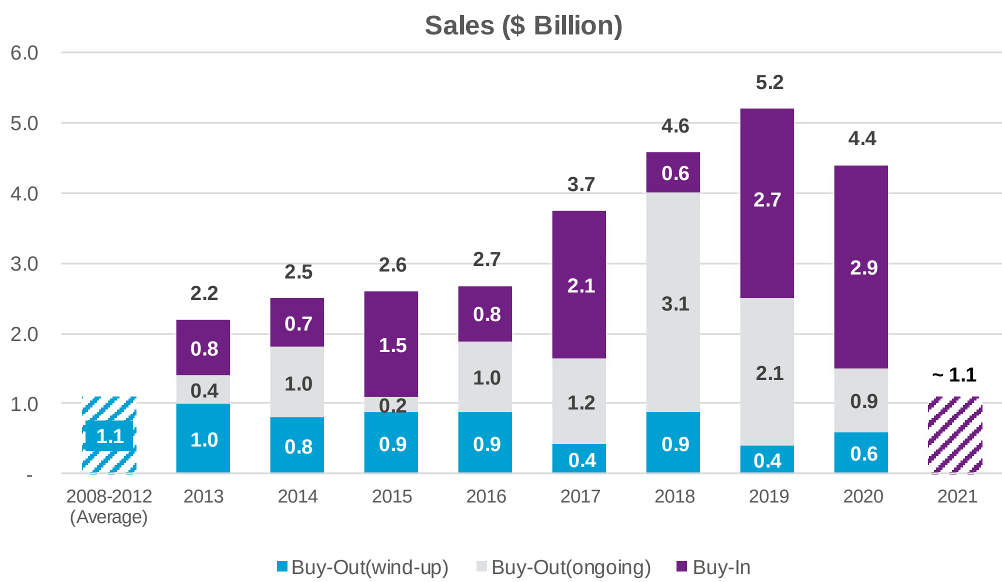
Group Annuity Market Pulse

Second Quarter 2021

Canada

Willis Towers Watson Annuity Purchase Index [1,2]



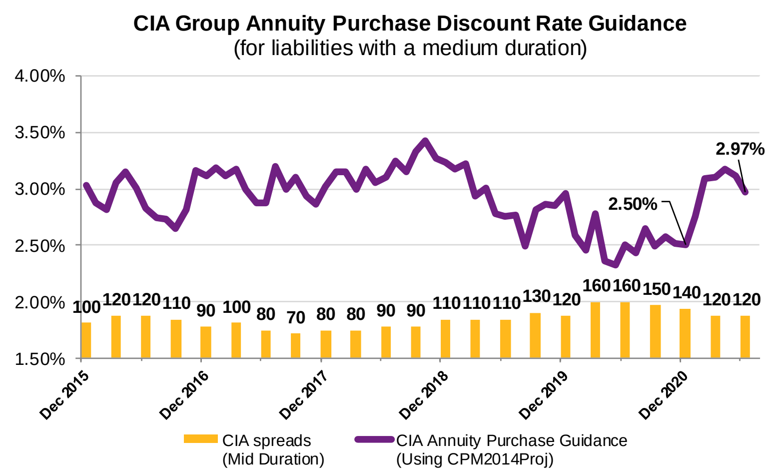
Key Observations:

- Estimated sales of ~$0.9 billion of group annuities were placed during the second quarter of 2021, bringing the 2021 market volume to an estimated $1.1 billion, compared to the prior year volume of $0.5 billion after two quarters.
- We expect the volume of sales to increase significantly in the second half of the year, driven by high volume of activity, larger deals coming to market and a robust pipeline of highly probable transactions.

CIA Annuity Purchase Guidance [3]

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 **120 bps** (using the CPM2014Proj mortality table) for non-indexed pensions with a medium duration, resulting in a discount rate of **2.97% as at June 30, 2021** (up from 2.50% as at December 31, 2020).



The **47 bps increase** in the CIA guidance since the beginning of the year can be attributable to the increase in GoC bond yields (67 bps) partially offset by the 20 bps decrease in the CIA guidance spread for non-indexed pensions with a medium duration.

Notes:

1. 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.
2. Source of data: LIMRA, Beneva, BMO Financial Group, Brookfield Annuity, The Canada Life Assurance Company, Co-operators Life Insurance Company, Desjardins Financial Security, Industrial Alliance, RBC Insurance and Sun Life Financial.
3. Details regarding the most recent CIA guidance can be found at www.cia-ica.ca/publications/guidance.

Market Insight for 2021

Observations on the first half of 2021

We observed a high number of small transactions in the first half of 2021 and a significant pipeline is building up for the rest of the year. This year's appetite for group annuities is fuelled by the improved funded status of pension plans, resulting from the 2021 increase in interest rates and the healthy equity returns generated over the past few years. Group annuities have proven to be a vital tool for plan sponsors looking to either terminate their DB plan in the near term, or to reduce the size of the DB liability on their balance sheet to help manage the plan in the medium to long term.

We do not foresee reaching the tipping point in 2021 where demand reaches levels preventing plan sponsors from transacting due to limited capacity supply. However, we have noticed that insurers were selective in their participation in the last few months due to high level of activity and limited staffing capacity, and we expect this trend to continue for the rest of the year. In general, larger transactions or transactions covering blue-collared members were able to achieve higher participation rates from insurers compared to smaller transactions covering white-collared members. Despite a lower participation rate on some of the transactions, plan sponsors who elected to transact were still able to obtain competitive prices. The key factors for success, especially for transactions with lower participation, is to remain flexible on timing and to be transaction-ready, including ensuring clean and complete data ahead of the transaction.

Predictions for the second half of 2021

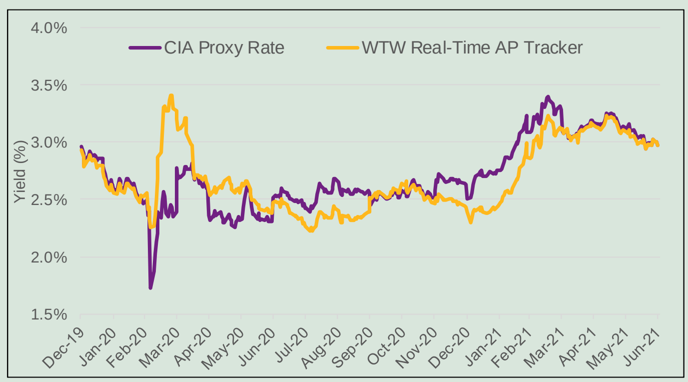
On the heels of the GM $1.8 billion transaction completed in 2020 and with many plans having the financial ability to transact, we expect a busy second half of the year. In fact, if the current pipeline of serious prospects fully concludes in transactions, we expect another record-breaking year with total market volume around the $6.0B mark to finish 2021.

While annuities continue to be a hot topic and a viable solution for many pension plans, plan sponsors and investment managers are also developing innovative solutions that maximize the financial benefits of managing an ongoing DB plan. **Target Yield Funds** (also known as *do-it-yourself* annuity strategy) represent an innovative investment solution to maintain the assets within the plan, mitigate the cash flow and interest rate risks, while aiming for returns of up to 100 bps above the implicit yield offered by the insurers. In other words, it is applying the proven and tested recipe that's been used by insurers for decades, but also keeping insurers' profit and operational margins within the plan for the plan sponsor's benefit. Refer to this article which compares the traditional annuities option versus the emerging target yield fund approach.

Track the price of annuities in real-time using 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.

The WTW - Real-Time Annuity Tracker suggests that the current spreads in the CIA Guidance provides for a reasonable proxy for estimating the actual cost of settling liabilities via annuities.



Want more information?

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