normandin beaudry
straight talk

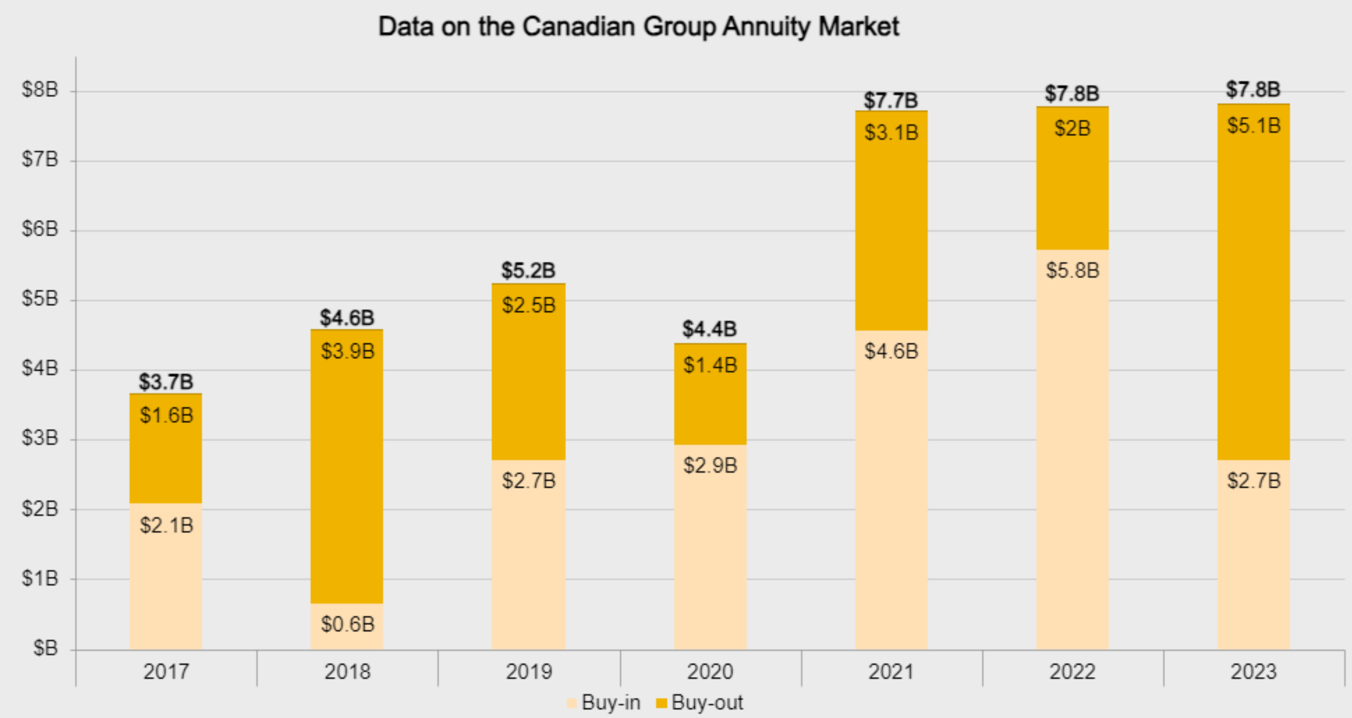
ANNUITY PURCHASES IN CANADA IN 2023

The enthusiasm continues

March 2024

In summary

- In 2023, annuity purchases in Canada surpassed $7.5 billion for a third consecutive year.
- With interest rates rising in recent years, many pension plans have seen significant improvement in their financial positions. Annuity purchases allowed organizations to crystallize some of the gains observed and, in some cases, even further improve their plans' financial position.
- The implicit returns on annuity purchases have been particularly high, making annuity purchases an attractive investment for pension funds of all sizes.
- Insurers have continued to offer attractive pricing for indexed annuities, despite the Government of Canada's decision to stop issuing real return bonds (more details here).



Source: Life Insurance and Marketing Research Association (LIMRA)

Interest rates

Despite the decrease in interest rates observed in late 2023, the sharp rise in recent years has only contributed to the growing enthusiasm for group annuity purchases. Annuity purchase rates continue to be closely aligned with discount rates used for the accounting valuations of pension plans, allowing many organizations to carry out transactions without significant accounting impacts.

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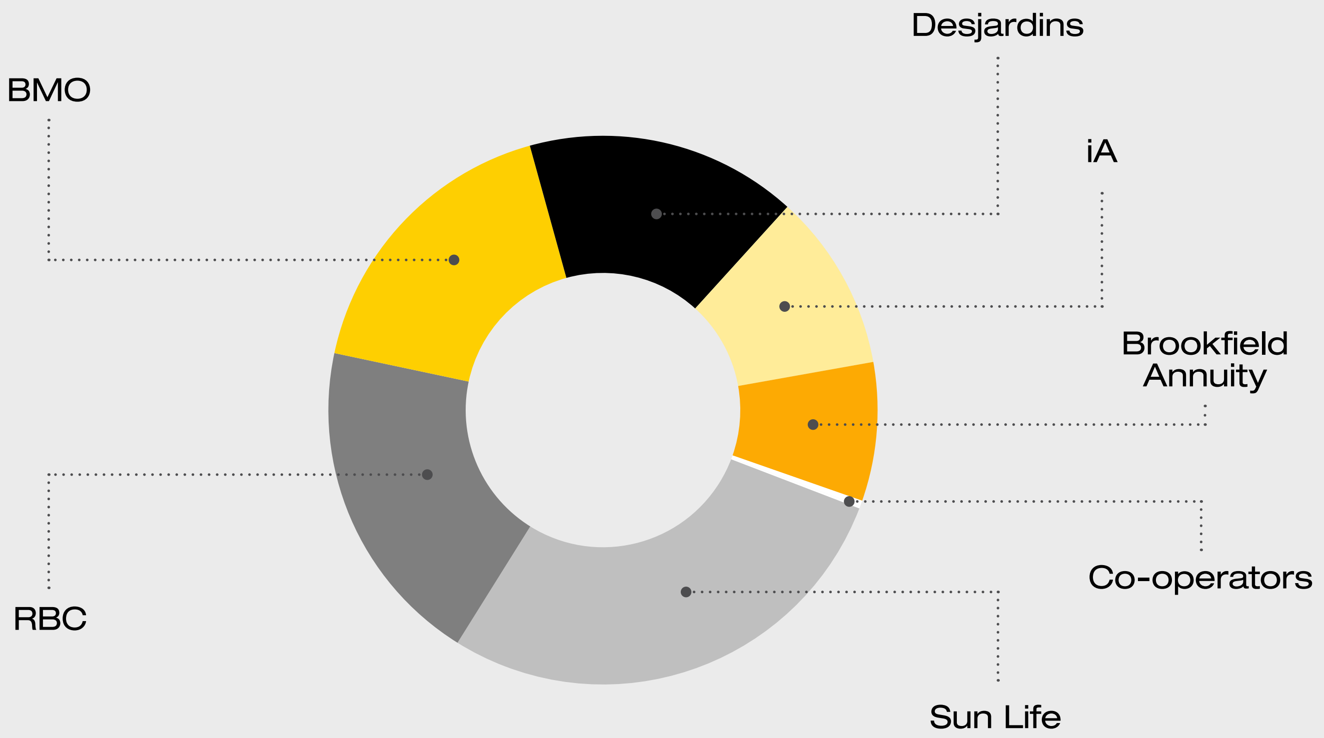
Insurers

Last July, Canada Life announced that it would be pulling out of the Canadian group annuity market. Since then, seven major insurers now share most transactions and their respective market share changes from year to year. Below is an overview of 2023:

Seven major insurers now share most transactions



Source: Data provided by insurers.

Transfer or manage Risks?

A diversified portfolio, adapted to the pension promise for a pension plan's specific group of retirees, can be considered as an alternative to an annuity purchase. With this segmentation strategy, the portfolio is comprised mainly of fixed-income assets that generate regular cash flows and can include private market investments, including private debt and commercial mortgages.

This approach is part of a broader family of liability matching risk management strategies. It is suitable for pension plans that want to maintain full flexibility in the management of their assets or that do not have the necessary funding to fully transfer risks to an insurer. While this strategy can prove to be less expensive if it generates a higher long-term return, the pension plan retains market and longevity risks.

WHICH STRATEGY SHOULD BE ADOPTED?

Several factors need to be analyzed, but one element remains essential: the pension plan must be adequately compensated for retaining the risks.

An annuity purchase can be seen as a very low-risk investment, as the monthly annuities paid by the insurer to retirees represent the return on investment in capital and interest. If a pension plan is unable to build a portfolio with an anticipated net return that is sufficiently attractive to retain market and longevity risks, the annuity purchase becomes all the more relevant.

Industry news

REAL RETURN BONDS

In 2022, the Government of Canada announced it would no longer issue real return bonds. This type of bond is a risk management tool used by pension plans providing indexation. Despite this announcement, insurers continue to offer competitive pricing for indexed annuity purchases, and opportunities should continue to arise in 2024. However, pricing for indexed annuity purchases may rise in the coming years, depending on alternative investment strategies adopted by insurers.

ASSURIS COVERAGE: BETTER PROTECTION FOR POLICYHOLDERS

In May 2023, Assuris, the not-for-profit organization that protects Canadian policyholders if their life and health insurance company fails, announced higher levels of protection.

	Before	After
buy-in	**85%**	**90%**
buy-out	Up to **$2,000** or **85%** of the monthly benefit, whichever is higher	Up to **$5,000** or **90%** of the monthly benefit, whichever is higher

These improvements change the way some transactions are structured, eliminating the need to transact with more than one insurer to maximize the Assuris protection. The protection can also apply per policy rather than per insured, thus offering possibilities to increase the protection to 100% regardless of the annuity amount. Existing annuity contracts also benefit from the new protections.

→Key factors for a successful annuity purchase

If you're looking to purchase annuities for your pension plan, here are five elements to act on now to be ready to seize opportunities that arise in the market:

1. INVESTMENTS

Ahead of the transaction, ensure that your pension fund's asset allocation has sufficient assets that are better hedged as well as liquid assets to pay the cash premium. In some cases, a transfer in-kind can also be considered if your assets are likely to interest insurers (e.g., real return bonds for an indexed annuity purchase). You should also think about the asset mix for the plan after the annuity purchase. It is also important to ensure that the annuity purchase is authorized under the investment policy.

2. FINANCIAL IMPACTS

Make sure you fully understand the financial impacts of an annuity purchase for your plan. It's possible that the annuity purchase may require a special contribution. The impact of the transaction on the plan sponsor's financial statements should also be well understood.

3. MEMBERSHIP DATA

Ensure that your retirees' data is accurate and up to date. A survival audit of retirees and their spouses could significantly reduce the insurers' premium if certain deaths were not reflected in your databases.

4. BENEFITS

Make sure you fully understand the characteristics of the annuities to be insured. Some death benefits have nuances that will need to be clarified. For instance, is marital status established at the time of retirement or at the time of the retiree's death? Also, some indexing formulas with a cap sometimes include a mechanism to adjust the annuity to catch up on indexing that was not granted in the past.

Consider communicating with insurers early in the process to inform them of a potential transaction. These discussions will help structure an optimal transaction—one that considers both the plan sponsor's risk transfer needs and the insurers' preferences for the risk profiles of the annuities to be purchased.

5. GOVERNANCE

Ensure that the decision-making process is clearly established and that the roles of the various stakeholders are identified ahead of time. On transaction day, who will have the authority to accept the transaction? Pre-selecting purchase criteria will facilitate decision-making on transaction day. To consolidate these criteria, an annuity purchase guide or policy could be helpful.

→Questions or looking to purchase annuities for your pension plan?

CONTACT OUR SPECIALISTS!

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Normandin Beaudry expanded its international reach and became a joint venture partner of MBWL International in 2023

MBWL International assists its clients with annuity purchase transactions to transfer risks to insurers. Our clients with international operations, particularly in the U.S. and the U.K., will be able to benefit from our expertise.

mbwl international