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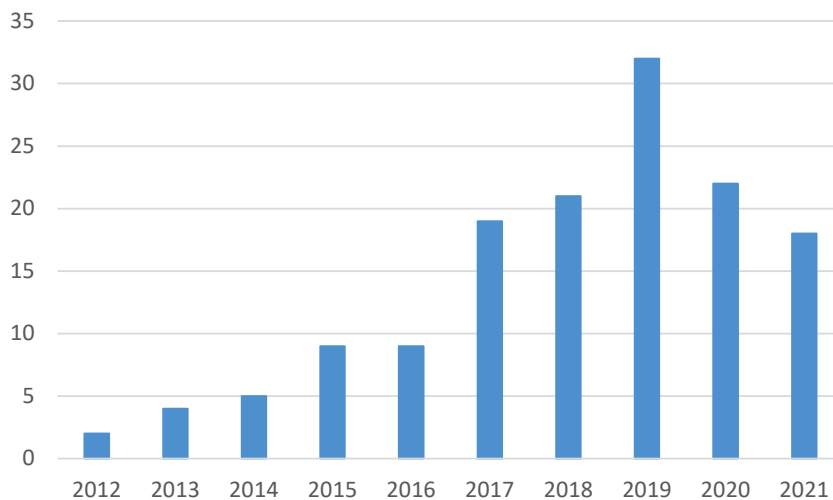
Pension Risk Transfer (PRT) Market Heats Up

By Scott Hawkins, Director, Insurance Research and Sean Kurian, Head of Institutional Solutions

During 2020, pension risk transfers (PRTs) slowed as pension plan sponsors and insurers became cautious in executing any de-risking moves during the height of the pandemic. As the year progressed and rolled into 2021, the number of PRTs increased.

After reaching a peak of 32 transactions in 2019, the number of U.S. PRTs decreased to 22 in 2020.¹ However, there have already been 14 transactions reported through March 31, 2021. In terms of the amount of liabilities transferred, insurers have assumed \$12.0 billion through March of 2021, compared to \$15.3 billion in 2020 and \$14.4 billion in 2019.¹

Figure 1 U.S. PRT Transactions
as of March 31, 2021



Prepared by Conning, Inc. Source: Company press releases

Part of the increased activity in early 2021 represents PRTs that were delayed during 2020 due to COVID-19. That said, PRT interest among insurers continues to grow, driven by the significant growth opportunities it represents. Looking at the remainder of 2021 and beyond, plan sponsor interest in PRTs is likely to increase as the financial impact of defined benefit plans on balance sheets and income statements continues to be felt. With all of this in mind, how hot is the market getting and how long will it remain so?

A Concentrated Market

The U.S. PRT market has seen a small number of insurers dominate. In 2021, for example, five companies accounted for 13 of the 14 PRT transactions thus far and \$10.6 billion of the \$12.0 billion in pension liabilities transferred.¹ Because PRTs are bespoke transactions, like M&A, their frequency and size vary. As a result, insurer rankings can change from year to year. In addition, new insurers in this market are impacted by Department of Labor safe harbor rules which can be a barrier to entry.² We see this variability in the top five for 2021 and the number of PRTs they executed in all of 2020.¹

Since 2012, when the U.S. PRT market emerged with the General Motors³ and Verizon PRTs,⁴ 22 separate insurers have conducted PRT business. Of those, seven were also involved in syndicated PRTs where two or more insurers joined forces to assume a plan's liabilities.¹ In 2021, for example, MetLife and Principal assumed \$1.2 billion in liabilities from the Phillips North American Pension Plan.⁵

Figure 2 Top PRT Companies: U.S. Pension Liabilities Transferred

through 03/31/2021, \$ in millions

Buyer	2021 Transactions	2021 Liabilities Transferred	2020 Transactions	2020 Liabilities Transferred
Rothesay Life	1	\$5,000	0	\$0
MetLife	2	\$2,100	1	\$1,900
Athene	1	\$1,700	1	\$1,000
MetLife & Principal Financial	1	\$1,200	0	\$0
MassMutual	2	\$609	2	\$392
Remaining	7	\$1,379	18	\$12,067
Total	14	\$11,988	22	\$15,359

Prepared by Conning, Inc. Source: Company press releases and news articles.

Five companies have assumed 70% of all PRT liabilities from 2012 through 2021. Prudential Financial, Athene, MetLife, Sunlife, and Legal & General assumed \$100.3 billion, or 75%, of the \$133.4 billion of U.S. pension liabilities transferred through a PRT.¹

Market Concentration Not a Barrier

Even with this concentration, the appeal of the PRT market continues to attract new players. During its Q420 earnings call, Fidelity National Financials' CEO, Raymond Quirk, stated that expansion into institutional products, including the PRT market, would be an area of strategic focus following its acquisition of F&G Life in 2021.⁶

During 2020, Pacific Life entered the PRT market and generated \$2.3 billion in PRT sales, with \$972 million just in Q420.⁷

The potential to build out a larger PRT franchise was one factor in Brookfield's partnership with American Equity Life. J. Bruce Flatt, Brookfield's CEO, said during his firm's investor day presentation in September 2020 that Brookfield had a small PRT operation and "We've learned a lot doing that, and we think that there's a significant area to grow."⁸

KKR also mentioned PRTs during the investor presentation on its acquisition of Global Atlantic.⁹ Global Atlantic also gave PRTs as one use of the \$1 billion of capital raised by its IVY Co-Invest sidecar in 2020.¹⁰

While new insurers enter the PRT market, established players continue to show commitment to the PRT market. In October 2020, Blackstone Group sold its 36% stake in U.K. pension buyout firm Rothesay Life to GIC and MassMutual for an undisclosed sum. Under the terms of the deal, GIC and MassMutual will each own 49.0% of Rothesay Life. Blackstone, GIC, and MassMutual originally bought stakes in Rothesay Life from Goldman Sachs Group in 2013.¹¹

In 2021, reports emerged that Prudential Financial was considering selling its retirement business segment yet retaining the PRT business from that segment.¹²

PRT as an Asset Gathering Opportunity

By entering into and developing their PRT businesses, insurers have an opportunity to increase their assets under management. Much of those assets are held in frozen plans. For example, the Bureau of Labor Statistics reported that in March 2019 out of all private industry workers participating in defined benefit plans, 24% participated in a soft-frozen defined benefit plan and 14% participated in a hard-frozen defined benefit plan.¹³

Frozen plans are pension plans that are no longer offered to new employees. Soft frozen pension plans differ from hard frozen pension plans in that existing members continue to accrue benefits under a soft frozen plan. Under a hard-frozen pension plan, existing members no longer accrue benefits.

While any defined benefit pension plan is a possible PRT candidate, frozen plans may be more open to considering a PRT. Once a plan is frozen, its ongoing importance to hiring, employee retention and overall compensation strategy is decreased. However, a frozen plan's impact on plan sponsor balance sheets and income statements remains. Reducing this impact through a PRT can therefore be attractive.

Plan Sponsor Interest in PRTs Likely to Grow

Looking ahead, 2021 and beyond may well just be the beginning of a PRT activity boom. Plan sponsor interest in PRTs is likely to remain, based on their highlighted concerns. That said, plan economics remain a key input in deciding PRT volumes.

Of course, the key factor determining PRT volumes will be funding status. PRTs are less expensive for the plan and its sponsor the closer the plan is to fully funded on a termination basis. In terms of funding status, the strong growth of equity markets in 2020 (post April) benefited those plans that had significant allocations to equities. Overall, our analysis of the end-2020 funding status of 667 U.S. defined benefit plans with five consecutive years of reported plan assets showed that their average funding status of 89% was slightly higher than end-2019's 87%.¹⁴

“The key factor determining PRT volumes will be funding status.”

Other factors will be plan sponsor expectations on where interest rates are likely headed. The Federal Reserve's continued low interest rate policy can impact the defined benefit pension discount rates used to calculate the present value of the liabilities by anchoring longer-term interest rate expectations and plan actuarial return assumptions.¹⁵ Lower discount rates and return assumptions can increase plan liabilities, potentially reducing a plan's funded status, and increase the cost of pension plan provision.

Equity allocations were a strong contributor to pension plan performance in 2020 and could continue to help funding. However, plan sponsors considering an asset-in-kind PRT strategy and better risk management may want to consider a shift in allocations towards fixed income, which is favored by annuity insurers for asset-in-kind PRTs. Asset-in-kind PRTs are when the plan gives assets to an insurer rather than paying the insurer a cash premium. Both plan sponsors and insurers may favor asset-in-kind PRTs since this strategy can lower transaction costs for the plan and reduce the insurer's need to deploy large cash premiums.

Regardless of paying cash or transferring assets, plan sponsors looking at executing PRTs over the medium term will need to assess the future for capital market risks, returns, and asset allocation strategies as they manage their pension plans and improve funding levels. Ultimately, it will be their success at those tasks, coupled with insurers' appetites to gather assets and assume PRT risks, that will determine just how long the PRT market stays hot.

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Footnotes

¹ Conning Pension Risk Transfer (PRT) transaction database, compiled by Conning's Insurance Research team since 2011 based on publicly available news items and press releases.

² <https://www.jdsupra.com/legalnews/reminder-the-secure-act-s-safe-harbor-1669812/>

³ https://media.gm.com/media/us/en/gm/news.detail.html/content/Pages/news/us/en/2012/Jun/0601_pension.html

⁴ <https://www.verizon.com/about/news/press-releases/verizon-transfer-75-billion-management-pension-plan-obligations-prudential>

⁵ <https://www.businesswire.com/news/home/20210223005917/en/MetLife-and-Principal-to-Provide-Annuity-Benefits-to-Philips-North-America-LLC-Retirement-Participants>

⁶ <https://platform.marketintelligence.spglobal.com/web/client?auth=inherit#news/docviewer?mid=153555032&KeyProductLinkType=2>

⁷ <https://www.businesswire.com/news/home/20210302005272/en/Pacific-Life-Reports-2.3-Billion-in-Pension-Risk-Transfer-Sales-in-First-Year-Under-New-Institutional-Division>

⁸ <https://platform.marketintelligence.spglobal.com/web/client?auth=inherit#news/docviewer?mid=143996643&KeyProductLinkType=2>

⁹ <https://platform.marketintelligence.spglobal.com/web/client?auth=inherit#news/docviewer?mid=140237222&KeyProductLinkType=2>

¹⁰ <https://apnews.com/press-release/business-wire/39ccccafea3b428eab3ba1ece853f925>

¹¹ <https://www.massmutual.com/about-us/news-and-press-releases/press-releases/2020/09/gic-massmutual-to-acquire-blackstones-shareholding-in-rothesay-life>

¹² <https://www.spglobal.com/marketintelligence/en/news-insights/latest-news-headlines/prudential-financial-up-amid-retirement-arm-sale-report-markets-hit-records-63700007>, <https://www.bloomberg.com/news/articles/2021-04-13/prudential-financial-is-said-to-weigh-sale-of-retirement-arm>

¹³ Bureau of Labor Statistics, U.S. Department of Labor (2020). <https://www.bls.gov/ncs/ebs/factsheet/defined-benefit-frozen-plans.htm#:~:text=In%20March%202019%20out%20of,in%20a%20soft%20frozen%20plan.>

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¹⁵ The Board of Governors of the Federal Reserve System, Federal Reserve issues FOMC statement, March 17, 2021 - <https://www.federalreserve.gov/newsevents/pressreleases/money20210317a.htm>