

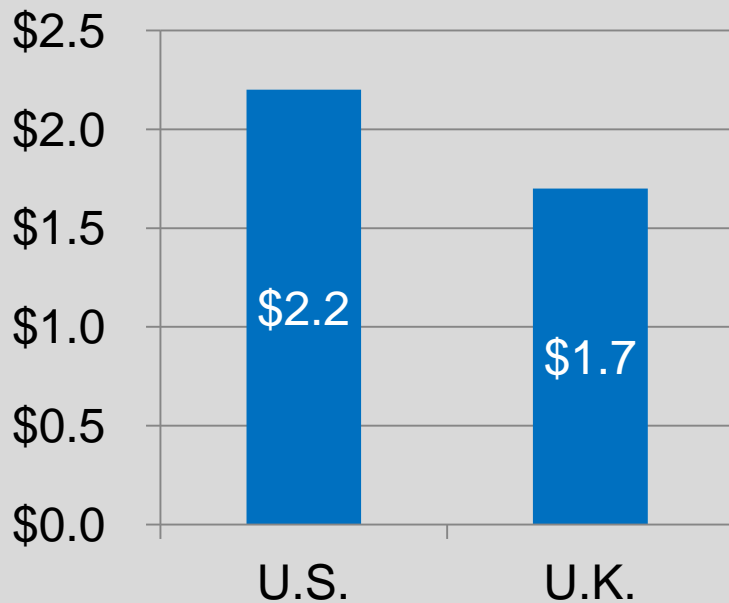
# A U.S. Perspective on Annuity Lifetime Income Guarantees

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Mexico City

- Defined Benefit and Defined Contribution plan trends in the U.S. and prospects for longevity bonds
- Behavioral influences on design of variable annuity and DC plan withdrawal-based lifetime income guarantees
- Introduction to variable annuity and DC plan withdrawal-based lifetime income guarantees
- Contribution of traditional fixed and variable immediate annuities and annuitization of deferred annuities toward improved retirement financial security in the U.S.

# Defined Benefit Plans in the U.S.: A Different Situation

## Corporate Defined Benefit Pension Plan Assets (\$ Trillions)



U.S. Data as of December 31, 2010  
Source: Investment Company Institute, 2011

U.K. Data as of December 31, 2010  
Source: *Pension Scheme Deficits - Latest Monthly Update*, Pension Capital Strategies Ltd., January 2011

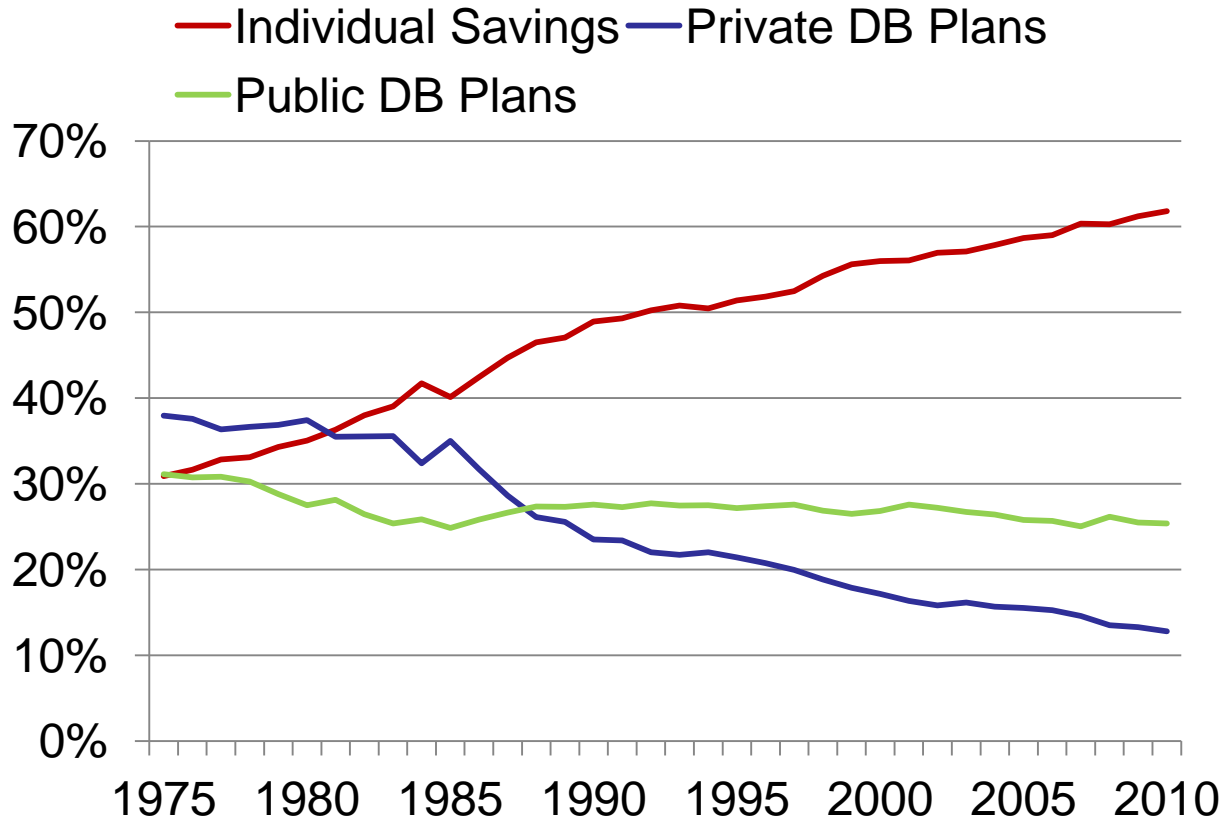
- U.S. corporate DB plans continue to be replaced by DC plans
  - 40% already or expected to be frozen within a year<sup>1</sup>
  - By 2005, U.S. private sector DB plans had fallen to 30,000 from a peak of 112,000 in mid-1980s<sup>2</sup>
  - In 2008, 21% of U.S. private industry workers had access to a DB plan<sup>3</sup>
- U.S. corporate DB plans rarely offer inflation-adjusted benefits, avoiding amplified systemic longevity risk
- U.S. public DB plans generally do provide inflation-adjusted benefits
- U.S. DC plans generally do not offer any lifetime annuity benefits

<sup>1</sup>Source: *U.S. Employer Trends for Retirement Plans: Implications for Future Retirees*, LIMRA, 2010

<sup>2</sup>Source: Pension Benefit Guaranty Corporation, 2005

<sup>3</sup>Source: *National Compensation Survey*, Bureau of Labor Statistics, U.S. Department of Labor, March 2008

# Percentage of Total U.S. Retirement Assets



Individual includes annuities, IRAs, and employer-sponsored defined contribution plans such as 401(k), 403(b) and 457 plans

- The percentage of all U.S. retirement assets held in individual accounts, including DC plans, has doubled to over 60%
- The percentage held in public employee DB plans has remained relatively stable while the percentage held in private DB plans has plummeted

Source: Investment Company Institute, 2010

- In the U.K., capacity for longevity risk is strained by mandated demand for inflation-adjusted lifetime annuity benefits
- Global reinsurers step in to create capacity
- Insurers with substantial mortality risk are best situated to hold longevity risk
- Creating a market for longevity bonds offers advantages/challenges
  - Sets a benchmark, facilitates a tradable market for longevity risk
  - Market imbalance – too few natural buyers? Bid/ask spread?
- In the U.S., corporate DB plan risk reduction actions will likely vary by sponsor type and plan size
  - Smaller frozen plans likely to transfer full risk
  - Large frozen and closed plans may transfer retiree liability in tranches over time

**"In the UK, most workers must convert their pension pot into an annuity on retirement. In the US, where self-managed pensions are more common, only a fifth of the population aged between 45 and 70 say they would buy an annuity, according to a Society of Actuaries survey."**

***-- Financial Times, May 28, 2011***

# Three Major U.S. Defined Contribution Plan Challenges

- Participants not contributing enough to the plan
- Participant asset allocation decision-making
- Participants unprepared for capital market and longevity risks

# Behavioral Considerations Influence Design of DC and Variable Annuity Lifetime Income Guarantees

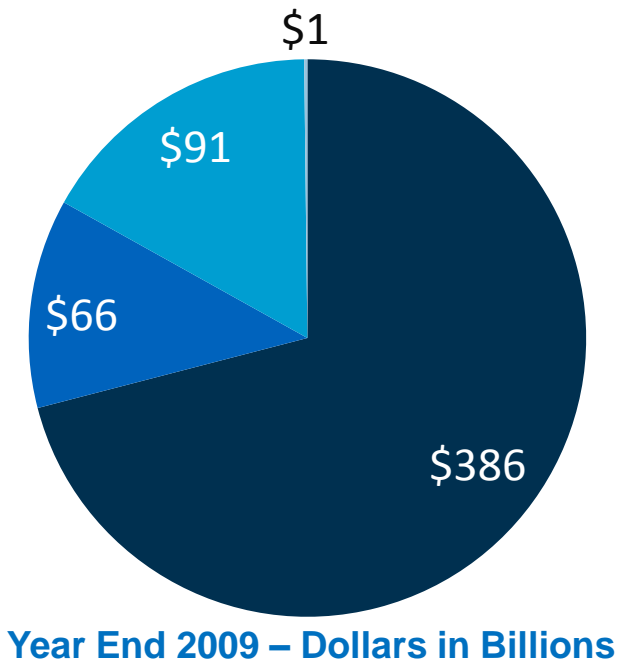
- Importance to consumers of maintaining control and liquidity of retirement savings
- Risk pooling of “self-managed” retirement savings (to achieve mortality cross-subsidy) viewed differently by consumers than retirement income sources that were not “self-managed”
- Consumers still want guaranteed lifetime income!
  - Many ACLI members offer traditional and in-plan annuities and expect these markets to grow

**Withdrawal-based lifetime income guarantees in variable annuities and certain defined contribution plans**



# Withdrawal-Based Variable Annuity Lifetime Income Guarantee Assets Exceed Traditional Annuitization

Annuities account for 83% of \$544 Billion of retirement income product assets

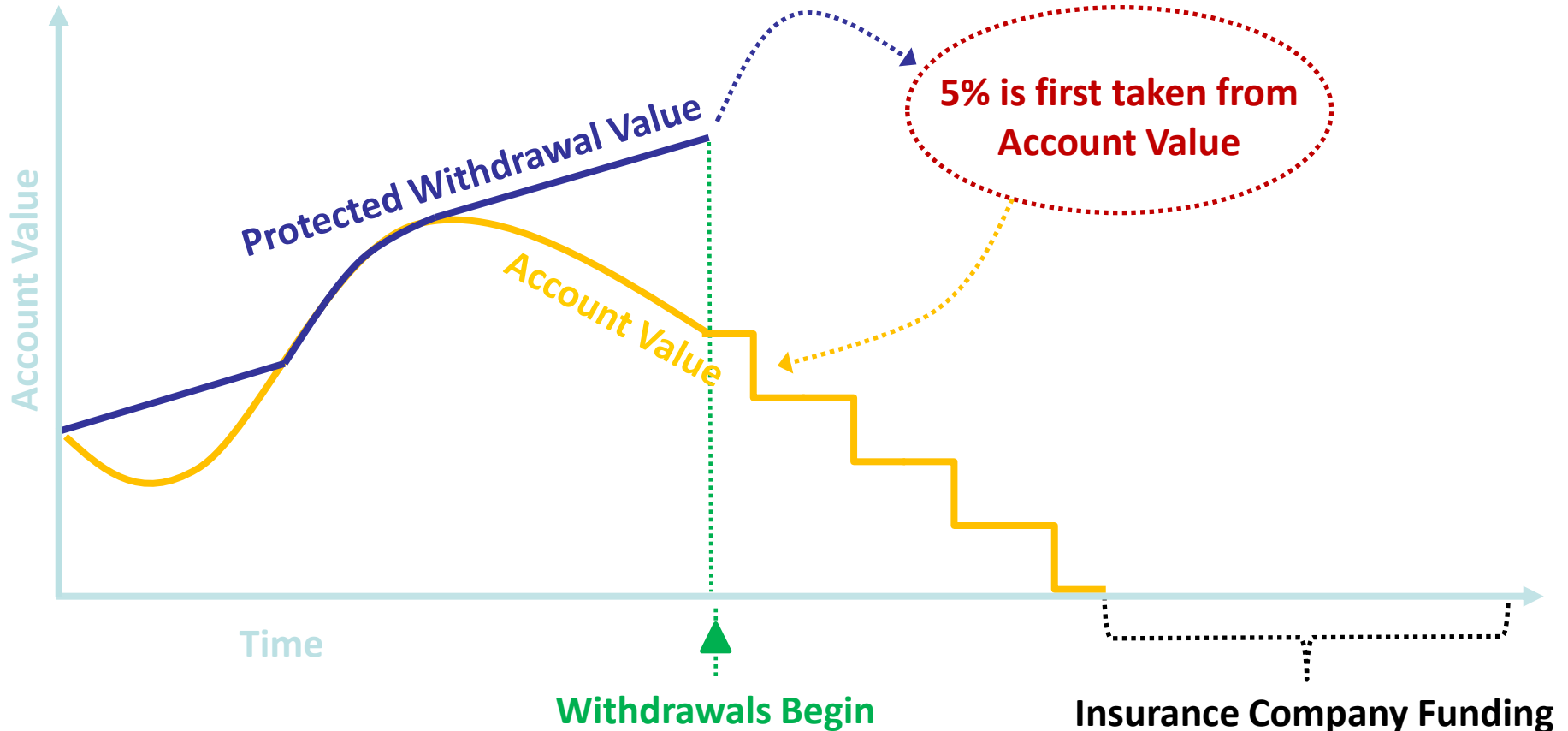


- Variable Annuity Guaranteed Living Benefits\* = 71%
- Single Premium Fixed and Variable Immediate Annuities/Annuitization of Deferred Fixed and Variable Annuities = 12%
- Reverse Mortgages = 17%
- Managed Payout Funds and Mutual Funds with Guarantees = 0%

Source: *Guaranteed Living Benefits Utilization - 2009 Data*, LIMRA, 2011

\* Includes GLWB, GMIB, GMWB designs

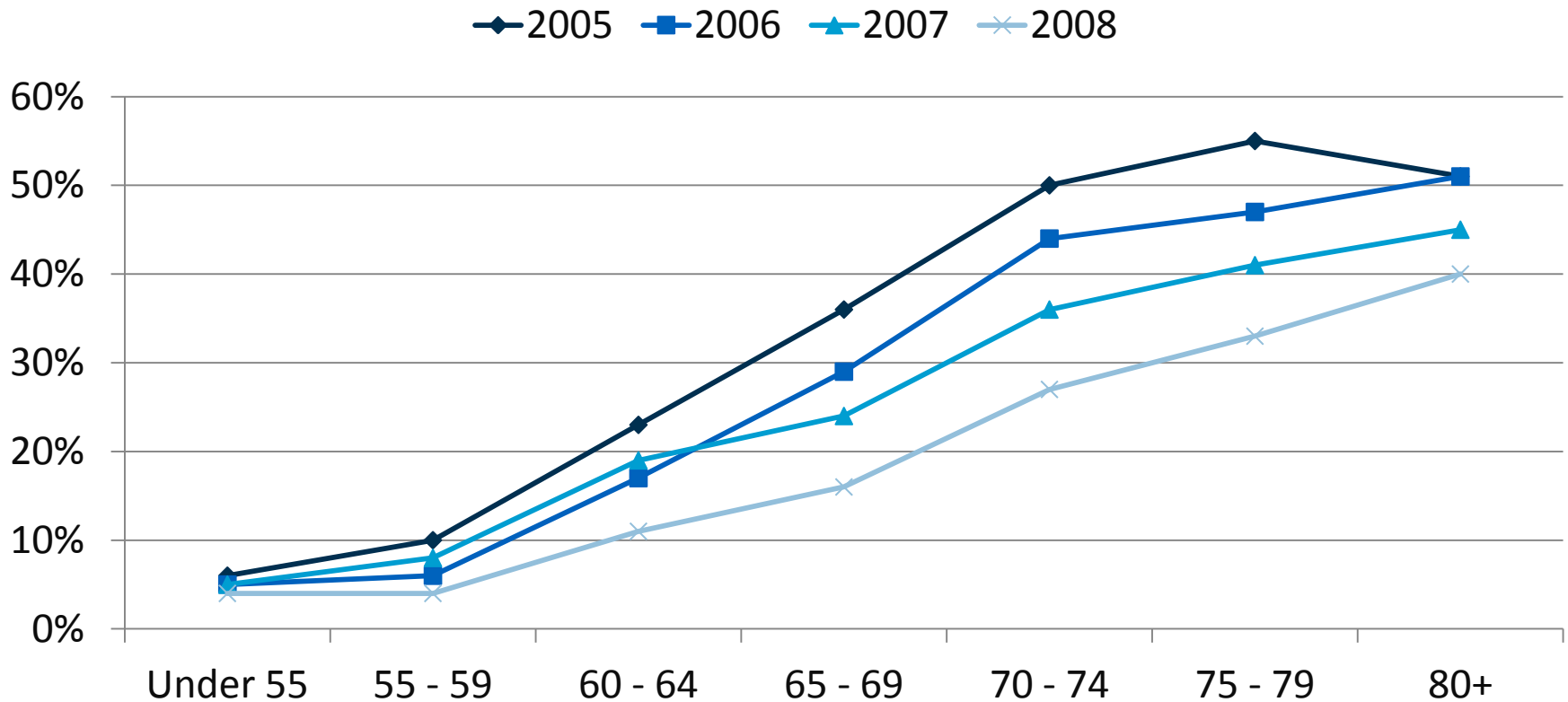
# Withdrawal-Based Variable Annuity Lifetime Income Guarantee Example



Source: Prudential Financial, Inc.

# Variable Annuity Withdrawal Activity by Age and Duration

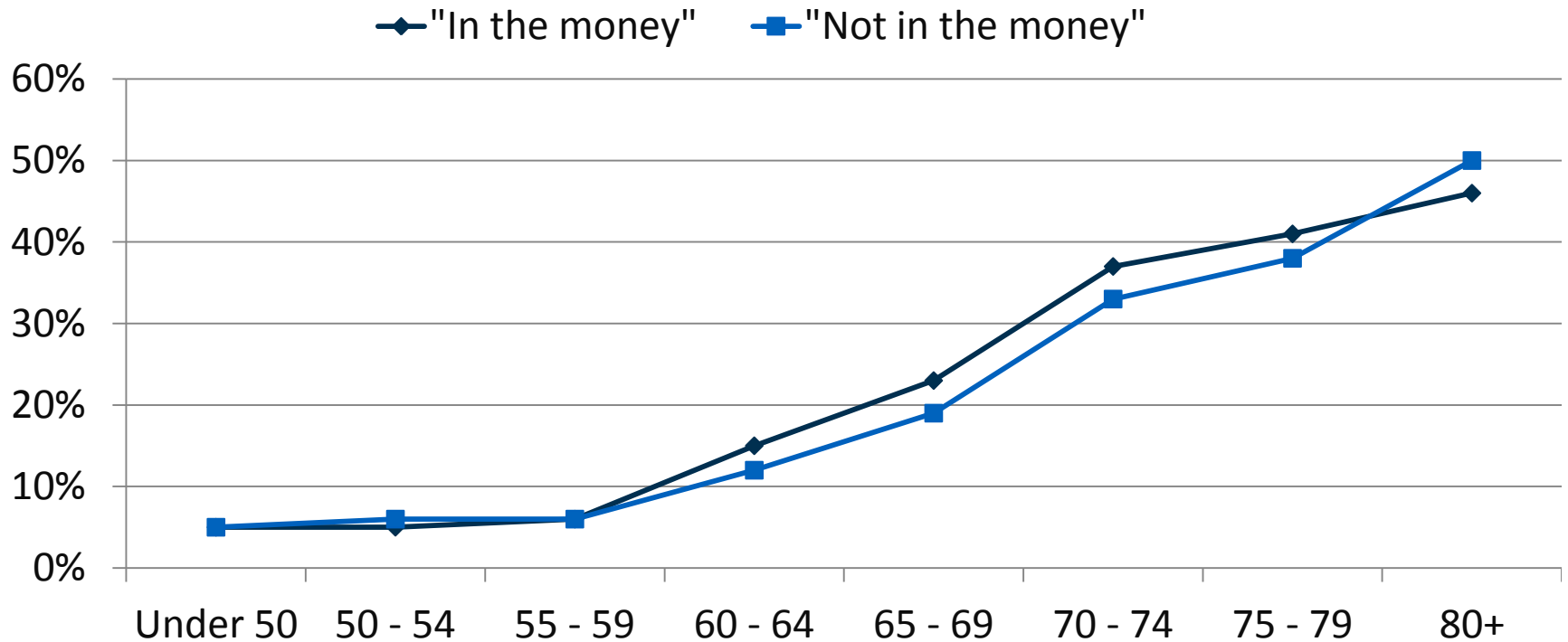
Age is a factor in predicting when one will begin withdrawals, but so is the length of time the person has owned the benefit



Source: Guaranteed Living Benefits Utilization - 2009 Data, LIMRA, 2011

# Variable Annuity Withdrawals: "In" or "Out" of the Money

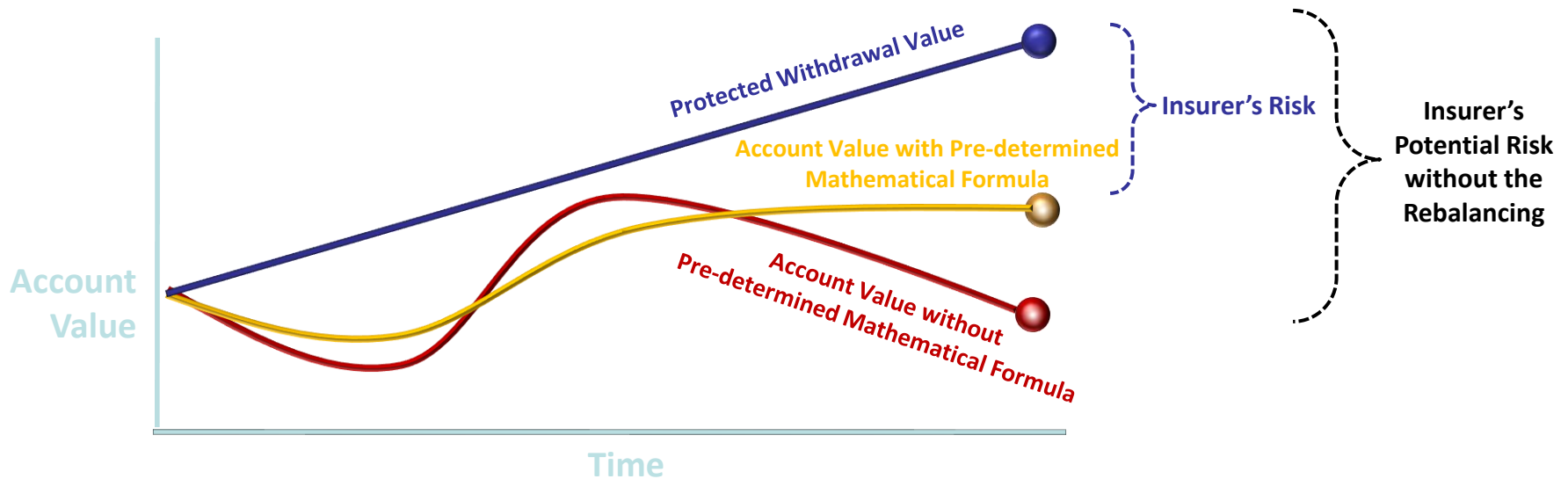
**"In the moneyness" does not significantly impact withdrawal activity**



Based on contracts issued prior to 2009 and still in-force on Dec. 31, 2009

Source: *Guaranteed Living Benefits Utilization - 2009 Data*, LIMRA, 2011

# Net Amount at Risk Illustration – Variable Annuity Withdrawal-Based Lifetime Income Guarantee



Source: Prudential Financial, Inc.

- Mandated inflation-adjusted annuities in U.K. present a special example
- Global insurers have capacity to assume systematic longevity risk
- Creating a market for longevity bonds offers advantages and challenges
- Lifetime income guarantees for personal retirement savings and DC plan assets must address consumer behavior biases
- Variable annuity "living benefits," mainly guaranteed lifetime withdrawal designs, were elected on 86% of variable annuities sold in 1Q 2011. Withdrawal-based income guarantees are now also being added to some U.S. defined contribution plans.<sup>1</sup>

<sup>1</sup> Source: *Variable Annuity Guaranteed Living Benefit Election Survey*, LIMRA, 1Q 2011