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# Variable Annuity Insurance carriers hunkering down

Despite investor demand, insurers want to steer clear of added exposure

**By Darla Mercado**
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Despite a marked increase in investor appetite for variable annuities, 2011 will go down as a year of retreat for many of the VA industry's biggest players.

The volatile stock market, coupled with a prolonged low-interest-rate environment, made it difficult — not to mention expensive — for life insurers to hedge variable annuities with living benefits. Consequently, many sought to limit their exposure to those hedging costs by exiting, or scaling back, on their VA business.

Indeed, 2011 was bookended by the exits of two big insurers from the VA market, beginning in January with Genworth Financial Inc. and ending last week with Sun Life Financial Inc. In between, a number of notable players, including Jackson National Life Insurance Co., MetLife Inc. and Prudential Financial Inc. closed the spigot on VA sales by eliminating attractive living benefits or derisking investment options.

## Hancock's Decision

In addition, John Hancock Life Insurance Co. said last month that it would withdraw an array of annuity products, including variable annuities, and limit the distribution of existing products to just a handful of broker-dealers.

“The marketplace has been diminishing over the last 12 to 24 months, and where rates are now, we're going to see people drop out of the game altogether — or reduce their benefits because they can't support the risk of such low interest rates,” said Stephen Esposito, a financial adviser with Macro Consulting Group LLC.

For advisers and their clients, the moves by insurers likely will mean less price competition among those insurers still in the market. It also means that advisers will be selling variable annuities on the basis of their tax deferral benefits, as opposed to their withdrawal benefits.

Ironically, the insurers' retrenchment comes as investor demand for the product is picking up. After two significant market downturns within a decade, many investors have pinned their hopes on the steady stream of retirement income offered by variable annuities.

This year, advisers and broker-dealers are likely either to meet or beat 2010's VA sales figures. Net sales, exclusive of product exchanges, reached a record $8.8 billion in the third quarter, up from $6.4 billion in the comparable period in 2010, according to Morningstar Inc.

Raymond James Financial Services Inc. alone sold $2.27 billion in variable annuities for the fiscal year ended Sept. 30, up from $1.84 billion in the prior year.

LPL Financial LLC reaped $591.8 million in VA commissions year-to-date through Sept. 30, reflecting a 20% increase from a year earlier.

By and large, advisers continue to send business to the three biggest sellers: MetLife, Jackson and Prudential. To some extent, negative news such as MetLife's announcement that next month, it will reduce income benefits on its variable annuities to 5%, from 5.5%, has fueled higher sales.

“For clients who were looking at the products, the reductions have helped them make that decision because they know it's going to be less generous and more expensive in the future,” said Brian Horn, an adviser at Somerset Wealth Strategies Inc., an affiliate of Raymond James.

With investor demand for variable annuities rising at the same time big insurers are backing away from the market, 2012 promises to be a sellers' market for variable annuities.

“In the short term, it puts less pressure on VA sellers to price aggressively and be innovative, which hurts advisers and clients,” said Bing Waldert, director at Cerulli Associates Inc.

Many advisers argue that variable annuities aren't worth the trouble and expense that it takes to buy them once withdrawal benefits dip below 5%.

If unattractive living benefits become the norm, insurers and advisers may decide to play up variable annuities' tax-deferred growth instead.

## Living Benefits

“Tax deferral has benefits for investors, and the annuity industry stopped talking about this to focus on living benefits,” Mr. Waldert said.

“There's a valid point in going back to annuities' root benefits,” he said. “The product development war has gone on and made it complex for insurers to price and sell annuities.”

Scott Stolz, president of Raymond James Insurance Group, agrees.

“Between fewer carriers and products' being less rich, we're going to go through a rotation phase,” he said. “You'll see a slow transition back to selling the tax deferral and death benefits.”

Kevin VanDyke, founder of Bloomfield Hills Financial, noted that though 2012 might be too early for him to sell variable annuities with an emphasis on tax deferral, 2013 might be a plum time to consider that strategy — depending on what happens to the Bush tax cuts.

“Now's not really the time to do it, but it's something we're focusing on toward the end of 2012, depending on where tax rates go,” he said.

## Tax Deferral

Indeed, at least one insurer already expects to play up tax deferral, along with the receipt of income through a strategy as opposed to using a withdrawal or income benefit rider. Such a plan is in the cards for Security Benefit Corp.

“The variable annuity in pure form is efficient accumulation, plus the ability to convert to income,” said Security Benefit chief executive Michael Kiley, who said that income strategies could include annuitization. “There's a place for living benefits, but it should never be the primary reason for buying a variable annuity.”

*dmercado@investmentnews.com*