A Pair of VA Contenders

By Editor Test *Tue, Jul 26, 2011*

Big deferral bonuses and safer investment options characterize the income riders of Nationwide and Sun Life, both of which aim to be among the leading sellers of VAs.

Nationwide and Sun Life are two financial services companies that claim to be committed to the variable annuity space and aim to be, if not one of the pace-setters, then at least among the top ten sellers. And that's about where they are today.

Ohio-based Nationwide, which took itself private a few years ago, sat in seventh place at the end of 1Q 2011, with $1.7 billion in sales, up from ninth place at year-end 2010. Canadian-owned Sun Life climbed to 10th on March 31, 2010, but had slipped to 12th by the end of the first quarter of this year.

The double-your-benefit-base-in-10 years has become the standard deferral bonus among VA contracts, and both the Nationwide Destination and Sun Life Masters offer a version of it. Nationwide's "L.inc" income rider offers a simple 10% annual rollup (or anniversary account value, if greater). The contract's age-65 withdrawal percentage, at 5.25%, is a quarter-percent richer than the typical payout.

Sun Life has introduced the Maximizer, an 8% compounded deferral bonus that can be "stacked" on top of annual step-ups, if any. The Maximizer Plus offers the additional feature of income protection; after payments begin, the withdrawal amount goes up by 2.5% each year for life.

Recently, RIJ had a chance to talk about VA strategy with Eric Henderson, senior vice president for individual investments at Nationwide, as well as with Sun Life's Steve Deschenes, senior vice president and general manager annuities, and Barbara Hume, chief marketing officer for annuities.

We asked Eric Henderson about Nationwide's ambitions in the VA space.

"We want to grow faster than the industry but at a responsible pace—not doubling our sales each year. Part of our risk management is around [product] diversification, and some is around time diversification. We grew by 30 percent last year, and this year we're growing faster than industry again. We are out there offering a consistent, simple value proposition of the highest guaranteed income from a strong and stable company.

"The fact that we've been consistent with our offer has resonated with advisors. Back in 2009, in March and in May, we pulled back a bit. We did a price increase. Then, last year, when we went from a payout of 5% to 5.25%, we raised the price again. Our research shows us that, of all the variables, the roll-up rate resonates the most with advisors. Among the bells and whistles we *don't* have is the stacking—the roll-up on top of the ratchet—or the daily or quarterly step-ups, or open asset allocation. We said, we'll place our chips on the highest roll-up.

"We put our chips there for two reasons. First, people are buying this for the guarantee, and they want the highest guarantee. Two, it's a lot easier to hedge our benefit, because we know what's going to happen. Open asset allocation and stacking adds a lot more variability. With the 10 percent roll-up, I know exactly what my bogey is year after year. We did the research, and it was the combination of the roll-up rate and the payout rate that advisors chose as the most important.

"There are a number of hurdles we need to get over. When advisors [first] hear about SALB, they drool. But when you get down to the issues, it's not so appealing. One is the state approval issue. A handful of big states don't allow it. The other big thing is the investment models that it covers. The real appeal of the SALB is that, instead of asking advisors to stop what they're doing, they can keep doing what they're doing, and wrap SALB around it. But in reality, with hedging, we end up wrapping a lot fewer portfolios than what's realistic. The question is, how do we go back to original value proposition."

"I can't go into some of the newer ideas. On these products, the benefit will never be as rich as in a variable annuity. In a traditional variable annuity, the base product stands on its own, and when you add the [income] rider, you just need to get a return on any additional capital. But without having the base product as part of it, especially where you have B share, you don't have—support is the wrong word, and it's not a subsidy.

"Here's an analogy. If you're selling a radio in a car, for instance, you're already selling the car and it's easy to add a radio. But if I were just selling a radio on a stand-alone basis, I'd have distribution and operational costs that weren't shared with the distribution and operational costs of selling the car. We're distributing through Smith Barney, but sales have not been big at all. The timing was bad—we came out in the middle of the financial crisis, just as Smith Barney was merging with Morgan Stanley, and this was put on a brand new Smith Barney platform. We have a high a percentage of the total sales on that platform, but the platform is tiny."

Sun Life is among the VA issuers that have reduced the vulnerability of their guarantees to market risk by including a hedged "dynamic asset allocation fund" into their contract's investment lineup. It was one of five companies (along with AXA Equitable, MetLife, Ohio National, and Transamerica) that are using AllianceBernstein's Dynamic Asset Allocation Porfolio (see today's RIJ story).

VA contract owners who opt for a Sun Life Maximizer or Maximizer Plus lifetime income rider must invest between 40% and 60% of their premia in one or more of five options. One is the AllianceBernstein fund. Two more are MFS Global Tactical Allocation Portfolio and PIMCO Global Multi-Asset Portfolio. The others are an SC Ibbotson Balanced Fund and Conservative Fund.

"We've tried to do a better job of managing the assets inside the VA for the long term viability," said Steve Deschenes, who came to Sun Life in 2009 and stints at Fidelity and MassMutual. "We have created core retirement funds, that have at their essence a dynamic risk management. We think of it as a volatility-managed investment with hedging strategies inside the fund.

"You're trying to capture more of the upside and less of the downside tail. You can have signals that move you in and out of asset classes. It uses out of the money puts, so that instead of managing to the return of a 60% stocks, 40% bonds fund, you can manage to volatility of 10.5.

"Going back a few years most VA issuers said, 'Invest where you want and we'll hedge to that.' Now we're saying, 'What's the right asset allocation to support both our roles?' Everyone is trying to strike the right balance. When you look at the demographics, we see long-term demand. So our feeling is that we can support that demand and provide an array of products that were comfortable with too."

Sun Life also offers an Income Riser optional living benefit that provides a 7%/ 10-year annual deferral bonus. That deferral bonus renews for a fresh 10 years at every step-up to a new high-water account value, if any. The Maximizer roll-ups do not renew at step-up. On the inflation-adjusted Maximizer Plus, the payout at 65 is just 4%–one percentage point less than the plan Maximizer.

On the marketing front, Barbara Hume said Sun Life recently published new plain-language product collateral that's intended for individual clients as well as their advisors.

"At the last IRI [Insured Retirement Institute] meeting, a group of financial advisors told us that they couldn't use most VA sales kit with clients. They said the charts were way too technical. So we had consumers work with us on how they understood the benefits. Firms have come back to say it's the first time they've seen a sales kit that can be used throughout the sales process," she said.

Since the financial crisis, Sun Life has been pursuing an aggressive branding initiative. The normally quiet company wanted to avoid being confused with SunAmerica, whose parent, AIG, generated so much negative publicity during the financial crisis. "Sun Life was having an image issue," Hume told RIJ. "When AIG was going through trouble, we were mistaken for SunAmerica."

Sun Life has intentionally sought out sponsorships that exploit the large astronomical body featured in its name. It bought the naming rights to the stadium in sunny greater Miami where the NFL's Miami Dolphins and National League Florida Marlins. It also sponsors the Cirque de Soleil acrobatic performance artists. The head of the brand initiative is Bill Webster, who, while at MetLife, was responsible for the 'if in Life' campaign," Hume said.