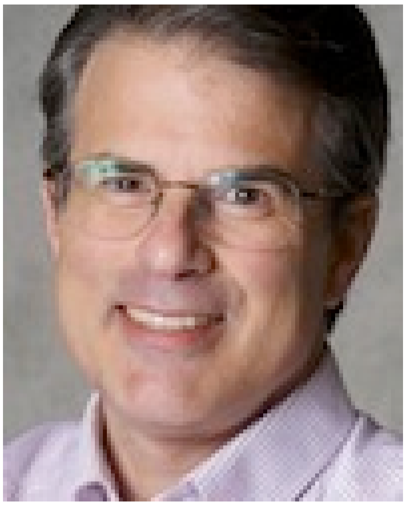
'Double Down or Get Out'

By Kerry Pechter *Thu, Jul 1, 2021*

If you haven't done so already, t's time to consider how the low interest rate environment has transformed the life/annuity business over the past ten years. And to assess the roles that reinsurers and big buyout firms continue to play in that transformation.



This week, Principal Financial became the latest life/annuity company to announce that it would focus away from selling most individual annuities. Only a day later, Ameriprise announced that it would sell in-force life insurance and annuity blocks to Global Atlantic.

One by one, for over a decade, publicly traded US life insurance companies have been trying to slip the noose of low bond yields by either a) leaving rate-sensitive businesses, b) getting rate-sensitive business off their books through reinsurance deals, and/or c) focusing on safe, stable fee-generating businesses.

Almost every major public life/annuity company has used this process to get the millstones of rate-sensitive businesses off its neck. Pressure keeps coming from the low interest rate environment, but also from their shareholders and boards of directors.

The Hartford succumbed after the Great Financial Crisis. In 2011, Harbinger bought Old Mutual, setting a pattern for more buyout company acquisitions of life insurers or blocks of in-force contract. MetLife spun off its retail annuity businesses as Brighthouse Financial.

Lincoln Financial, Jackson National, Equitable, Great American, and Voya have all done reinsurance deals, divestitures, and/or product re-tooling. Allstate sold its annuity business. AIG announced last fall that it might spin off its life/annuity businesses as a separate company.

The exceptions are the big mutuals—MassMutual, New York Life, and Northwestern Mutual—which, while not unaffected by low rates, don't have rebellious shareholders egging them to get out of annuities. Allianz Life, which is affiliated with Germany's Allianz, is also in a separate category.

The trend has accelerated since last fall, when American Equity underwent a makeover last fall. Its new CEO, freshly arrived from Brighthouse Financial, helped it fend off suitors by investing in the asset manager Brookfield, which will manage its assets.

The cellphones of reinsurers and reinsurance brokers began to ring. “We are hearing and seeing this more and more,” said Mike Kaster of Willis Re, a reinsurance broker, in an interview with *RIJ*. “Companies are asking if they should be leveraging reinsurance. They’re realizing that they need to explore it.”

Asset managers like Blackstone have positioned themselves as “insurance solutions” providers who could help troubled life/annuity companies with an efficient bundle of reinsurance and investment services. Reinsurers like Fortitude Re, which is affiliated with the $222 billion Carlyle Group, are actively seeking this type of business.

While they may have staunched the bleeding from old business, one insider told me, all life insurers still have to decide what kind of business they want to be in the future. They can either double down on the annuity business—as MassMutual did by purchasing Great American, a robust fixed indexed annuity issuer—or they can find a fee-based business that grows with the stock market. In any case, there will be further industry concentration to achieve economies of scale.

Is this trend a good thing? One person says it reflects the benefits of specialization. Life insurers are good at selling annuities and servicing customers. Reinsurance specialists can back the liabilities more cheaply than US life insurers can. Massive asset managers like Blackstone, KKR, Carlyle or Apollo can originate and securitize high-yield loans. With higher returns, they can in theory offer policyholders better pricing. In any case, the alternative is to let life insurers take huge losses or even fail.

One other point that was impressed on me: The ‘Bermuda Triangle’ strategy has matured over the past decade. When Harbinger bought Old Mutual, and then Apollo created Athene, no one knew where the trend would lead. Would Wall Street ‘buccaneers’ force wounded life insurers into one-sided agreements? Today, I’m told, the business is civilized and life insurers know how to protect themselves and their policyholders.

So what could possibly go wrong? People outside of the deals are wary of them, especially if they can’t see exactly what assets are backing the liabilities.

Some observers note that the asset managers are taking too much risk by bundling dicey loans into CLOs (collateralized loan obligations) and selling the investment-grade senior tranches to life insurers or reinsurers. These observers are reminded of the CDOs of the

Great Financial Crisis, and not in a good way.

Others worry that as in-force annuity contracts get sold, and perhaps resold, that there will be breakdowns in administration and customer service. (It has already happened, at least twice.) Companies who put the shareholder’s interest ahead of the policyholder’s by going public are now, if owned by private investors, putting the investors’ interests first.

Going forward, the public will have fewer sources of the kinds of pooled retirement income products that it arguably needs. Instead, people might be offered products tailored to the needs of the life insurer’s asset manager. If the industry consolidates, it might lead to greater economies of scale; but there’s no guarantee that policyholders will benefit from them.