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Drama in Des Moines

By Kerry Pechter *Wed, Oct 21, 2020*

Rejecting a takeover bid by Athene and MassMutual, fixed index annuity issuer American Equity will partner with Brookfield Asset Management. The deal releases up to $350m in capital for American Equity, and makes it a 'Bermuda Triangle' player. Photo: AEL headquarters in Des Moines.

Having spurned a takeover bid from insurance giants Athene Holding and MassMutual a few weeks ago, tiny American Equity Investment Life Holding Company, a leading issuer of fixed index annuities (FIAs), announced a deal this week with Brookfield Asset Management, Inc. [For related story, click **here**.]

Brookfield will reinsure $5 billion of its existing FIA liabilities and up to $5 billion more in the future. It will also acquire a 19.9% ownership interest in the common shares of American Equity. American Equity will use the Brookfield equity investment and cash on hand to buy back up to $500 million of its common shares, thus offsetting the dilution created by issuing new shares to Brookfield. The repurchases will begin after the third-quarter earnings report.

This deal, combined with its partnerships with Agam Capital and Varde Partners (see below), gives American Equity all the elements it needs—a life insurer to issue fixed index annuities, an offshore reinsurer for capital arbitrage, and a private equity specialist for "liability origination"—necessary for it to practice the **"Bermuda Triangle"** strategy, as rivals Athene and Fidelity & Guaranty Life do.

In a release, American Equity said the deal will allow it and its stakeholders "to benefit from exposure to differentiated alternative asset strategies with long-term, contractual cash flows and deploy significant capital into proprietary Brookfield investments."

MassMutual and Athene sent a letter to American Equity on Sept. 8, offering to buy the company for $36 a share in a deal valued at $3 billion, according to the Des Moines Register. Brookfield offered $37. After the *Wall Street Journal* reported the deal on October 1, the stock price rose about 50%. The price dropped suddenly to about $26 on October 19, after the deal was cancelled. Athene, like American Equity, is based in Des Moines, Iowa.

American Equity said this week:

"After careful review with the assistance of its financial and legal advisors, American Equity's Board unanimously determined that Athene and MassMutual's unsolicited, non-binding proposal made public by Athene on October 1, 2020 is opportunistic, significantly undervalues the Company, and is not in the best interests of American Equity and its shareholders and other stakeholders."

These events add a new episode to the story of annuities over the past five years. Private equity firms have been buying or partnering with fixed annuity issuers. The deals are mutually beneficial. On the one hand, they give insurers access to the private equity firms' investment skills at a time when low interest rates make it hard for issuers to keep promises made when rates were higher.

For their part, private equity and asset management firms get access to multi-billion blocks of fixed annuity liabilities. They can re-invest some of the general account assets underlying those liabilities in high-yield asset-backed securities. They can also sell blocks of annuity business to captive reinsurers in foreign havens like Bermuda that have lower reserve requirements. According to AM Best, the ratings agency, the reinsurance deal with Brookfield will free up as much as $350 million in regulator capital for American Equity.

American Equity, Agam and Varde

Founded in 1995, American Equity has fewer than 700 employees. But it has been a leading seller of FIAs in the independent agent channel for almost two decades. It also has some $53 billion in policyholder funds under management. Those funds stand to be better invested by American Equity's recently added asset management partners—Agam Capital Management, Varde Partners and now Brookfield.

Brookfield's equity investment in American Equity will take place in two stages: an initial purchase of a 9.9% equity interest at $37.00 per share (promptly following **Hart-Scott-Rodino** approval), and a second purchase of a 10.0% equity interest, at the greater value of $37.00 per share or adjusted book value per share (excluding AOCI and the net impact of fair value accounting for derivatives and embedded derivatives).

The second equity investment is subject to finalization of certain reinsurance agreement terms, receipt of applicable regulatory approvals and other closing conditions. It is expected to close in the first half of 2021.

Brookfield agreed not to transfer any common shares purchased in the equity investment for a period of two years after the applicable closing of the investment, as well as to customary standstill restrictions until the five-year anniversary of the initial equity investment. Brookfield will also receive one seat on American Equity's Board of Directors following the initial equity investment.

In the release, Anant Bhalla, president and CEO of American Equity, said: "This partnership accelerates the transformation of our business toward a ROA model from our historical focus on ROE, unlocks new investment opportunities, and enables us to deliver significant value to our shareholders and policyholders."

According to the release, the transaction:

- Provides access to Brookfield's higher-returning alternative asset strategies, which may generate sustained returns in a low interest rate environment.
- Provides access to permanent capital and supports new products, including IncomeShield.
- Accelerates the transformation of American Equity's business model from return on equity (ROE) toward return on assets (ROA) and releases capital available for share repurchases, organic growth, and strategic initiatives.
- Builds on AEL's **partnership** with Värde Partners and Agam Capital Management, LLC.

Regarding the buyback of $500 million in shares, the specific timing of repurchases and the exact number of common shares to be purchased will depend upon market conditions and other factors, the release said. Under the repurchase program, repurchases can be made using a variety of methods, including open market purchases.

J.P. Morgan and Morgan Stanley & Co. LLC are serving as financial advisors to American Equity. Ardea Partners is serving as exclusive financial advisor to American Equity in the Brookfield transaction. Skadden, Arps, Slate, Meagher & Flom LLP is acting as legal counsel to American Equity.

Brookfield Asset Management is a global alternative asset manager with approximately US$550 billion of assets under management across real estate, infrastructure, renewable power, private equity and credit. It owns and operates long-life assets and businesses, and offers alternative investment products to public and private pension plans, endowments and foundations, sovereign wealth funds, financial institutions, insurance companies and private wealth investors.

Following the transaction, AM Best said that the Financial Strength Rating of A- (Excellent) and the Long-Term Issuer Credit Ratings (Long-Term ICR) of "a-" of the members of

American Equity Investment Group (Iowa) remain unchanged following its announcement that Brookfield Asset Management Inc. will acquire a minority interest in American Equity Investment Life Holding Company (AEILHC) (West Des Moines, IA). Concurrently, AM Best has commented that the Long Term ICR of “bbb-” of AEILHC and its existing Long-Term Issue Credit Ratings also remain unchanged. The outlook of these Credit Ratings is stable.