Fewest Open Variable Annuity Contracts Since 1997: Morningstar

By Michael Manetta *Fri, Apr 19, 2019*

The top ten VA issuers stayed much the same and accounted for 83% of total sales. TIAA dropped to fourth place from second and AEGON/Transamerica replaced New York Life in the top ten, writes Morningstar's senior quantitative analyst.

New sales of variable annuities (VAs) came in at $22.5 billion in the fourth quarter of 2018, a 4.3% decline compared to a year earlier but in line with average quarterly sales figures over the past two years.

Sales of VAs with guaranteed living benefits posted a fifth consecutive quarter of positive year-on-year (y/y) sales growth, versus negative sales growth for VAs without a living benefit in three of the past five quarters (including Q4).

Sales shifted away from some traditional market leaders and toward newer VAs offering more generous living benefits and/or negative return protection. The ten top-selling VA issuers stayed much the same and accounted for more than 83% of total sales. TIAA dropped to fourth place from second and AEGON/Transamerica replaced New York Life in the top ten.

Among the five leading sellers, Jackson National remained the overall leader by a wide margin but AXA, Lincoln Financial and Prudential all gained market share at the expense of Jackson National and TIAA.

Jackson National introduced the only new VA in Q4 of 2018, the Elite Access Advisory II I-share. With no M&E fee and only a $240 annual fee, the contract is one of only about 10 deferred VAs currently available with no explicit asset-based fee linked to longevity risk. The product offers no living benefit riders.

Three of the best-selling VA contracts over the past several years—Jackson National's Perspective II (7-year), TIAA-CREF's R1, and Riversource Life's RVS RAVA5 Advantage (10-year)—saw new sales fall by a combined $1.377 billion, or 22%, in the fourth quarter compared to a year ago, equivalent to a five-percentage-point decline in market share in just one year.

There were three newcomers to the top 10 contracts in sales, including two VAs issued within the previous 12 months.

Pruco's Defined Income and Premier Retirement O-share policies were two of the fastest-growing VAs, thanks to strong living benefits. Defined Income jumped to sixth place from 12th place in sales, while Premier Retirement moved up one place, to third.

Each Pruco VA offers a guaranteed minimum withdrawal benefit (GMWB) with annualized step-ups equivalent to 6.3 and 5.5 times the associated benefit fee, corresponding to minimum withdrawal percentages for a 65-year-old of 6.3% and 5.8%, respectively. Perspective II and RVS GMWBs have step-up-to-fee ratios of 4.0 and 4.8 respectively, corresponding to guaranteed withdrawal fees for a 65-year-old of 5%.

Registered index-linked annuities (RILA) saw continued sales growth. Also known as structured, buffered, or hybrid annuities, these products include VAs that offer both variable- and fixed-indexed-like investment options. Others are effectively fixed-indexed annuities (FIAs) attached to a VA chassis.

Morningstar collects only sales data on the former, which we estimate accounted for around 65% of all the RILA sales in Q3 2018. Consistent with the booming popularity of pure FIAs, RILAs have seen significant sales growth in recent quarters, including Q4.

We estimate approximately $2.3 billion in the mixed-RILA space, equivalent to around $3.1 billion for the entire RILA space if we use our "65% rule." That equals nearly 14% of all VA sales in the fourth quarter, compared to about 10% a year earlier.

Heightened market volatility may have contributed to the shift in VA sales patterns in Q4. GMWBs and RILAs are designed to protect against losses, but flows into managed volatility subaccounts did not increase despite a volatile market environment.

VA contract issuance and closures

Only one new variable annuity contract (VA) was issued in the fourth quarter, bringing the 2018 total to just 13 new contracts versus an average of roughly 33 per year over the 2014-17 period.

New issuance has failed to keep pace with contract closures. The number of VAs open to new investors has continued to decline: excluding New York-only contracts, there were only about 300 open VAs at the end of 2018. By our count, that is the fewest number of open contracts since 1997.

The lone VA brought to market in Q4 was an I-share from Jackson National. I-shares, also known as fee-based contracts, now account for around 22% of the open VA universe, up from 15% three years ago.

The lack of commission is attractive to investors looking to minimize costs at purchase, while uncertainty about the future of trail commissions—particularly following recent events concerning Ohio National—has made fee-based compensation that much more appealing to advisors.

VA benefit changes

Sun Life introduced a new guaranteed lifetime withdrawal benefit (GLWB) in the fourth quarter. At 0.30% for the single beneficiary version, the fee for the new Sun Life GLWB is among the lowest in its cohort. The benefit is available through the company's Masters Prime VA, introduced in September, which has total annual expenses of 1.2%, above average but in line with other recent-vintage VAs.

The total number of available GLWB riders in the VA space was 112 as of end-2018, up from 94 a year prior and 66 three years ago. Such growth has coincided with the significant increase in sales of fixed indexed annuities (FIAs), many of which also offer an optional GLWB.

VA GLWBs tend to cost about 20 basis points more on average than their FIA counterparts, but the potential size of VA withdrawal benefits can be much larger. VA carriers offering GLWBs appear to be trying to compete by offering lower fees, as Sun Life has done.

Pacific Life lowered fees on several of its existing GLWBs in the fourth quarter. Fees on the CoreIncome Advantage Select series—which is still available to new investors—declined by 10 to 25 basis points. Fees on several other (closed) Pacific Life GLWBs also declined.

There were 22 non-fee-related benefit changes in Q4, many of them increases in withdrawal rates, which enrich the benefits without increasing the cost.

In the pipeline (based on preliminary SEC filings)

Prudential Annuities is preparing to release a new I-Share, called the Premier Advisor.