MetLife, Sun Life feel the pressure from low interest rates

By Editor Test *Wed, Nov 2, 2011*

MetLife's reduction of the deferral bonus on its hot-selling GMIB Max VA rider by a half-percent and news that Sun Life's strength rating is under review are symptoms of the impact of ultra-low interest rates on VA issuers.

With low interest rates driving up the costs of hedging variable annuity living benefits, MetLife announced that it will reduce the deferral bonus on the benefit base of its recently-introduced GMIB Max product from 5.5% to 5%, the company said in a release.

“As of January, the roll-up rate on our GMIB Max product will be reduced from 5.5 percent to 5 percent,” MetLife CEO Steven Kandarian told analysts in a conference call last Friday.

The announcement by MetLife, which was the top seller of variable annuities in the second quarter of 2011, coincided with A.M. Best’s announcement that it would review Sun Life Financial’s strength rating. Sun Life, also hurt by the turbulent stock market and low interest rates, said it expected to lose $621 million in the third quarter of 2011.

The Federal Reserve has said that it may keep benchmark rates near zero through mid-2013 as long as unemployment remains high and the inflation outlook stays “subdued.”

MetLife’s third-quarter variable annuity sales jumped 84% from a year earlier to $8.6 billion, the New York-based company said yesterday. Some of the increase may have been driven by customers who wanted to lock in rates before the terms changed, the insurer said on the conference call.

The following information comes from reporting by Bloomberg on MetLife’s conference call.

“The $8.6 billion variable annuity sales result was record breaking, though we are concerned that this new business would be well below targeted returns given the current low-rate environment,” Randy Binner, an analyst with FBR Capital Markets, said in a research report. “We expect the company to actively manage sales to a more appropriate level.”

MetLife is expanding in retirement products as it retreats from banking. The company, working to sidestep tighter capital rules enforced by banking regulators, is seeking a buyer for its deposits-gathering business and considering the sale of its mortgage operation. The divestitures are “on track” and the company may wind the businesses down if it can’t find a buyer, Chief Financial Officer William Wheeler said today.

“Probably Plan B, though I think this would be an extreme scenario, is we would wind it down,” Wheeler said. “But I think a sale is much more likely.”

Profit at MetLife’s bank unit fell by half to $51 million in the third quarter due to higher expenses, the company said. Operating revenue rose 4 percent to $425 million. MetLife Bank had $17.7 billion of assets and $10.7 billion of deposits at the end of September.

MetLife beat analysts' estimates when it announced that third-quarter operating profit was $1.11 a share. Net income surged more than 10-fold to $3.58 billion, helped by gains in derivative hedges. The yield on 10-year U.S. Treasuries plummeted 39 percent in three months to 1.915 on Sept. 30.

Kandarian was ordered by the Fed to scrap his plans to resume share buybacks and raise MetLife's dividend, the insurer said this week. MetLife, which as an insurer is regulated by the U.S. states, is "well capitalized" and will seek approval for an increase early next year, Kandarian said in a statement.

"We want to return capital to shareholders," Kandarian said on the call. "The hope is that over time people in Washington will understand the difference between the banking business model and the insurance business model."

The A+ (Superior) financial strength ratings and "aa" issuer credit ratings of the core life insurance subsidiaries of Toronto-based Sun Life Financial Inc. have been placed under review with negative implications by A.M. Best Co., the ratings firm reported.

The subsidiaries include Sun Life Assurance Company of Canada, Sun Life Assurance Company of Canada (U.S.), Sun Life Insurance and Annuity Company of New York and Sun Life and Health Insurance Company.

The "under review" status follows Sun Life's estimate that it expected to lose $621 million for the third quarter of 2011.

"The results for the third quarter were impacted by substantial declines in both equity markets and interest rate levels. Due to the sensitivity of SLF's U.S. individual life and variable annuity businesses to these market changes, its U.S. operations were most impacted. In addition, SLF's fourth quarter results are expected to include a methodology change of $500 million related to the valuation of its variable annuity and segregated fund liabilities, which will provide for the estimated future lifetime hedging costs of these liabilities," A.M. Best said in a release.

Despite the expected losses, A.M. Best notes that SLF and its operating subsidiaries remain well capitalized from a risk-adjusted perspective.

By placing the ratings under review, A.M. Best can conduct an analysis of the full third quarter 2011 financial results, which will include both an enterprise and legal entity review.