What Are Sales Trends Telling VA Issuers?

By Editor Test *Wed, Feb 29, 2012*

Investors were running scared after 3Q equity market turmoil. But they didn't flock to variable annuity guarantees for protection.

Although variable annuity sales fell 4.6% in the fourth quarter of 2011, they managed to finish the year at $153.4 billion, up 12.3% from the $136.6 billion at year-end 2010. But that was well below the 2007 high-water mark of $179.5 billion, according to year-end sales data from Morningstar's Annuity Research Center.

As in the past, most of the new sales transactions were simply exchanges of existing contracts for new contracts. Net new cash flow for the year was just 18% of total sales, or $27.7 billion. That was up from only $21.7 billion in 2010 but well below the high of $46 billion back in 2003.

MetLife repeated as the quarter's top seller, with $7.23 billion and a 21.7% share of individual annuity sales (19.7% of all variable annuity sales, including group sales). "MetLife has stated their objective to drive to greater balance across product lines, however, so their market share will likely drop in 2012," said Frank O'Connor, Product Manager at Morningstar's Annuity Research Center, in a release.

Prudential Financial (the 2010 sales leader) came in second, followed by Jackson National Life, TIAA-CREF (a group annuity specialist) and Lincoln Financial Group. These five companies accounted for more than 55% of total sales. (A table of the top ten VA sellers for Q4 and all of 2011 is below.)

Variable annuity issuer	Q4 2011 sales ($bn)	2011 sales ($bn)
MetLife	7.23	28.44
Prudential Financial	4.41	20.24
Jackson National Life	3.76	17.49
TIAA-CREF	3.41	13.54
Lincoln National	2.17	9.32
Nationwide	2.07	7.38
SunAmerica/VALIC	2.02	7.98
AXA Equitable	1.74	6.87
Ameriprise	1.56	6.40
AEGON/Transamerica	1.38	5.25
Source: Annuity Research Center, Morningstar, Inc.		

The VA industry continues to consolidate, mainly because the product demands the kind of sophisticated hedging programs, robust wholesale forces, brand strength, financial strength, and economies of scale that only a few companies have achieved.

Just a few major companies saw sales increases in 4Q 2011. Nationwide's sales rose more than 20%, to $2.07 billion. That raised its sales rank to sixth from ninth. TIAA-CREF, AXA Equitable, AEGON/Transamerica, Ohio National, Northwestern Mutual, Guardian and MassMutual also added modestly to sales.

VAs remain something of a puzzle. Despite the fact that Americans are getting older and more risk-averse, there's still no clear indication that Boomers are gaining an appetite for variable annuities—a product that actuaries and marketers have spent over a decade custom-tailoring for precisely their situation. Variable annuities are surviving, but the VA market should be much bigger than it is.

The perennial objection to VAs is that they are expensive. Part of that expense stems from their primary method of distribution. According to Morningstar's report, insurers rely on commissioned brokers for 98% of VA sales. It takes generous incentives and product features to win that business, but those factors add cost to the product. Simpler, cheaper contracts are available—contracts built to appeal to fee-based advisors or to the direct-sold market—but they aren't getting much traction.

If marketers are trying to position VAs as all-season products, the message doesn't seem to be getting through. VA sales are still correlated with equity market performance. If investors perceived VAs as a form of protection, then VA sales should have gone up in the fall, after the big volatility storm in August spooked investors. Instead, sales went down, which suggests that the public still doesn't understand or appreciate the risk-mitigating aspect of the product. VA sales are also correlated with the generosity of the product features, such as payout rates and deferral bonuses, but the financial crisis and recent volatility have forced insurers to make products more austere.

In his quarterly commentary, Morningstar's O'Connor was hopeful that less-expensive, more client-friendly variable annuities might finally break through in 2012. "An area to watch this year is the development of new low-cost, advisor-sold products offering living benefits, such as Transamerica's Income Elite product, which offers both single and joint lifetime withdrawal benefits for a 1.25% annual fee on top of a base product cost of 0.45% for an all-in insurance cost of 1.70% per annum as compared with the industry average of 2.75%," he wrote.

O'Connor pointed out that "Historically, advisor-sold products have captured around 2% of the overall VA market, with most such 'simplified' annuities failing to generate significant sales; will it be 'different this time,' to use a financial markets aphorism? If investor demand grows, perhaps fueled by the combination of longevity, return, tax, and inflation expectations, we may finally see the market develop for these products. But for now the broker-sold, fully-commissionable product is getting 98% of the business."

Assets under management in variable annuities were essentially unchanged in 2011 relative to 2010, closing out the year at $1,502.3 billion vs. year-end 2010 assets of $1,504.4 billion. These assets have gradually become concentrated in fewer hands over the past decade.

Eight of the 37 firms that reported their sales results to Morningstar accounted for 75.4% of the individual VA assets in 2011, compared to the 12 of 44 firms sharing 73.8% of the individual market in 2001. The top five firms by individual product assets were MetLife (13.4%), Prudential (10.5%), Lincoln Financial (7.8%), and Hartford (6.6%), according to Morningstar.

More than 60% of variable annuities continue to be sold either through independent broker-dealers or captive agents. Banks, wirehouses, and regional broker-dealers contribute about 10% each to overall sales. In the fourth quarter of 2011, MetLife was the sales leader in banks/credit unions, independent broker/dealers, regional broker/dealers, and wirehouses. It was second to TIAA-CREF in captive agency sales.