

## Why American Equity's Share Price Spiked Today

By Kerry Pechter     Thu, Oct 1, 2020

*With new management and a new business model, American Equity Investment Life hopes to climb back onto the FIA sales leaderboard. It's using the strategy that RIJ dubbed 'The Bermuda Triangle' in two stories six weeks ago.*



It's now clear what American Equity intended when it hired Anant Bhalla, a former Brighthouse/MetLife financial star, as its new CEO last January. He was brought in to guide the publicly-held fixed indexed annuity (FIA) issuer into what *RIJ* calls the "[Bermuda Triangle](#)."

[Editor's note: As we were publishing this article last week, the news about Athene and MassMutual's takeover of American Equity broke in the *Wall Street Journal*. So our claim to explain the reason for the explosion in AEL share prices was completely wrong—but not really. The information in this article may offer some context for the acquisition, and may even help explain why this deal went through when previous flirtations between AEL and acquirers did not.]

Bhalla appears to be replicating the three-part business formula—including life insurer, private-placement debt shop, and Bermuda-based captive reinsurer—that Athene Holdings, Fidelity & Guaranty Life and others have been using to climb the FIA sales chart in recent years. American Equity dropped out of the top 10 sellers of FIAs in 1Q2020, after two decades as a regular top-five finisher (top three in the independent-agent channel).

The architecture of the new strategy was revealed this week, when Des Moines-based American Equity (American Equity Investment Life Holding Company; AEL), with \$53 billion in policyholder assets, announced that it has teamed with [Värde Partners](#) and [Agam Capital Management](#) in a move to vastly improve AEL's investment game—and, ideally, make its FIA crediting rates more competitive.

American Equity Holding's first quarter FIA sales (including units American Equity and Eagle Life) were \$739.6 million, eleventh highest in the industry. In 2Q2020, after a cut in interest rates hit all life insurers, the company's sales dropped to \$559 million. Average investment yield fell to 4.12% from 4.36%.

The firm's share price spiked today, rising from \$22.01 at close yesterday to \$33.99 at 9:30 a.m. this morning, before falling back to just under \$31 at midday. (Most investors evidently found out about the deal from mass media today, missing the press release on Monday.) The price was \$33.52 last February 14. Before that, its previous peak was more than \$37 in August 2018, when the Fed's downward push on interest rates began hurting life insurers' investment returns.

Värde Partners, Inc., specializes in "corporate and traded credit, real estate and mortgages, private equity and direct lending." Agam Capital Management, a New Jersey-based asset manager, describes itself as a "one-stop operating platform to price, value and risk-manage the entire gamut of life and retirement businesses globally."

Under the terms of the agreement:

- Värde will establish a Bermuda reinsurance company that would reinsure \$5 billion of American Equity fixed index annuity liabilities. The deal will reduce capital requirements for the block by 7%, releasing \$350 million to AEL.
- American Equity and Värde will also jointly establish an asset management entity to provide insurance asset management services to the reinsurance company.
- American Equity is intended to have a significant minority interest in the new reinsurer and a 35% interest in the newly formed asset manager.

Bhalla, American Equity's CEO, came from Brighthouse Financial, where he was CFO of the U.S. retail business and co-led its spin-off from MetLife. In 2012, his Bhalla Capital Management firm specialized in aggregating and refinancing annuity blocks. Before that, he worked at American Express, Ameriprise and Lincoln Financial.

Chak Raghunathan, president and COO of Agam, was chief risk officer at Apollo Global Management when Apollo established the three-part strategy, from 2008 to 2014.

Värde (Swedish for "value") was founded in 1993 by three Minnesota alternative investment pioneers, George Hicks, Marcia Page and Greg MacMillan. The firm specializes in several of the same relatively high-yield asset categories and strategies that Bermuda Triangle life insurers now look for: commercial real estate, private placement, opportunistic credit and capital structure arbitrage.

This week, AEL also announced the hiring of Equitable Holdings veteran Graham Day to run Eagle Life, the AEL holding company subsidiary that markets FIAs in the broker-dealer channel. Kirby Wood, American Equity's chief distribution officer, left the firm after 15

years in June 2020.

The Bermuda Triangle model has, in a sense, rescued the annuity industry from ruin by chronic low interest rates after the Great Financial Crisis (GFC). Low yields on traditional investments, such as high quality corporate bonds, threatened their ability to earn enough to service their large blocks of fixed annuity liabilities. Relatively tiny investment teams at traditional life insurers didn't have the resources to hunt down higher-yielding yet still-suitable investments.

Private equity (PE) firms, by comparison, have armies of credit analysts who can do that. Firms like Apollo, Guggenheim Partners, Blackstone, Goldman Sachs and others saw opportunities to acquire blocks of in-force fixed annuity business and then reinvest the underlying assets to, ideally, greater effect. In some cases, the asset managers bought life insurers and began selling new fixed annuities. (See today's story on [Aspida](#).)

The asset managers used their more sophisticated, algorithm-driven, labor-intensive "loan origination skills" to lend to cash-hungry private companies when bank lending to them dried up (a result of post-GFC regulations). They also bundled and securitized these loans. PE-led firms were able to generate returns great enough to service old blocks and issue competitive new contracts.

According to a senior executive at one of the new breed of fixed annuity issuers, the "liability origination skills"—the ability to create and place customized private equity loans—of the practitioners of this model can give them a decisive 20-basis point average investment yield advantage.

The triangle model also includes a captive offshore reinsurance company in a jurisdiction with less stringent reserve requirements for backing insurance liabilities such as in-force blocks of FIAs. Life insurers can sell blocks of FIA assets and liabilities to a Bermuda-based reinsurer, which then credits excess capital back to the life insurer. In this case, the process yielded \$350 million to American Equity's holding company.

In the second-quarter of 2020, Athene used the model to unseat long-time leader Allianz Life as the top seller of fixed annuities in the U.S. Allianz Life was second, followed by Fidelity & Guaranty Life (a historic leader in indexed annuity sales which now collaborates with Blackstone on the three-way model), AIG, and Sammons.

(In August, *RIJ* asked Allianz Life if it uses the Athene model, with a captive offshore reinsurer. A spokesperson for the life insurer said it does not. We asked the same question

of Great American Insurance Group, another major FIA issuer, but no one was available to comment.)

In reporting its 2Q2020 financial results, American Equity said, "Policyholder funds under management at June 30, 2020 were \$53.1 billion, a \$203 million, or 0.4% decrease from March 31, 2020. Second quarter gross and net sales were \$559 million and \$553 million, respectively, representing decreases of 63% and 61% from second quarter 2019 sales. On a sequential basis, gross and net sales decreased 21% and 20%, respectively. Compared to the first quarter of 2020, gross sales at American Equity Life and Eagle Life declined 18% and 34%, respectively."

In late June, American Equity Life launched the Destinations 9 & 10 fixed index annuity, which includes the Destinations index the life insurer co-developed and co-branded with Bank of America, to the independent agent channel, according to a news release. This index uses a rules-based, multi-asset sector strategy that combines investing in low volatility S&P500 equities, 10-year US treasury bonds and gold. The products haven't changed much, but it's a whole new game for American Equity.

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