8 notable trends in the VA business

Annual variables

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Variable annuities are at a turning point in product development, as insurers juggle a desire to remain in the market without saddling their books with even more long-dated risk. Life insurers are suffering from lengthy periods of low interest rates, which dampen the returns they earn on bonds and raise the cost of hedging living benefits – the lifetime income riders that are so popular with clients. As a result, companies are taking steps to back away from those long-dated features and are testing out different product models. The constant parade of new and revised will not make things any easier for advisers or their clients.

Here, then, are eight of the more notable trends that will ripple the VA lake in 2013.

8. Advisers get their share

Advisory share classes will become commonplace among insurers. Sixty-three I share variable annuities are in the market now, compared to 34 last year, noted John McCarthy, product manager of annuity solutions at Morningstar Inc. Just last December, Nationwide released Destination Income, a new I share VA contract that's available for rollovers from the firm's own qualified plans. Generally, these products are low cost so that the adviser can add in an advisory fee.

7. Cash money paid

(Photo: Bloomberg News)

Buyouts of legacy variable annuities, another method for insurers to get out from under their liabilities, will be closely watched this year. Settlement offers from Transamerica, AXA and The Hartford are giving clients a boost in account value if they agree to walk away from their guaranteed benefits. Hartford’s offer is the most recent as the firm filed with the SEC a detailed document explaining the deal on Dec. 28. Advisers are skeptical of the offers, but time will tell whether customers take up the insurers on the opportunity.

6. Enough with the rollercoaster already

Expect funds that use volatility management to become a fixture among VA investment offerings. Late last fall, Nationwide added a group of volatility management funds to the roster for its guaranteed lifetime withdrawal benefit, the Nationwide Lifetime Income Rider or L.inc. Those options included the TOPS ETF portfolios, an offering from Milliman and ValMark Advisers. Similar offerings are available at a number of other insurers, including up-and-coming VA provider Ohio National Life. “Volatility management is going mainstream and going hand-in-hand with the living benefits,” said Morningstar's McCarthy.

5. P-E flyers

As life insurers look to shed problematic blocks of legacy variable annuity business, expect private equity buyers and other big investors to jump in. Late last year, Sun Life sold its VA block to Delaware Life, a Guggenheim Partners company. Cigna followed that up when it reached an agreement in February with Berkshire Hathaway Life to have the company assume Cigna's exposure to up to $4 billion in VA living and death benefits. The move gave hope to the industry that while VAs have proven difficult for some insurers, there's a buyers' market that's willing to snap up the businesses.

4. No more 'Night of the Living Benefits'

Extending the trend of backing away from lifetime income, experts predict insurers will go the route of Jackson National Life. Jackson offers VAs that are largely investment-focused, with an eye toward tax inefficient investments, like alternatives. Generally, these contracts don't offer lifetime income features. Such products permit insurers to stay in the VA business without pushing living benefits that will eventually add to their long-term liability and interest rate exposure.

3. Jois de fee

Stop us if you've heard this one before: Higher fees are coming. Indeed, if there is one thing clients can count on, it's that fees on annuity contracts will climb across the board. Ratcheting to fees accounted for 37 out of 101 total VA contract changes filed with the SEC during the fourth quarter. Not everyone is hopping on the fee-hike bandwagon, however. AIG's VALIC cut back fees on a couple of products, including a 20 bps reduction to 1.10% on its Income LOCK 8 Lifetime GMWB, according to Morningstar. The withdrawal percentage at age 65, though, fell to 4.75% from 5%.

2. The 4% solution

MetLife Inc. shook up the VA industry in January when word got out about its Guaranteed Minimum Income Benefit Max V, a product feature that will raise clients' benefit base by 4% each year and allow 4% dollar-for-dollar withdrawals. Though the insurer predicts that 4% is as low as it will go with this current VA design, other competitors will follow, given today's low rates. "I expect to see more companies go down to 4%. There is no question that the thinking of the population has changed: We're a society that's looking at some very tarnished golden years," said Joan Boros, who is of counsel at Jorden Burt LLP. "Given the market place, a 4% guarantee isn't that unappealing."

1. Getting mileage out of hybrids

One product model that will definitely gain traction this year: A combination structured product and VA. The resulting hybrid gives clients potential upside gain along with downside protection. AXA already has such a product, which offers clients a number of indexes to choose from while the insurer absorbs the first 10%, 20% or 30% of a loss within a certain period. Allianz filed for a similar concept in January, as did MetLife in December. The latter filing, however, does not have any variable subaccount options, offering guarantee options that are tied to an index, noted Tamiko Toland, managing director of retirement income consulting at Strategic Insight. "It's not just good for the insurer because it's a low capital product, but it's also a fundamentally different guarantee," she said. "If the market goes up, you get a stated percentage credited. If the market is negative, you lose nothing. This is more of a return-of-premium guarantee."