HYMANS ROBERTSON
The Spirit of Independence

Buy-outs, buy-ins and longevity hedging

Q4 2012

Managing pension scheme risk

Welcome to our quarterly update, summarising the activity in the buy-in, buy-out and longevity hedging markets during the fourth quarter of 2012, and the year to 31 December 2012 ('the last year').

Buy-outs and buy-ins - Deals during Q4 2012

The total value of buy-out and buy-in deals struck in Q4 2012 was around £2.0 billion (around £4.5 billion for the year to 31 December 2012).

Buy-out and buy-in deals Year to 31 December 2012	Number of deals completed					Value of deals completed				
	Q1	Q2	Q3	Q4	Total	Q1	Q2	Q3	Q4	Total
Aviva	5	14	8	6	33	£21m	£68m	£40m	£59m	£187m
Legal & General	9	19	27	35	90	£30m	£32m	£410m	£539m	£1,011m
Lucida	1	-	-	-	1	£40m	-	-	-	£40m
MetLife	4	4	4	6	18	£62m	£135m	£101m	£49m	£347m
Pension Insurance Corporation	4	5	5	6	20	£338m	£408m	£378m	£344m	£1,468m
Prudential	-	1	1	-	2	-	£272m	£140m	-	£412m
Rothesay Life	-	-	-	3	3	-	-	-	£1,025m	£1,025m
Total	23	43	45	56	167	£491m	£914m	£1,069m	£2,016m	£4,490m

Longevity swaps - Deals during Q4 2012

There was one longevity swap completed in Q4 covering liabilities of around £0.8 billion. Fifteen deals, covering liabilities worth around £19.6 billion, have now been completed between 30 June 2009 and the end of February 2013.

Organisation	Date	Number of pension schemes	Provider	Approximate value of deal (on a buy-in basis)
Babcock	Q3 2009	3	Credit Suisse	£1.2 bn
RSA Insurance	Q3 2009	2	Goldman Sachs/Rothesay Life	£1.9 bn
Berkshire	Q4 2009	1	Swiss Re	£1 bn
BMW	Q1 2010	1	Deutsche Bank/Abbey Life	£3 bn
Pall	Q1 2011	1	JP Morgan	£0.1 bn
ITV	Q3 2011	1	Credit Suisse	£1.7 bn
Rolls Royce	Q4 2011	1	Deutsche Bank/Abbey Life	£3 bn
British Airways	Q4 2011	1	Goldman Sachs/Rothesay Life	£1.3 bn
Pilkington	Q4 2011	1	Legal & General	£1 bn
Azko Nobel	Q2 2012	1	Swiss Re	£1.4 bn
LV=	Q4 2012	1	Swiss Re	£0.8 bn
BAE Systems	Q1 2013	1	Legal & General	£3.2 bn
Total to date		15		£19.6 bn

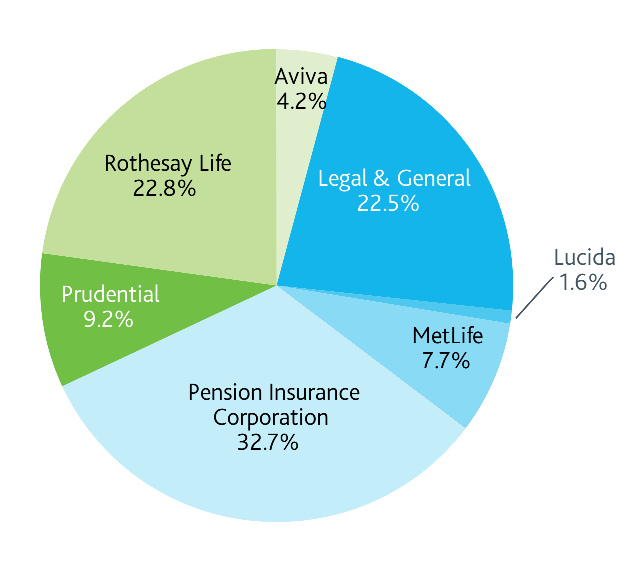
Risk transfers during the last year Facts and figures

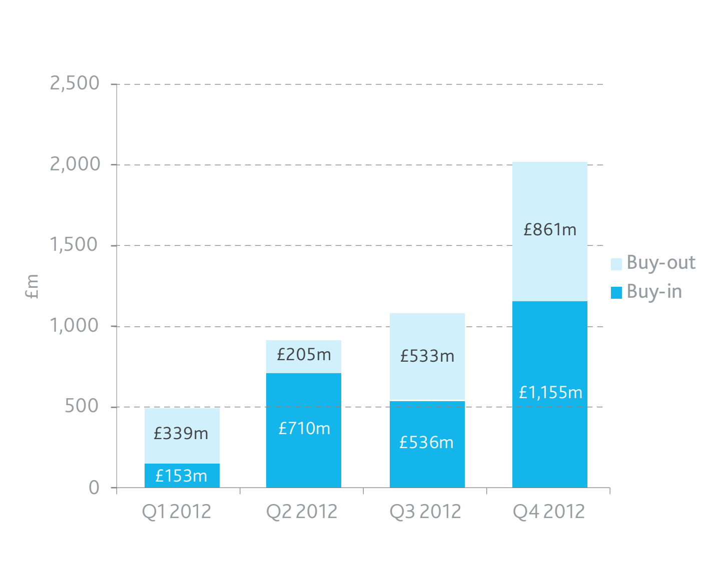
Buy-ins and buy-outs Market share (by value) during the year to 31 December 2012

The buy-in and buy-out market was dominated by Aviva, Legal & General, MetLife, Pension Insurance Corporation, Prudential and Rothesay Life during the last year and this looks set to continue throughout 2013.

Buy-ins v buy-outs

During the last year, the value of buy-ins was more than the value of buy-outs (around £2.6 billion of buy-ins versus around £1.9 billion of buy-outs).





Largest buy-ins and buy-outs

The last year saw six deals in excess of £200m.

	Pension Scheme	Provider	Value	Deal type	Date
1	West Midlands Integrated Transport Authority	Prudential	£272m	Buy-in	Q2 2012
2	The Cookson Group	PIC	£320m	Buy-in	Q3 2012
3	Undisclosed	L&G	£250m	Buy-in	Q3 2012
4	Tate & Lyle	L&G	£347m	Buy-in	Q4 2012
5	General Motors	Rothesay Life	£230m	Buy-in	Q4 2012
6	MNOPF	Rothesay Life	£680m	Buy-out	Q4 2012

Risk transfer deals (including longevity swaps)

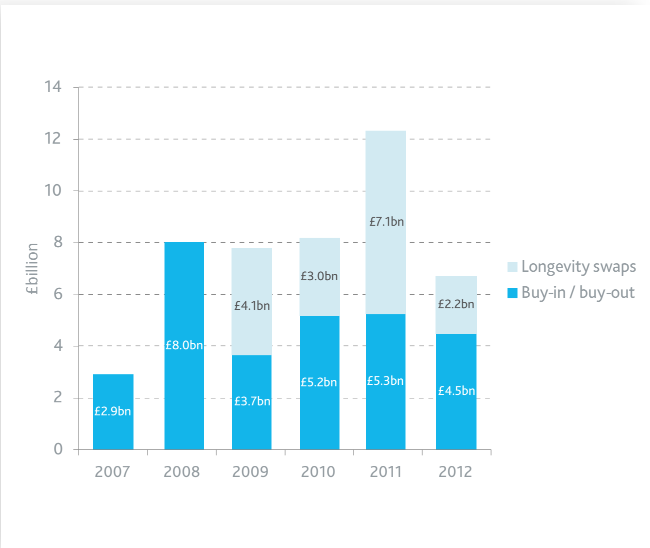
Total pension scheme risk transfer deals over the last year covered liabilities of around £6.7 billion. Since 30 June 2009 the longevity swap market has now seen deals covering £19.6 billion of liabilities.

Average buy-in and buy-out deal size

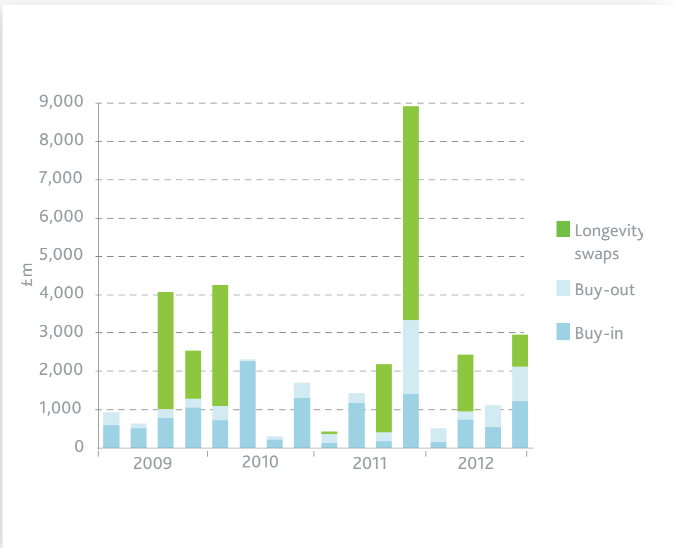
The overall average buy-in/buy-out deal size for the last year was £27m, similar to the average over the year to 31 December 2011 of around £30m. The average deal size during the last year varied significantly between the different insurers.

Insurers	Average deal value (number of deals)
Aviva	£6m (33)
Legal & General	£11m (90)
Lucida	£40m (1)
MetLife	£19m (18)
Pension Insurance Corporation	£73m (20)
Prudential	£206m (2)
Rothesay Life	£342m (3)
Totals	£27m (167)

Volume of risk transfer deals since 2007 up to the end of Q4 2012



Quarterly risk transfers since 2009



Buy-outs and buy-ins

Recent developments

Buy-ins and buy-outs have covered around £4.5 billion of pension scheme liabilities during the 12 months to 31 December 2012, with £2 billion completed in Q4 2012. PIC claimed the top spot in terms of buy-in and buy-out market share over the year, with 33% during the year to 31 December 2012. The £1.1 billion Turner & Newall buy-in with Legal & General, at the end of October 2011, was one of the largest of its kind to date. Insurance companies and banks have taken on the risks associated with over £50 billion of pension scheme liabilities since 2006/2007. With pipelines in this market looking so strong, we expect this figure to rise to £100 billion before the end of 2017.

FTSE100 companies have now transferred the risks associated with over £18 billion of pension scheme liabilities to insurance companies and banks.

See the ‘Risk transfers during the last year—Facts and Figures’ section for further details.

Pension schemes are increasingly viewing buy-in deals simply as an investment strategy decision, and one that looks particularly attractive in the current market. Many pension schemes are reviewing their Government gilt holdings, which provide quite a good match for pensioner liabilities, given the option to exchange some of their Government gilts for a buy-in policy, which provides a near perfect match for pensioner liabilities, and at a similar cost. This pricing dynamic is one of the few positives for UK pension schemes following the market turmoil since the summer of 2011.

Market outlook

We expect activity in the pension scheme de-risking market will continue to increase in the medium term, particularly because the recent volatility means that companies and trustees have an even greater appetite to reduce risks. Banks and insurers continue to offer new flexibility which means that risk transfer deals are more affordable for many UK pension schemes. For example ‘enhanced buy-ins’, which make use of impaired life annuities, are increasing in popularity given their ability to significantly reduce the buy-in cost for many UK pension schemes. It is also interesting to note that several FTSE 100 companies have completed risk transfer deals for their pension schemes in recent months.

There has been some consolidation in the buy-in / buy-out provider market over the last two years. However, given the ever increasing demand from pension schemes to transfer their risks, we would not be surprised to see further new providers enter this market over the next year.

Many trustees are now working towards a secondary ‘self-sufficiency’ funding target which they are then using as a benchmark to measure risk, against which trustees are able to take practical decisions to reduce risk over time. Putting in place a longer term strategy can also ensure that trustees are ready and able to make decisions quickly, to capture any short term opportunities to reduce investment risk when market conditions improve.

FTSE 100 pension scheme risk transfer deals:

FTSE 100 company	Provider	Value	Deal type	Date
Smiths Group	L&G Paternoster Rothesay Life	£250m £250m £150m	Buy-in Buy-in Buy-in	Mar 2008 Sep 2008 Dec 2011
Lonmin	Paternoster	Undisclosed	Buy-out	May 2008
Friends Provident	Aviva	£350m	Buy-in	May 2008
Cable & Wireless	Prudential	£1,000m	Buy-in	Sep 2008
RSA Insurance	Rothesay Life	£1,900m	Longevity swap	Jul 2009
Cadbury Schweppes	PIC	£500m	Buy-in	Dec 2009
Liberty International	PIC	£61m	Buy-out	Feb 2010
British Airways	Rothesay Life Rothesay Life	£1,300m £1,300m	Buy-in Longevity swap	Jun 2010 Dec 2011
Next	Aviva	£124m	Buy-in	Aug 2010
GlaxoSmithKline	Prudential	£892m	Buy-in	Dec 2010
ITV	Credit Suisse	£1,700m	Longevity swap	Aug 2011
Rolls-Royce	Deutsche Bank	£3,000m	Longevity swap	Nov 2011
Tate & Lyle	L&G	£347m	Buy-in	Dec 2012
BAE Systems	L&G	£3,200m	Longevity swap	Jan 2013

Longevity swaps

Recent developments

Longevity swap deals have now covered £19.6 billion of pension scheme liabilities since 30 June 2009.

In February 2013, BAE Systems became the 18th FTSE 100 company to complete a material risk transfer deal with its pension scheme, when it completed a £3.2 billion longevity swap deal with Legal & General (the largest deal to date).

In December 2012 , LV= completed a £0.8 billion longevity swap and in May 2012 Akzo Nobel completed a £1.4 billion longevity swap - both deals were with Swiss Re.

Market outlook

Our clients are finding that the competition, particularly amongst reinsurers, in this market is leading to some attractive pricing for removing longevity risk and this is a key driver for the recent level of longevity swap activity. The pace of this activity continues to accelerate and we anticipate a number of large transactions will complete this year.

We believe that longevity hedging deals will continue to be popular for large pension schemes, who may consider that the best way to de-risk is to carry out a DIY buy-in; that is to use interest, inflation and longevity swaps directly to reduce risk. However, providers are now offering longevity swaps to smaller pension schemes, down to pensioner liabilities of around £50m in size.

We believe that this is a positive development as it makes longevity hedging more accessible for many more UK pension schemes.

In order to assess the potential value of a longevity swap, companies and trustees will need to apply sophisticated modelling techniques to accurately understand their own scheme's longevity risk, based on the unique characteristics of their membership (in terms of affluence, lifestyles, location etc). This will be best achieved by pooling their mortality data with other pension schemes.

FTSE 250 pension scheme risk transfer deals:

FTSE 250 company	Provider	Value	Deal type	Date
Weir Group	L&G	£240m	Buy-in	Dec 2007
Rank	Rothesay Life	£700m	Buy-out	Feb 2008
Morgan Crucible	Lucida	£160m	Buy-out	Mar 2008
BBA	L&G	£270m	Buy-in	Apr 2008
Dairy Crest	L&G	£150m	Buy-in	Dec 2008
	L&G	£160m	Buy-in	Jun 2009
Babcock	Credit Suisse	£1,200m	Longevity swap	Jul 2010
Aggregate Industries	PIC	£305m	Buy-in & Buy-out	Mar 2010
Undisclosed	L&G	£220m	Buy-in	Jun 2010
London Stock Exchange	PIC	£203m	Buy-in	May 2011
Home Retail Group	Prudential	£280m	Buy-in	May 2011

If you would like to discuss this quarterly update in more detail please contact your usual Hymans Robertson contact or:

Richard Wellard
Buy-out specialist
T 0121 210 4355
E richard.wellard@hymans.co.uk

James Mullins
Head of Buy-out Solutions
T 0121 210 4379
E james.mullins@hymans.co.uk

Russell Chapman
Partner
T 020 7082 6134
E russell.chapman@hymans.co.uk

Andrew Gaches
Longevity consultant
T 020 7082 6128
E andrew.gaches@hymans.co.uk