Navigating you through your de-risking journey

Risk settlement market 2018

Pensions expert
PENSION AND INVESTMENT PROVIDER AWARDS 2018
Winner
DERISKING CONSULTANT
Aon

PROFESSIONAL PENSIONS
UK PENSIONS AWARDS 2018
WINNER
Risk Reduction Adviser of the Year

European Pensions
AWARDS 2018
WINNER
Risk Management Firm of the Year

Aon
Empower Results®

Longevity risk

Part of the Risk Settlement Market Review 2018

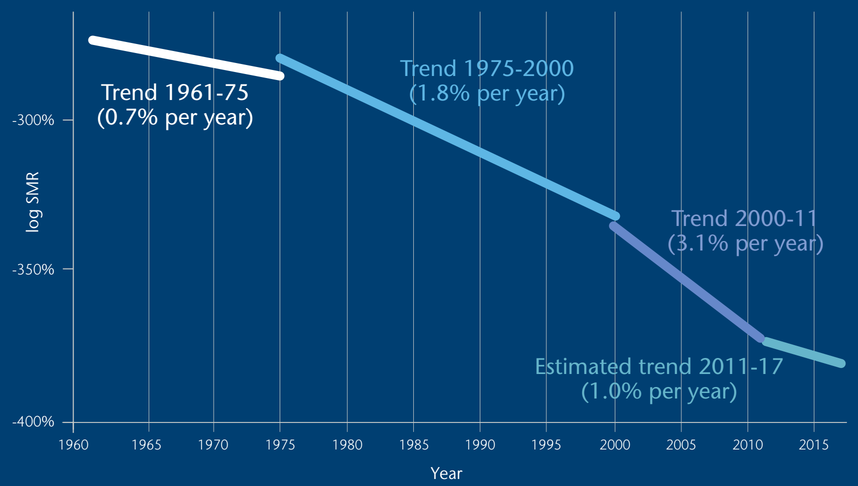
To download your copy visit
aon.com/risksettlementuk

Changing views on longevity trends

Improvement trends in male mortality rates 'dramatically lower'

It is no longer seriously disputed that we have entered a low national mortality improvement phase. In the chart below, you will see that we have plotted standardised male mortality rates by calendar year since 1961[1], together with some trend lines. The steeper the slope of the trend line, the higher the rate of longevity improvement.

Standardised England & Wales mortality rate (males aged 50 to 89 inclusive)



The chart shows:

- The relatively high longevity improvements over the final quarter of the last century (1975-2000)
- The very high longevity improvements experienced over the first decade of this century (2000-11)
- The dramatically lower improvement trend that has emerged since 2011 (2011-17)

Source: Aon calculations using data from the Office for National Statistics. Note that the value for 2017 is an estimate based on part year data. The standardised mortality rate (SMR) is based on the subset of the European Standard Population 2013 for ages 50 to 89 last birthday inclusive.

[1]The standard Office for National Statistics starts in 1961. This is also a reasonable starting point to review mortality improvement trends in the modern (ie, post Second World War) period.

Key points

- Strong evidence suggests that we have entered a phase of low improvements in mortality
- At the time of writing, it seemed likely that the number of deaths in England & Wales in 2017 would be the same as in 2015 – which was regarded as exceptional at the time
- The longevity market has taken this information on board and, following a year or more of pricing dislocation, it has relocated to pricing that is fair in historical terms

The '2015 was a blip' argument is no more

The chart on the previous page highlights the stark contrast between recent annual male mortality improvements of 1% over the seven-year period 2011-2017[2], compared with those of around 3% the previous decade.

So the debate on whether 2015 was a 'blip' or part of a change in trend is essentially over – and team blip has lost. In fact, the period of 3% improvement now looks to be the outlier when compared with historical improvements.

National improvement in male mortality continues at

1% per year

compared to over 3% per year for the previous decade

What does this mean for pension schemes?

The debate has now moved on to whether the fall in the national trend can be applied unadjusted to pension schemes. This is because the fall-off in mortality improvements may be less marked for pension schemes.

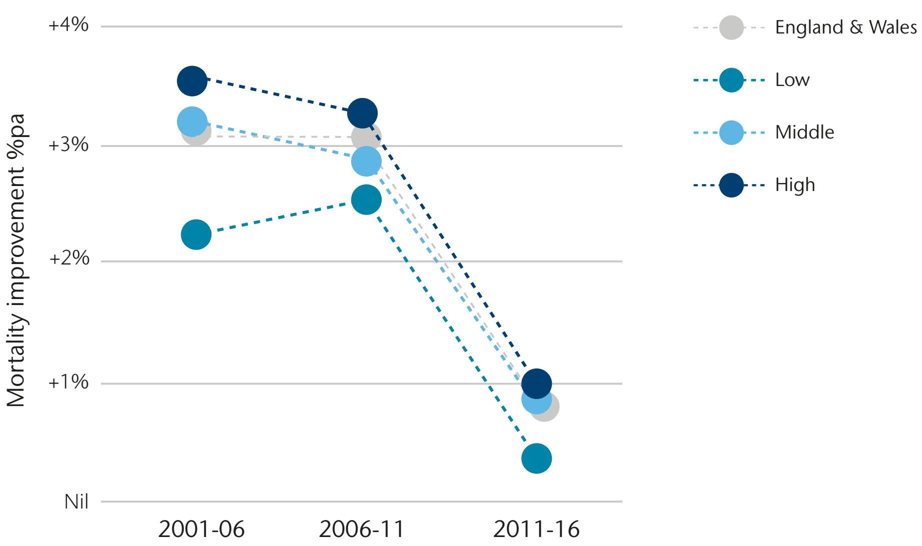
Defined benefit pension schemes are biased towards the better off because the individuals able to accrue a meaningful pension will have been in work for a long period, which implies a certain level of good health, and because pension liabilities are weighted towards individuals with larger pensions.

[2] This estimate is based on part year data for 2017 and a neutral estimate for the remainder of the year.

Male mortality improvements

We can take a closer look at this using data from the Office for National Statistics (ONS) for male mortality improvements by socio-economic group. We have used this data to estimate mortality improvements over five-year intervals from 2001 to 2016, shown in the chart below.

Male mortality improvement by socio-economic group over five-year periods



Source: Aon calculations using data from the Office for National Statistics. Improvements are for standardised mortality rates using the subset of the European Standard Population 2013 for ages 50 to 89 last birthday inclusive

The striking features of the chart are:

- Mortality improvements were higher for the better off over all of the five-year intervals
- It appears that the situation was beginning to revert, with the gap in improvements narrowing for the second period, 2006-11
- Improvements for all groups have fallen dramatically in the last five-year period.

It is important to be wary of over-interpreting the ONS data, but it seems that there is a strong case to suggest that mortality improvements have fallen for all sub-groups and this should therefore be reflected in mortality best estimates for pension schemes.

Get in touch to find out more here

Matt Fletcher
matthew.fletcher.2@aon.com

Tim Gordon
tim.gordon@aon.com

Longevity market dislocation and relocation

Longevity insurers and reinsurers were initially – and understandably – reluctant to recognise the heavier than expected mortality data, in case it turned out to be a transient effect. Trustees and scheme actuaries shared the same concern but, as the evidence continued to mount, they started to adjust their best estimates to reflect the data. However, reinsurers and insurers delayed their response. This led to a dislocation in market pricing during 2016 and early 2017, with pricing materially lagging best estimates.

Key points

- 2016 and early 2017 saw a dislocation in market pricing, with insurers and reinsurers slow to respond to changing mortality figures
- Aon's experience enabled us to spot this dislocation and advise clients not to transact if pricing was not favourable
- External pressure and ongoing low improvements have led longevity reinsurers to adjust their pricing

Our stance

Given our engagement in the market on numerous potential deals, Aon was well placed to observe this price dislocation and, as the leading adviser on longevity swaps, we led the market by calling out this issue publicly to:

- Ensure our clients did not enter unattractively priced transactions in the short term
- Accelerate the process of price relocation.

This meant that some very large Aon-advised deals did not proceed, illustrating that we are fully prepared to advise our clients not to proceed with a deal when the terms are unfavourable.

Relocation, relocation, relocation

Partly because of this pressure – and with further data reinforcing the view that low improvements are not a blip – longevity reinsurers have now incorporated lower life expectancies into their pricing. The longevity market, assessed in a competitive broking scenario, has relocated to pricing that we consider to be broadly fair in historical terms.

Get in touch to find out more here

Martin Bird
martin.bird@aon.com

About Aon

Aon plc (NYSE:AON) is a leading global professional services firm providing a broad range of risk, retirement and health solutions. Our 50,000 colleagues in 120 countries empower results for clients by using proprietary data and analytics to deliver insights that reduce volatility and improve performance.

For further information on our capabilities and to learn how we empower results for clients, please visit **aon.mediaroom.com**

Empower Results®