Unit linked business in Europe

Development of the unit linked market in Germany

Vladimir Novikov
Ulrich Wiesenewsky

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TOWERS WATSON

AGENDA

- Introduction
- Historical development of unit linked business in Germany
- Selected aspects of unit linked business in Germany

Regular Premium New Business by product (€ mn)

	2011	2010	2009	2008	2007	2006
Conv. Endowm.	666	693	717	758	855	988
UL Endowm.	273	296	317	444	481	491
UL Annuity	1,184	1,168	1,289	1,863	1,566	1,217
Term	410	415	430	408	431	433
Conv. Annuity	2,028	1,773	1,807	2,203	1,860	2,250
Disability	411	353	320	273	287	255
Long-Term Care	13	10	8	7	8	5
Other (primarily Capital Redemption)	128	151	98	100	92	101
Total Individual	**5,113**	**4,859**	**4,987**	**6,056**	**5,580**	**5,742**
Endowment	98	107	122	128	145	161
Mortgage Protection Term	22	20	54	53	57	44
Decreasing Term	8	10	11	12	14	13
Other	872	660	637	605	611	560
Total Group	**1,000**	**797**	**825**	**798**	**827**	**778**
Grand Total	**6,112**	**5,657**	**5,812**	**6,855**	**6,407**	**6,520**

Source: GDV

Single Premium New Business by product (€ mn)

	2011	2010	2009	2008	2007	2006
Conv. Endowm.	1,082	1,398	864	455	348	397
UL Endowm.	319	467	289	185	236	55
UL Annuity	1,342	1,452	1,058	1,304	1,369	853
Term	9	6	6	7	7	7
Conv. Annuity	10,631	13,011	8,438	4,587	4,629	5,222
Disability	10	0	0	0	0	0
Long-Term Care	17	13	10	8	7	5
Other (primarily Capital Redemption)	3,657	4,513	4,803	2,346	1,750	1,383
Total Individual	**17,067**	**20,859**	**15,469**	**8,892**	**8,347**	**7,923**
Endowment	345	450	349	409	349	446
Mortgage Protection Term	0	0	0	0	0	0
Decreasing Term	700	505	579	697	661	697
Other	3,456	4,603	3,339	2,307	2,559	2,497
Total Group	**4,501**	**5,558**	**4,268**	**3,413**	**3,569**	**3,641**
Grand Total	**21,568**	**26,417**	**19,736**	**12,306**	**11,916**	**11,564**

Source: GDV

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Accumulation/Decumulation products: Unit linked products – development phase 1

Phase 1 („Phase before the Telekom Stock“): From 1970 to 1994

- life companies had no appetite offering UL products
  - high profit margins for conventional products (and low margins for UL products)
  - stable capital markets with high-yield government bonds
  - guaranteed interest rate of 3.5% p.a. (plus profit participation)
  - low disclosure and transparency requirements
  - clients were risk averse
  - huge investments required for development & launch (systems, admin, marketing, distribution) of UL products
- only few companies offered UL products (13 providers up until 1994)
- UL were only sold as a add-on if client already had a conventional product
- regulated market (pre-approval of products)
- low sales via IFAs, nowadays the most relevant channel for unit linked business
- only pure UL products (i.e. client bearing the entire investment risk)

Accumulation/Decumulation products:
Unit linked products – development phase 2

Phase 2 („Phase of the Telekom Stock“): From 1994 to 2001

- market deregulation: foreign companies entered and sold via IFAs (and independent multi-tied agents) only
- appetite to offer UL products increased
  - equity and equity fund investments became more popular
  - distributors called for equity oriented life products which provide fronted commissions
  - interest rates decreased at end of century
  - conventional products lost attractiveness: guaranteed interest rate first went up to 4% p.a. in 7/1994 and then down to 3.25% p.a. in 7/2000
- increased concerns about stability of state pension system => need for more private cover
- fund management companies identified UL providers as sales channel and increased the fund offering
- enhanced admin systems due to technological progress
- product innovation: internal funds, fund-of-funds, „managed UL products“, index-linked policies, UL annuity, mixture of conventional & UL products

Accumulation/Decumulation products: Unit linked products – development phase 3

Phase 3 („After the crash“): From 2001 to 2008

- only few companies not offering UL products,
- further reductions of guaranteed interest rate (down to 2.75% in 1/2004 and to 2.25% in 1/2007)
- tax changes
  - 2001: Riester pensions and enhancements for company pensions
  - 2005: Basic pensions and end of tax-freedom for regular premium products
- innovation: UL with guarantees
  - first funds with guaranteed unit prices
  - static hybrid products
  - variable annuity VA
  - dynamic hybrid products
- increasing regulation & transparency
  - Insurance Mediation Directive
  - reform of Insurance Contract Act (disclosure, hidden reserves participation, etc.)
  - novations of Insurance Supervisory Act (e.g. minimum profit participation)

Accumulation/Decumulation products: Unit linked products – development phase 4

Phase 4 („After the financial crisis“): From 2008

- further cut in the guaranteed interest rate down to 1.75% in 1/2012
- flat tax introduction in 2009
- more requirements to qualify as tax-preferred life insurance (life cover, wrapper policies, guaranteed annuity factors)
- more focus on
  - risk management (Solvency II)
  - disclosure and transparency
- innovation
  - more VAs, more dynamic hybrid products, etc
  - ETFs in UL products
  - more emphasis on funds and portfolio management („Best-in-Class“, „UL with safety concept“, VolCap funds)
- companies review corporate, risk, product and sales strategy
  - focus on capital management (Solvency II)
  - outsourcing (admin, IT or investment management), closing to new business or sale
  - co-operation between insurance companies (e.g. sourcing products)

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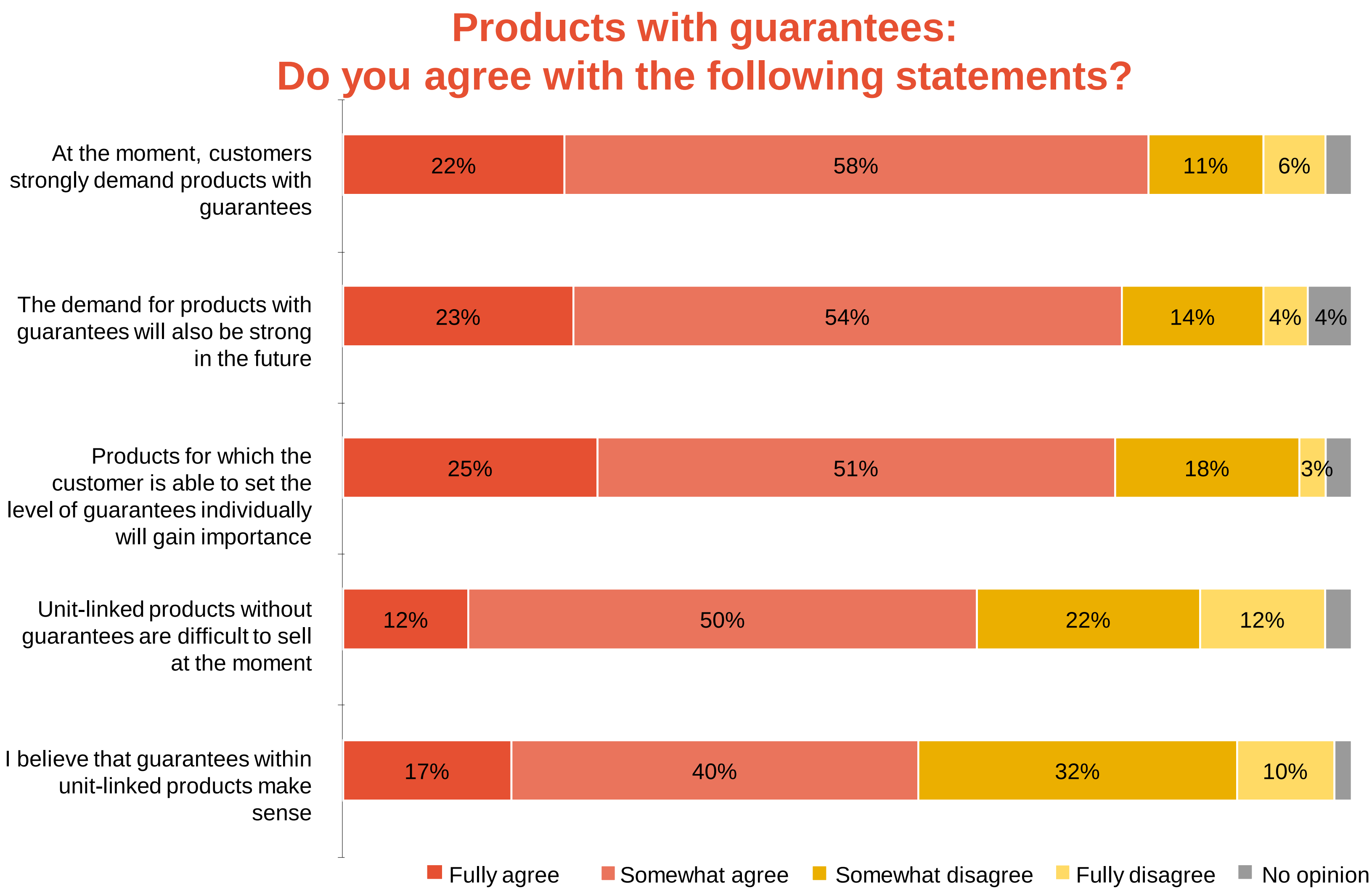
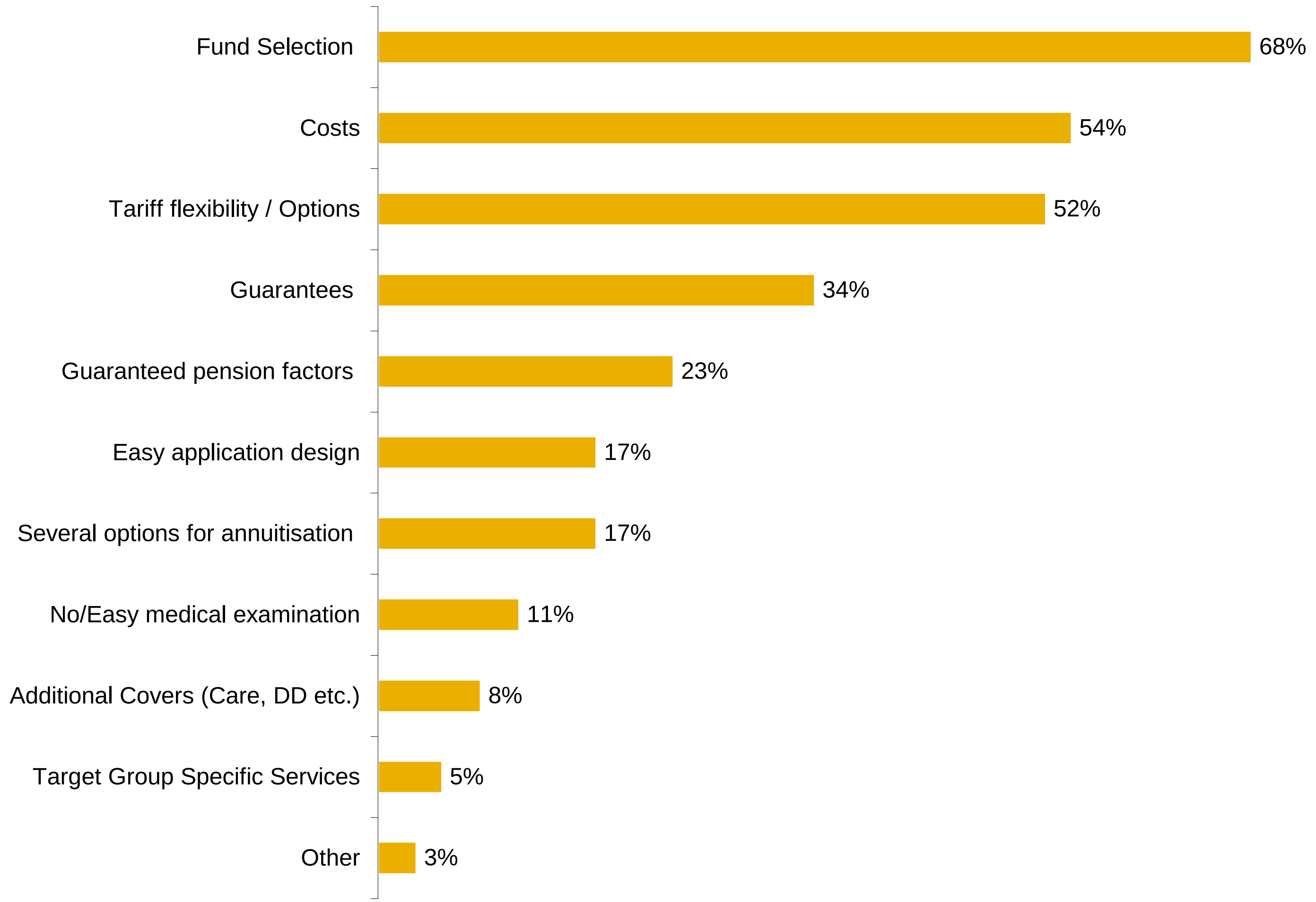
Guarantees are regarded as an indispensable element of unit-linked products by German brokers



Source: Towers Watson Broker Survey 2011

Fund selection still is an important criterion for product selection

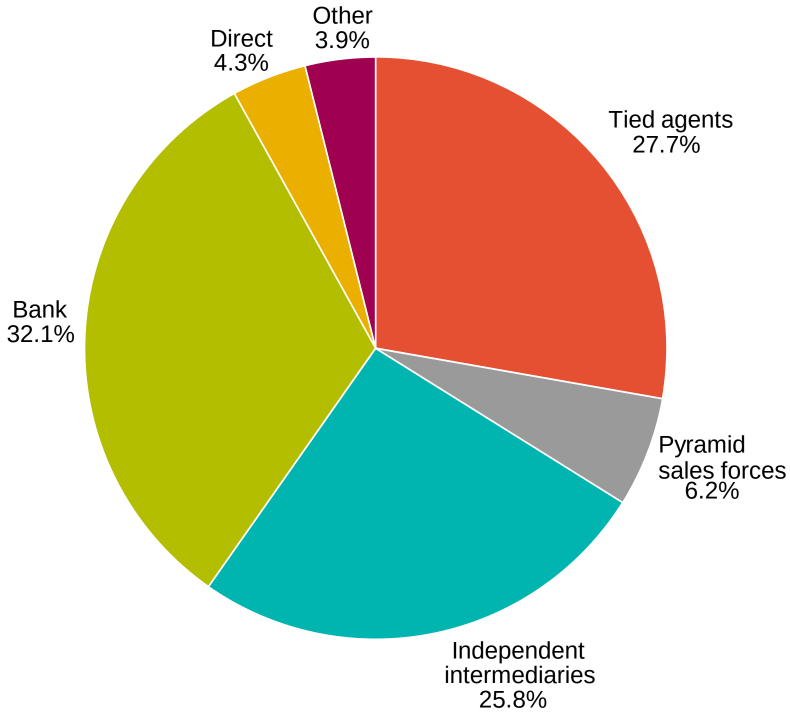
What are the 3 most important criteria regarding product selection?



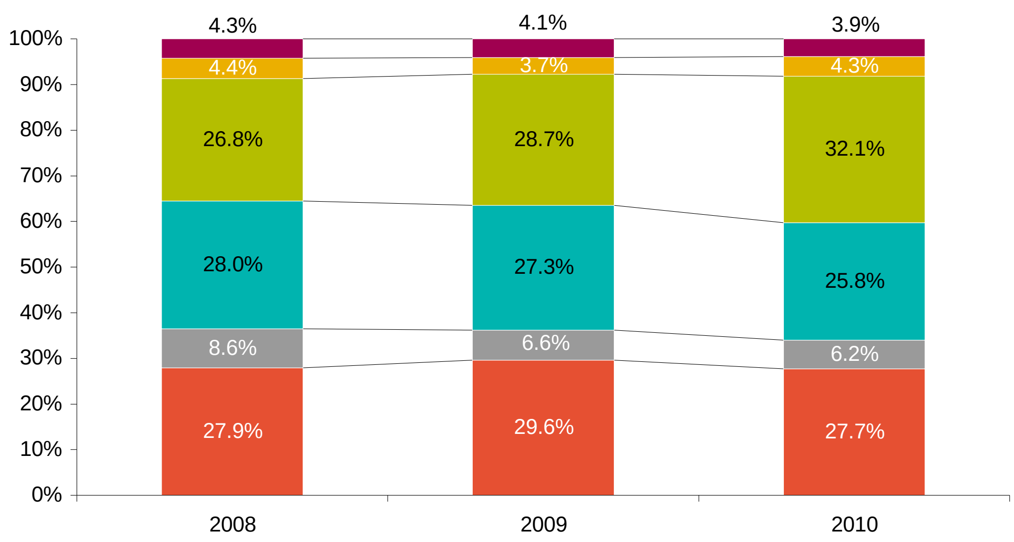
Source: Towers Watson Broker Survey 2011

Distribution channel mix (total life) – APE

APE* TOTAL LIFE 2010



APE* TOTAL LIFE PREVIOUS-YEAR COMPARISON

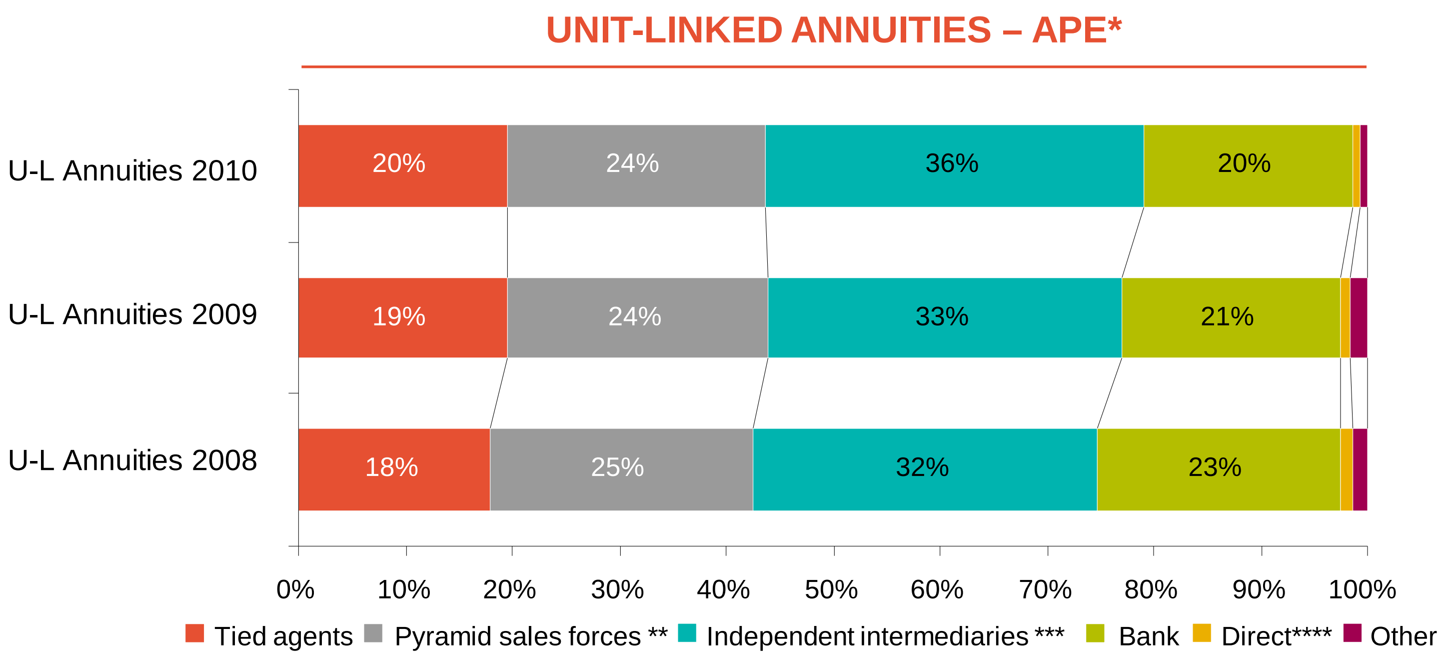


Tied agents · Pyramid sales forces ** · Independent intermediaries *** · Bank · Direct**** · Other

* Estimation
** e.g. HMI, OVB, DVAG
*** incl. brokers, multi-tied agents, advised- based distribution firms (AWD, MLP etc.)
**** Internet sales are part of Direct

* APE = Current Premiums + 10% of Single Premiums

Shares of distribution channels by product



* APE (Annual Premium Equivalent) = Regular Premiums + 10% of Single Premiums

- New business of unit-linked annuities slightly decreased in terms of APE compared to previous year. While regular premiums dropped, single premiums increased significantly. The distribution mix has only slightly been influenced.
- Independent intermediaries were able to gain market shares and fostered their leading role in this segment. The gain was achieved via growth in regular premiums.
- As in the previous years, pyramid sales forces achieved the second place in this segment. This product category accounts for over 50% of the new business in this distribution channel.

Contact

Ulrich Wiesenewsky

Habsburgerring 2
50674 Köln
Telefon: +49 175 583 77 71

E-mail:
ulrich.wiesenewsky@towerswatson.com

Internet: www.towerswatson.com