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Fixed Annuity Sales: The Money is Moving Like Water

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"We just had the biggest fixed annuity sales month we've ever had, at the lowest interest rates in our company's history. It's incredible, but true!"

I've been hearing that comment a lot over the past couple of months from an assortment of insurance company executives.

From my vantage point, there are two primary reasons for fixed annuity sales being so hot:

1) The largest increases are coming from CD type annuities, where the rate guaranteed period matches the length of the surrender penalty period.

In the past couple of years, companies that saw the future developed CD type annuities. These turned out to be the right product at the right time. They are "right," because today's clients and agents are trusting insurers less and less to pay a 'fair' floating interest rate. Through experience, they've learned that renewal rates on traditional designs don't generally float up, only down. That's why CD type annuities are pushing annuity sales up.

2) Fear is driving money to guaranteed safe investments.

A lot of people have lost all the money in the market they care to lose and are moving their money to where they can earn a guaranteed return without risk.

For example, a lady recently came to my office and said, "I invested $80,000 with my stockbroker two years ago and he made it grow all the way to $50,000. It may not be his fault, but I'm having bad dreams about him making it grow to $30,000. At my age, I can't afford to lose any more money. Can you invest my money for me and guarantee a good rate and my money be safe?"

In one form or another, I hear those comments every day.

A general consensus of opinion from financial advisors is that client portfolios are far over weighted in stocks. A lot of rebalancing is going on.

In short, investors believe the outlook for stocks in the next 5 to 10 years may be only single digit returns. "If that's true," they reason, "why subject my money to risk when I can earn a competitive return in a guaranteed safe fixed annuity?"

Money, like water, may sit still for a while, but it will eventually move.

Without any help from the financial world media, people are discovering that "boring" fixed annuities are safe and pay higher rates than CDs, Treasury Bonds, and the like.

As one of my clients told me, "You know, my annuities aren't sexy and they aren't as much fun to talk about at the country club, but every night when I go to bed, I know that my annuities are earning interest, and I will wake up richer than I was the day before. I just love 'em!"

In the past, FA sales have plummeted when rates fell below 6%. But, that hasn't happened this time. Sales have actually exploded. The big question now is what will happen to sales when rates go below 5%?

Most of the agents I talk to feel that lower rates will slow down FA sales with longer durations, just like it will with CDs. But they also feel that, if we offer our clients a rate period 'ladder' with durations of one day to five years in length, FA sales will continue to thrive – because the amount sold is directly related to the lower rates paid at the local bank.

In the past 10 years, FA rates fell below 5%, people would move their money to equities. But now that we've been through 2 1/2 years of negative equity experience, I don't think that's going to happen this time around. People will stay liquid while they shop for the best rates available.

As a result, we sell a lot of FAs paying 3% to 4% without any surrender charges. Huge sums of money are moving from money market accounts into these new "liquid flexible" annuities while they wait for rates to go up.

The public wants CD type annuities while insurers prefer floating rate annuities. That's the Catch-22.

The dilemma for insurers is that CD type annuities require higher reserving than non-guaranteed rate annuities and therefore limits the amount of premium that a company can write. Also, by guaranteeing the rate, the company cannot afford to make a mistake in setting the rate [making their spreads], nor can they afford to buy bonds that are called or downgraded.

These two investment problems have led to a ceasing of FA production at several companies and/or A. M. Best downgrades in the last two months. I don't know how some insurers have avoided these investment issues, but a handful have consistently had higher rates and commissions for CD Type annuities than most other companies.

The CD annuity is great for the buyer, but has more risk for the insurance company. With rates below 5%, most reinsurers are not willing to coinsure these FAs because the small margin between current rates and the 3% guaranteed floor is too risky. Therefore, smaller companies that have less capital are restricted in the amount of CD annuities they can write, if they want to keep their Best ratings.

Regardless of how you feel about CD type versus floating rate annuities, there is a huge opportunity for agents and companies to utilize their marketing skills to meet market demand for safe money havens.

Money, like water, may sit still for a while, but it will eventually move. Are you in the right position to catch all you can? **NU**