With-Profit Endowments
April 2018

With-Profit Endowments 2017

During the first quarter of each year, most UK Life Insurance companies publish results on the performance of their With-Profit funds during the previous calendar year. Alongside this they will also announce the changes that they are making to annual reversionary bonus rates, terminal bonus rates and ultimately the levels of payout for maturing With-Profit policies. Individual policyholder statements will be sent out detailing the annual bonus additions and updated guarantees that are to be applied to policies.

SL Investment Management Limited (SL) has been a major participant in the traded endowment market for over 27 years and is constantly monitoring the performance of the larger UK Life Insurance companies; comparing the relative performance of With-Profit funds and changes in bonus rates from year to year to understand how traded endowment policies may perform in the future.

Financial Markets and With-Profit Fund Performance

The major UK equity indices (FTSE 100, 250 and All-Share) all achieved solid gains over the 2017 calendar year with each hitting a record high during the year; this despite the markets wavering during the summer months following the snap general election in June. High dividend payments and ongoing loose monetary policy from the Bank of England are believed to be the major domestic factors contributing to the gains with global factors such as China's pro-business, pro-growth policies as well as tax cuts and infrastructure projects in the US also helping to boost the UK equity indices.

Property indices recovered from the low single digit figures of 2016 to post double digit returns; however, the main UK gilt indices showed a significant drop over the same period. Nevertheless, the assets and investments of the With-Profit funds are in many instances actively managed and the published 2017 annual returns for all of the analysed With-Profit funds were positive, although all except Scottish Widows showed a lower return compared to the returns achieved during 2016.

Table A: Return on With-Profits funds over the calendar years 2016 & 2017

Life Company	2016 Annual Return	2017 Annual Return
Clerical Medical	8.5%	7.8%
Commercial Union	12.1%	8.9%
Friends Provident	11.9%	6.6%
General Accident	12.1%	8.9%
Legal & General	15.3%	8.1%
Norwich Union	11.4%	8.1%
Prudential	14.5%	10.3%
Royal Life	11.3%	8.3%
Scottish Amicable	14.9%	10.3%
Standard Life	8.2%	6.1%
Scottish Widows	9.0%	9.0%
Average	**11.7%**	**8.4%**
FTSE All Share Index (total return)	16.8%	13.1%
FTSE 100 index (total return)	19.1%	11.9%
ABI UK - mixed 20%-60% Shares - Life	10.4%	6.2%
IPD UK All Property Monthly (total return)	2.8%	11.0%

Table source: Life Company data, reports and press releases.

FTSE Actuaries UK Conventional Gilts Over 5 yrs	13.7%	2.8%
Morningstar 90 days notice	0.5%	0.4%

Table A (above) shows the reported gross annual returns achieved in the With-Profit funds of some of the more established Life Companies. The figures for the previous two complete calendar years are shown together with comparable performance figures for other investments and indices. The figures in the table represent gross annual return figures, i.e. before the deduction of tax and expenses. The With-Profit funds of Prudential and Scottish Amicable top the 2017 calendar year returns both having achieved 10.3%, with no other fund breaking into double digits. SL's analysis shows that for these funds the investment managers have consistently maintained higher than average allocations in property and equities than competitors in recent years. The weakest performer was Standard Life with posted returns of 6.1%, whose asset allocation and investment strategies have obviously performed comparatively poorer.

Asset Allocation

The asset mix of a With-Profit fund can be a key driver to the overall performance achieved. As With-Profit funds mature they will tend to adopt a strategy of holding a greater proportion of fixed interest assets (i.e. government and corporate bonds) which are considered more secure. This will be to both support capital preservation and to ensure that the funds comply sufficiently with stringent solvency regulation. The liability profile of the funds and the requirements to comply with such stringent regulation can restrict investment freedom and limit the investment strategies that can be adopted going forward.

The equity backing ratio (EBR) is typically defined as the ratio of the equity and property assets to the total assets in the fund. Table B below shows the breakdown of the reported Equity, Property and Fixed Interest assets for each of the funds. The levels of reported EBR at the end of 2017 are, on average, slightly higher compared to end 2016 levels although there are noticeable differences in the EBR for some With-Profit funds compared to previously reported figures, ranging from a 31% decrease (Royal Life) to a 14% increase (General Accident/Commercial Union). Commercial Union and General Accident have the highest reported holding of Equities and Property assets at 78% while Royal Life has the lowest reported holding at the end 2017 with just 37%.

Table B: Asset Mix as at end of 2017

Life Company	Equities	Property	Fixed Interest / Cash/ Other
Clerical Medical	43.8%	16.0%	40.2%
Commercial Union	63.2%	15.0%	21.8%
Friends Provident	34.6%	8.0%	57.4%
General Accident	63.2%	15.0%	21.8%
Legal & General	40.0%	11.0%	49.0%
Norwich Union	62.5%	12.8%	24.7%
Prudential	52.0%	14.1%	33.9%
Royal Life	31.0%	6.0%	63.0%
Scottish Amicable	49.9%	11.5%	38.6%
Standard Life	43.1%	11.5%	45.4%
Scottish Widows	15.0%	51.0%	34.0%
Average	**45.3%**	**15.6%**	**39.1%**

Table source:
Life Company data, reports and press releases.

Maturity Payouts

The payout amounts for maturing endowment policies are significantly higher than that of a conservative investment into a bank savings account over an equivalent term. Table C below shows the actual maturity payouts for 25 year term policies maturing at 1st March 2018, for a male aged 30 (next birthday) at issue and a monthly premium of £50. The largest payout is from Scottish Amicable – £30,365, yielding an annualised return of approximately 5.2% per annum; however, this is the computed payout amount for a Unitised With-Profit policy. The largest payout for conventional policies is from Royal Life – £29,559; equivalent to an annualised yield of 5.0% p.a. over the 25 year term. Standard Life, as in 2017, produces the lowest return over the 25 year term of £24,485 with an annualised yield of 3.7% per annum.

Table C: Maturity Payouts

Average Saving Account
Payout = 16,605
Return = 0.8%

* The Clerical Medical figures were not available at the time of compilation of this report.

** Scottish Amicable released figure is for a Unitised With-Profit policy.

Table source:
Life Company data, reports and press releases.

Life Company	March-18 (£)	Return
Clerical Medical*	-	-
Commercial Union	27,027	4.4%
Friends Provident	29,270	5.0%
General Accident	27,027	4.4%
Legal & General	25,515	4.0%
Norwich Union	26,368	4.2%
Prudential	29,407	5.0%
Royal Life	29,559	5.0%
Scottish Amicable**	30,365	5.2%
Standard Life	24,485	3.7%
Scottish Widows	26,640	4.3%
Average	**27,566**	**4.5%**

The average payout on maturing endowment policies has remained relatively consistent over the last couple of years, albeit that payout levels are now at a substantially lower level than the peaks achieved in the early 2000s. This is in part a result of the low interest rate / low inflation economic environment that has been in place in the UK for the past 10 years. Despite positive returns being achieved by all reported With-Profit funds in 2017 changes to payouts have been both positive and negative for 25 year term policies when compared to the equivalent period last year. Table D shows the maturity payout for a policy maturity this year and the comparable figure from 12 months ago.

Table D: Maturity Payouts Calendar Year-on-Year Change

* The 2018 Clerical Medical payout figure was not available at the time of compilation of this report.

Table source:
Life Company data, reports and press releases.

Life Company	March-17 (£)	March-18 (£)	Change (£)	Change
Clerical Medical	25,004	-	n/a	n/a
Commercial Union	27,046	27,027	(19)	(0.1%)
Friends Provident	29,235	29,270	35	0.1%
General Accident	27,670	27,027	(643)	(2.3%)
Legal & General	26,408	25,515	(893)	(3.4%)
Norwich Union	27,450	26,368	(1,082)	(3.9%)
Prudential	29,268	29,407	139	0.5%
Royal Life	30,612	29,559	(1,053)	(3.4%)
Scottish Amicable	29,865	30,365	500	1.7%

Standard Life	24,929	24,485	(444)	(1.8%)
Scottish Widows	25,071	26,640	1,569	6.3%
Average	**27,505**	**27,566**	**61**	**0.2%**

For the ten Life Companies analysed in this report that have made data available, four have increased payouts while six have reduced payouts. The most significant increase in maturity payout is by Scottish Widows with an increase from £25,071 to £26,640, 6.3% up on 2017, while Norwich Union policies are showing the largest decrease in maturity payout of £1,082 (3.9% down on 2017).

The fact that the maturity payouts on average have remained unchanged will be a combined result of the asset returns achieved during 2017, the smoothing processes employed by the respective Life Companies and the returns achieved over the lifetime of the policies. A further contributory factor to the levels of payout for this year and in future will be the potential of a distribution from the 'inherited estate'. Most With-Profit funds are now closed to new business and in a period of run-off and regulatory requirements dictate that the Life Companies responsible for these funds must put in place plans to distribute surplus funds to policyholders. As such we have seen a number of Life Companies make statements about their intentions to enhance the levels of payout to policyholders on surrender or at maturity to reflect distributions from the 'inherited estate'.