Insured Retirement Institute

STATE OF THE INSURED RETIREMENT INDUSTRY

2016 Review & 2017 Outlook

December 2016

ABOUT THE INSURED RETIREMENT INSTITUTE

The Insured Retirement Institute (IRI) is the leading association for the retirement income industry. IRI proudly leads a national consumer coalition of more than 40 organizations, and is the only association that represents the entire supply chain of insured retirement strategies. IRI members are the major insurers, asset managers, broker-dealers/distributors, and 150,000 financial professionals. As a not-for-profit organization, IRI provides an objective forum for communication and education, and advocates for the sustainable retirement solutions Americans need to help achieve a secure and dignified retirement. Learn more at **www.irionline.org**.

©2016 IRI

All rights reserved. No part of this report may be reprinted or reproduced in any form or used for any purpose other than educational without the express written consent of IRI.

STATE OF THE INSURED RETIREMENT INDUSTRY

2016 Review and 2017 Outlook

OVERVIEW

The *State of the Insured Retirement Industry* is the fifth in an annual series of reports covering significant trends and developments in the retirement industry. This year has been marked by significant shifts in product sales, ongoing low interest rates putting continued stress on the industry, and historic expansion of regulation via the Department of Labor (DOL) fiduciary rule. And as of this writing, a largely unexpected presidential election victory by Donald Trump has created a great deal of uncertainty regarding public policy affecting the industry in 2017 and beyond.

In 2016 the DOL fiduciary rule was finalized. The second half of 2016 was marked by unprecedented changes in compensation structures and business practices, as well as product development as both distributors and manufacturers worked to create conditions and products designed to work for both financial advisors and consumers under the new regime.

This report will take an in-depth look at the macro and micro factors that impacted the retirement industry in 2016, with a particular focus on the impact of the DOL fiduciary rule and expectations for the future of the rule in the wake of Election Day results. Additionally, this report will provide context for possible market developments in 2017.

Market Environment and Demand Drivers

- Kathleen Casey-Kirschling turned 70 in 2016. Born a few seconds past midnight on January 1, 1946, Casey-Kirschling was one of 3.4 million babies born that year and the first of the Baby Boomer generation.
- By the end of 2016, approximately 24 million Boomers will be age 65 or older.
- The largest wave of Baby Boomers, those born between 1952 and 1959, will begin to retire in 2017. There are roughly 33 million Baby Boomers in this group.
- The average pre-retirement Baby Boomer (those aged 55-65) has $136,200 saved for retirement.[1]
- Baby Boomers have an aggregate net worth of approximately $7 trillion.[2]
- Only one in four Boomers expects to receive a pension in retirement, leaving 57 million who may need to use their retirement savings to produce steady, predictable retirement income.[3]
- Despite low interest rates and an uncertain regulatory environment, insurers continue to offer a diverse suite of annuities and lifetime income strategies, affording individuals the opportunity to match multiple lifetime income solutions to their unique needs, goals, and risk tolerances.
- As financial professionals seek to provide added value to cost-conscious consumers, more advisors are likely to employ a holistic retirement planning framework, leading to more focus on retirement income planning.

Headwinds

- Low interest rates persisted in 2016, constraining the ability of insurers to offer higher payouts on immediate annuities, and higher withdrawal rates on lifetime income benefits.

- Tremendous resources were allocated to preparing for the DOL fiduciary rule. This limited innovation and progress in other areas, for example straight-through processing (STP) improvements to streamline transaction processing.

Key Observations

As noted above, many demographic trends favor increased adoption of annuities in retirement planning, but market environment (interest rates) and regulatory (the DOL fiduciary rule) challenges continue to producing headwinds in product development, expanded use of annuities by financial professionals, and growth of the market for annuity products. A main focus of the industry in 2016 was the effort to adapt to the DOL fiduciary rule. Other observed trends in 2016 are continuations of market trends that have been evolving for several years.

- **Significant Trends in 2016:**
  - **Fixed Indexed Annuities (FIA) and Investment-Oriented Variable Annuities (IOVA) are growing rapidly.** FIAs are posting strong sales as both a fixed income substitute — meaning a bond-like return without interest rate risk — and on the attractiveness of optional guaranteed lifetime income benefits.
  - **Industry Evaluation:** Companies are reevaluating their product offerings and distribution strategies as they digest the potential impact of the DOL fiduciary rule.
  - **Self-Reliance in Retirement:** 42 percent of retirees receive at least half their income from a pension, compared to only 24 percent of current workers being covered by a defined benefit plan.[4]
- **Expected Trends in 2017:**
  - **Retirement Entering Millennials' Radar Screens:** Heretofore a blip, as the oldest Millennials turn 35, retirement becomes more real. IRI research shows that 68 percent of Millennials are saving for retirement, 65 percent believe Social Security will not provide meaningful income in retirement, and only 29 percent say they are actively preparing for retirement. It is a generation thirsty for guidance, as they rapidly move into their peak earnings years.
  - **Interest Rates Rise?** Pundits have declared higher interest rates "right around the corner" for several years, but 2017 may prove to be the year rates finally see a meaningful increase. Bond yields spiked after Donald Trump won the presidential election, as markets generally believe rates will be higher under a Trump Administration than they would have been under Hillary Clinton. Policy observers agree that there are increased chances of tax cuts and deficit spending under President Trump. These actions could fuel inflation and prompt swift action by a hawkish Federal Reserve.
  - **DOL Fiduciary Rule Scheduled to Take Effect:** The DOL fiduciary rule's initial compliance deadline is scheduled for April 10, 2017. Financial professionals will embrace a more holistic retirement planning framework as a result.
  - **Risk-Driven Product Development:** Retirees face many risks in addition to longevity, notable among them the need for health care and long-term care. Long-term care risk and costs, in particular, may increase as medical advances extend lives and increase the population subject to the diseases of advanced age, such as dementia. Expect continued development of hybrid solutions, such as long-term care riders on life and annuity products, designed to provide affordable solutions to those who cannot afford the increasing cost of pure long-term care insurance.

» **Hybrid Annuities:** Global volatility in both equities and fixed income may increase in 2017 as markets react to potential changes in public policy — fueling development and innovation in options-based products such as FIAs and structured annuities.

» **Traditional Pension Risk Transference:** Several large companies have moved from defined benefit to defined contribution plans in recent years, and at the same time have moved pension obligations off their books by transferring the plans to insurance companies. General Motors, Verizon, and WestRock (a large paper and packaging company) are a few recent examples of multi-billion dollar plans that have purchase group annuities to manage retiree benefits. Expect this trend to gain momentum in 2017 and beyond, as these transfers can improve balance sheets and relieve companies from PBGC premiums.

» **Demand for Lifetime Income:** Demographics, increasing longevity, decline of traditional pensions, and consumer appreciation for products providing guaranteed retirement income each month will support demand for lifetime income strategies. We anticipate that more advisors will embrace a holistic retirement planning approach, allowing them to tailor retirement plans — that include income-generating strategies — to meet clients' unique goals and needs.

2016: A YEAR IN REVIEW

	Q2 2012 YTD		Q2 2013 YTD		Q2 2014 YTD		Q2 2015 YTD		Q2 2016 YTD		% Change from 2012
	$Bln	%	$Bln	% Δ	$Bln	% Δ	$Bln	% Δ	$Bln	% Δ	
Variable											
All VA	**74.4**		**71.9**	**-3.4**	**69.1**	**-3.9**	**67.0**	**-3.0**	**52.4**	**-21.8**	**-29.6**
GLI	65.1		63.6	-2.3	60.8	-4.4	58.8	-3.3	44.4	-24.5	-31.8
IOVA	0.30		0.50	66.7	0.60	20.0	0.70	16.7	0.50	-28.6	66.7
Group	8.9		7.6	-14.6	7.5	-1.3	7.3	-2.7	7.5	2.7	-15.7
Immediate	0.1		0.2	100.0	0.2	0.0	0.2	0.0	0.0	-100.0	-100.0
Fixed											
All Fixed	**34.0**		**32.1**	**-5.6**	**46.7**	**45.5**	**43.7**	**-6.4**	**59.4**	**35.9**	**74.7**
Book Value	10.0		8.2	-18.0	11.1	35.4	9.4	-15.3	11.9	26.6	19.0
MVA	2.6		2.3	-11.5	4.8	108.7	4.5	-6.3	9.2	104.4	253.8
FIA – GLI	1.6		2.1	31.3	5.5	161.9	4.3	-21.8	5.1	18.6	218.8
FIA – No GLI	15.4		14.8	-3.9	18.6	25.7	19.8	6.5	26.1	31.8	69.5
Income (SPIA/DIA)	4.4		4.7	6.8	6.7	42.6	5.7	-14.9	7.1	24.6	61.4
All Annuities	108.4		104.0	-4.1	115.8	11.3	110.7	-4.4	111.8	1.0	3.1

Flat Sales, Shifting Product Landscape

Through the midway point of 2016, year-to-date sales of fixed annuities exceeded sales of variable annuities for the first time, and despite significant headwinds total annuity sales are up 1 percent compared to 2015 and up over 3 percent versus 2012. Variable annuity sales were down more than 20 percent as compared to same period in 2015. Meanwhile fixed annuity sales rose 36 percent compared to the same period in 2015, and are up 75 percent versus the same period in 2012. When sales are broken down by specific product type, variable annuities with guaranteed lifetime income (GLI) benefits are the largest single category. Sales of VA products with GLI still dwarf sales of fixed indexed annuities (FIA) with similar benefits, though the latter has grown rapidly. Among all fixed annuity types, FIA products, collectively, have posted the highest sales and growth, and account for more than half of total fixed annuity sales. However, traditional fixed annuities with market value adjustment (MVA) features have seen explosive growth recently, likely due to sidelined cash held by retirees and near-retirees seeking competitive yield and comparative safety.

In summary, based on year-to-date sales trend analysis from 2012 to 2016:

- Total annuity sales, while below their high-water mark in 2014, are trending upward.
- FIAs continue to gain market share. VAs with GLI still represents the largest category of products designed to offer lifetime income.
- Sales of fixed annuities with MVA features have grown tremendously. MVA features carry risk in that surrender values can be negatively impacted in a rising interest rate environment, but years of near zero interest rates in cash and cash equivalents have moved money from the sidelines into these higher yielding products.
- Investment-oriented variable annuity (IOVA) sales have leveled, though are still significantly higher than in 2012. IOVAs are primarily geared toward the higher net worth non-qualified market and generally do not offer lifetime income or death benefits or principal guarantees, so they serve a smaller market.
- Income annuities, rather remarkably in a persistent low interest rate environment, continue to grow in sales, rising more than 60 percent in the past five years. Immediate Variable Annuities, a very small segment with only a couple of products available in the market, round to zero, but single premium immediate annuities (SPIA) and deferred income annuities (DIA) continue to grow as demographics drive demand.
- Group variable annuity sales are contracting. Group VAs refer to registered variable annuities sold into a group setting, for example a 403(b) plan administered by a university for the benefit of its teaching staff and other employees. An aging, shrinking employee population are slowly eroding sales, and net flow is increasingly negative as retiring employees draw down assets.

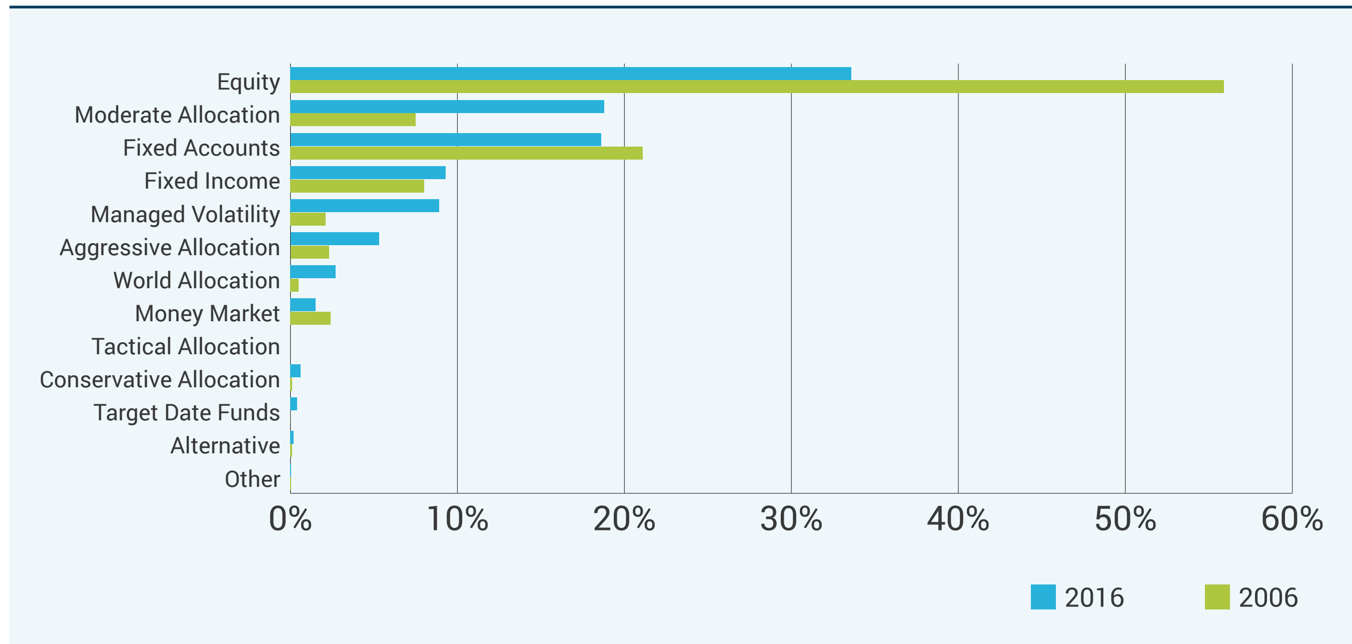
Assets under management (AUM) in variable annuities were $1.88 trillion as of the end of the second quarter of 2016, down from recent historic highs as market volatility has increased. With the S&P 500 rising 3.3 percent in the third quarter, AUM as of September 30, 2016, is expected to be somewhat higher.

Variable annuity AUM has historically tracked fairly closely with the change in the S&P 500 Index, but this relationship is beginning to break down due to increasing outflows and the continued shift in assets toward moderately allocated balanced funds and managed volatility funds. A negative change in AUM during the same period as a positive change in the S&P is indicative of de-risking and negative net flow, neither of which is likely to abate in the short term (see chart).

Growth in VA Assets Versus Change in S&P 500

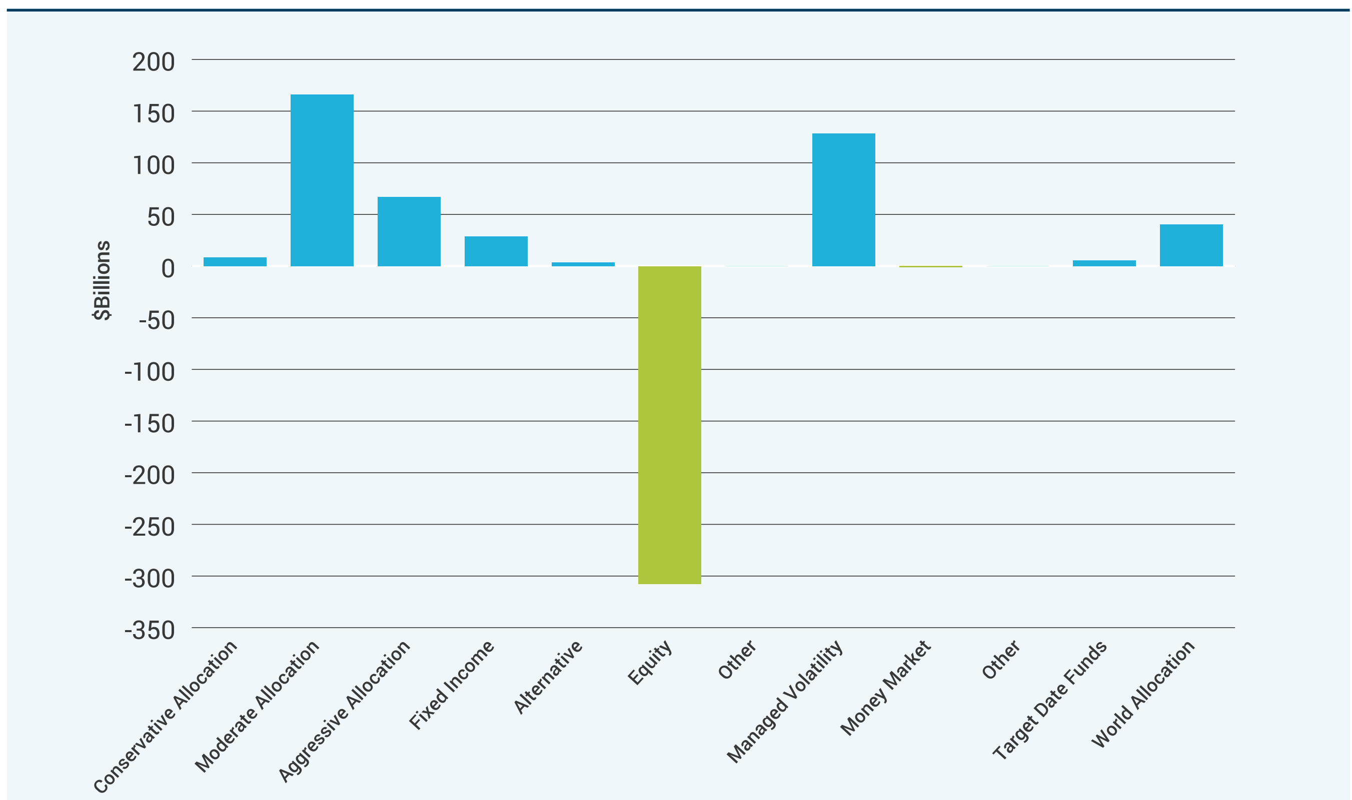
Since 2006, the aggregate asset allocation in variable annuities has changed slowly but dramatically. In 2006, equity funds held more than half the assets in VA products, but that has dropped to about a third. Driven primarily by the asset allocation mandates of many variable annuities with guaranteed lifetime income benefits, today the bulk of assets reside primarily in moderate asset allocation funds, which hold more than 20 percent of assets as compared to less than 8 percent a decade ago. Theoretically such funds provide enough equity exposure for account values to keep pace with lifetime withdrawals, and enough allocation to bonds and other lower-risk asset classes to enable insurers to avoid excessive risk. As a result of the shift to allocation funds, all else equal, expect to see less growth when equity returns are robust, but dampened losses during major corrections. Additionally, there is a growing trend in the use of managed volatility funds, particularly those which seek to manage tail risk by employing specific options strategies designed to cushion the portfolio from the effects of market downturns. Roughly 6 percent of assets currently reside in funds employing such strategies, triple the share such funds claimed in 2006.

Percentage of AUM by Investment Category: June 30, 2016, Versus June 30, 2006



These asset changes also are evident when examining aggregate net asset flow, or net cash activity, over the same period. The flows clearly show the shift of assets from equity funds into allocation and managed volatility funds, with moderate allocation and managed volatility seeing the largest inflows due to the frequent requirement to select such funds when lifetime income benefits are added to VA contracts.

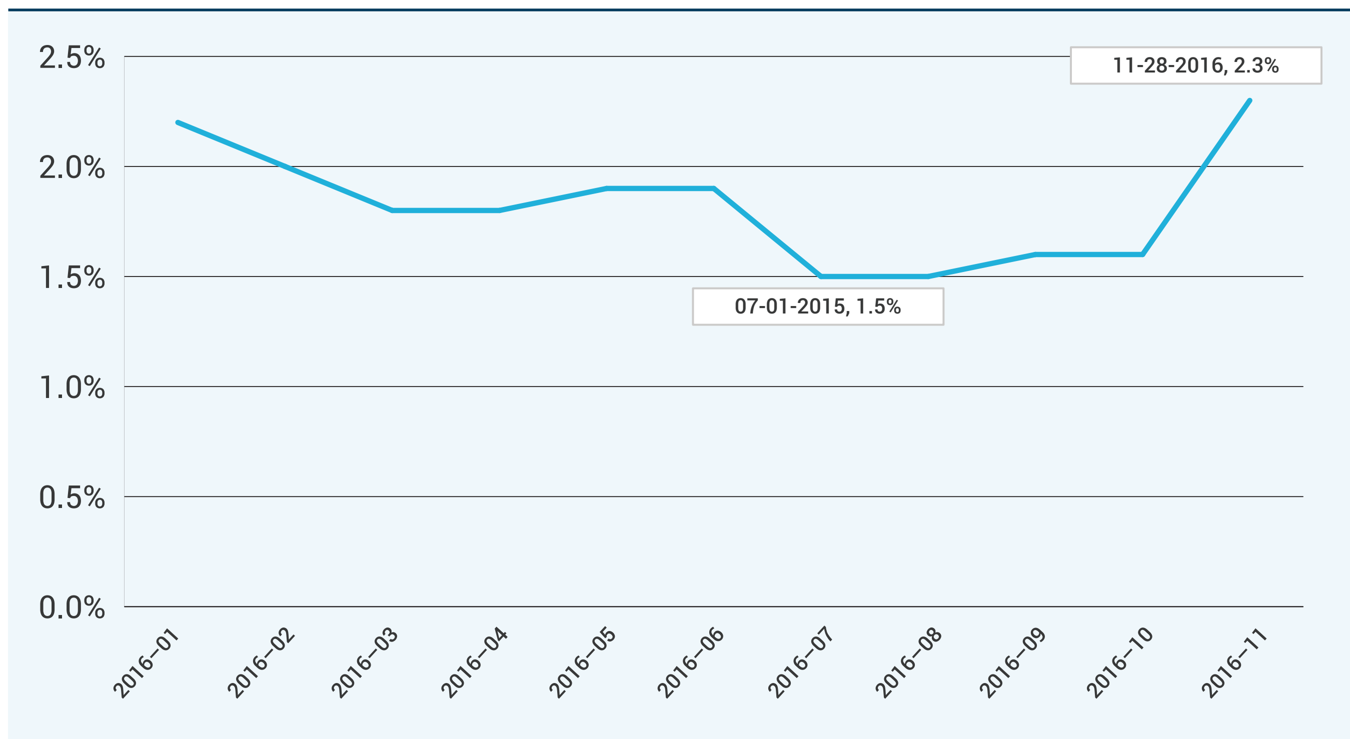
Aggregate Net VA Asset Flow by Investment Category: June 30, 2006, to June 30, 2016



Interest Rates

Interest rates dropped almost continuously throughout 2016, only to return to almost exactly the point at which they began the year after the presidential elections. Market anticipation of deficit spending to repair and improve U.S. infrastructure, combined with an expectation of tax cuts, could fuel inflation and lead to rate tightening. This resulted in a spike in interest rates. Moving off an intra-year low of 1.37 percent on July 5 to 2.34 percent as of November 28, 2016, bodes well for the retirement income industry. If rates remain on a trajectory to return to a more historically normal level, at or above three percent, more attractive income payments from SPIAs and lifetime income benefits should result.[3]

10-Year Treasury Constant Maturity Rate in 2016



Increasing interest rates will benefit the retirement income industry in several ways, including:

- Payout amounts will increase in immediate and deferred income annuities, making them more attractive to retirees and near-retirees weighing options for securing income in retirement.
- Crediting rates on fixed deferred annuities will increase, including the declared rates on the non-indexed “bucket” in fixed indexed annuities. Rates on Certificates of Deposit (CDs) will rise as well, but fixed annuities should remain quite competitive, and more products will likely offer lifetime income features.
- Fixed indexed annuity caps and participation rates may rise, as higher rates will permit more of each premium dollar to be put toward the “budget” for purchasing index options. However, higher interest rates also increase options costs, as does higher market volatility, so there is not necessarily a direct relationship between higher rates and greater participation in index returns.

10-Year Treasury Constant Maturity Rate: 2006 - 2016

Source: Federal Reserve Bank of St. Louis

- Higher rates should lower hedging costs for variable annuity lifetime income benefits, allowing insurers to offer more generous terms, such as higher withdrawal and roll-up rates.

While there are certainly broader economic implications for rising interest rates, not all of them positive, the direction the next administration seems to be headed certainly sets the stage for rates to continue their uptick in 2017.

Continued Financial Strength

As a whole, annuity issuers continue to project financial strength and will enter 2017 on an even stronger footing than in 2016. Healthy asset levels should continue to prop up the performance of legacy variable annuity blocks and drive profits through AUM-driven fee businesses such as pensions, mutual funds, and institutional asset management. Most insurers have focused on diversifying their product offerings to avoid over concentration in any one strategy and the risks inherited through those offerings. Many providers have also implemented mandates to use managed volatility funds with guaranteed income benefits. This helps from a hedging and risk standpoint, as it reduces volatility and/or the likelihood of cash values being reduced to zero. Recent rising interest rates will slowly release pressure on interest rate sensitive businesses, so though stable and well-positioned for 2017, insurers may still have exposure to volatility in equity markets as well as the potential continuation of low interest rates. Insurers will need to maintain risk mitigation efforts to offset these forces.

Observations on the life and annuity industry's financial trends and dynamics:

- Rising equity markets should continue to support legacy variable annuity blocks by holding account values close to liabilities, reducing reserve requirements otherwise forced upward by low interest rates. AUM-driven fee business should also continue to improve due to higher account values in fee-based and investment-oriented variable annuity products.
- Continued innovation in variable annuity product designs will further reduce risk exposure to insurers. This includes requiring investments in managed volatility funds when lifetime income benefits are elected to manage excessive market exposure during downturns.
- As noted, interest rates are rising and will likely continue to rise in 2017. Should interest rates trend toward historic norms, the increases will take time to have an effect on the industry given the longer durations of insurance company assets. Therefore rising rates should be viewed as having a late-2017 impact on product design and/or sales.
- Improvements in the unemployment rate and incremental wealth gains should improve the overall sales picture for the insurance industry.
- Credit positive merger and acquisition activity should continue, as companies continue to move sub-scale and under-performing or non-core businesses to acquirers with the capacity to make them perform better, or to acquirers with different return objectives.
- A stable credit rating outlook, according to Fitch Ratings, "reflecting strong balance sheet fundamentals, very strong liquidity, disciplined asset-liability matching, and operating performance."[5]

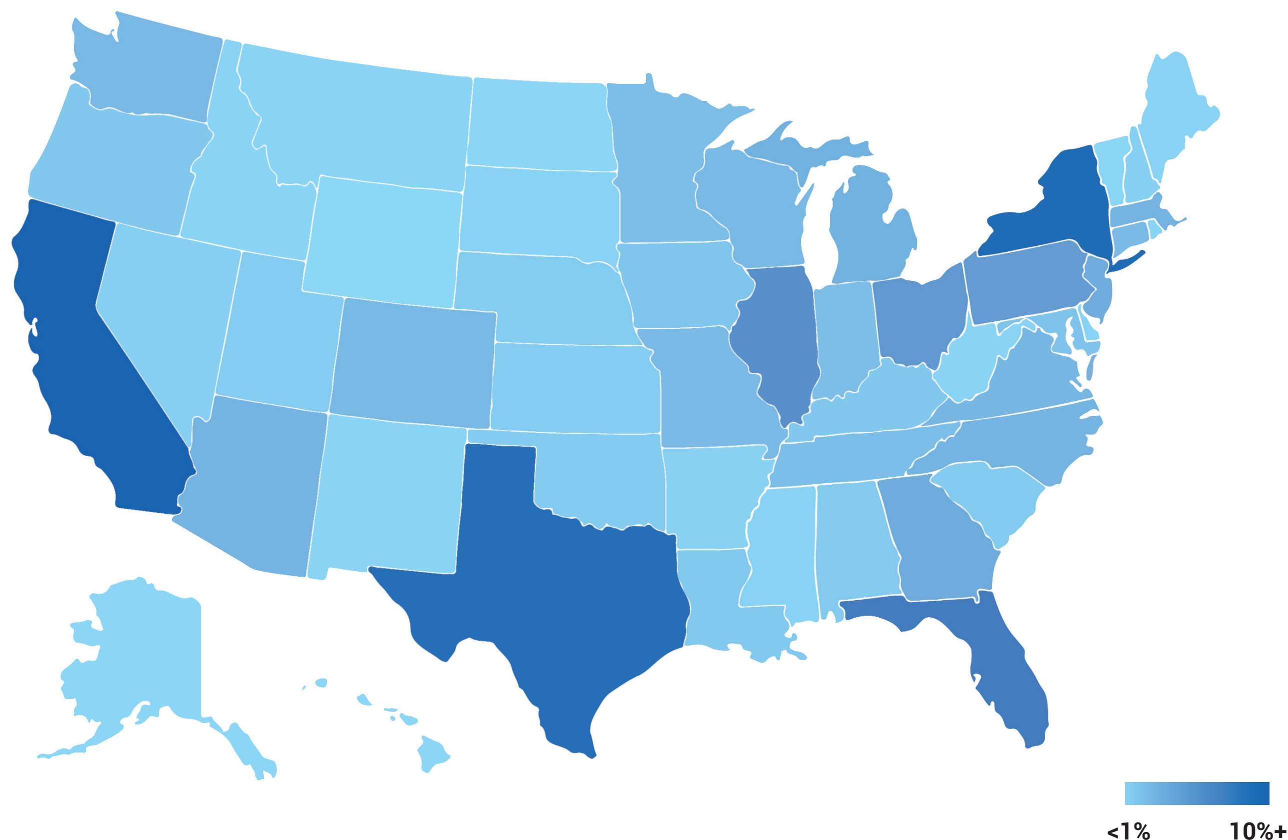
Gains in equities markets since the election and increasing bond yields have eased pressure on insurance company balance sheets, and the stock prices of several major insurers have seen double digit percentage gains. Proposed stimulus plans should continue these trends, providing more appealing reinvestment opportunities for insurers and further strengthening their financial positions.

The Retirement Industry as Economic Engine

The retirement income industry has deep, historic roots in the annuity products and investment solutions offered by insurance companies and asset managers, and provided by the financial professionals who help millions of consumers realize successful and financially secure retirements. The providers of retirement products and services employ tens of thousands of professionals across the United States, contributing to economic growth as they work diligently to help Americans secure their futures.

More than one million Americans are employed in the insurance, asset management, and financial services industries. These insurance agents, financial advisors, actuaries, underwriters, fund managers, and other professionals are located throughout the United States, working for companies with headquarters or major operations in Alabama, California, Colorado, Connecticut, Florida, Georgia, Illinois, Kansas, Massachusetts, Minnesota, New Jersey, New York, North Carolina, Ohio, Pennsylvania, Texas, and Wisconsin.

Distribution of Insurance and Securities Industry Employees as of May 2015



In addition to those working directly with retirement products and the consumers who benefit from them, thousands of other professionals such as computer programmers, web designers, database administrators, and office managers support, and are supported by, the insurance and securities industries.

Product Development

Broadly speaking, there were two overarching backdrops to product development in 2016: persistent low interest rates, and the Department of Labor (DOL) fiduciary rule. The former continued to influence product features, fueling benefit designs such as expanding the use of managed volatility funds as required investments in variable annuity products with lifetime income benefits, and the use of custom indexes with volatility overlays in fixed indexed annuities. The latter drove many companies to begin designing, or expanding, their lineup of fee-based products. Dubbed “pivot products,” the thinking is to have products ready to go that can fit into the product offerings of distributors that decide to eliminate commissionable business and move to a fee-based compensation structure. It is too early for meaningful sales data to emerge on such products, as companies that have made this move are in the early stages of converting their platforms.

Specific observations on product development:

- **Fixed Indexed Annuities (FIAs)**
  - » There are still relatively few FIA products offering optional guaranteed lifetime income benefits, but the product suite and sales are growing.
  - » The persistent low interest rate environment has helped fuel the development of custom indexes with volatility overlays, which enable companies to offer more generous declared rates.
- **"Uncapped" Fixed Indexed Annuities**
  - » Same basic structure as other FIA products — a portion of the premium is invested in the general account at a fixed rate of return, the remainder is used to purchase options on one or more market indexes.
  - » Rather than using a declared participation rate on the full premium or spread to manage risk, either a "bucket" approach or a volatility managed index is used.
    - Bucket approach: Only a portion of the premium, for example 60 percent, is credited with interest based on the change in the index value; the remainder is allocated to a fixed, interest bearing account. The portion that receives the index-based credit receives 100 percent of the increase in the index.
    - Volatility managed index: The interest credited is 100 percent of the increase in the index, but the index itself is risk managed through a volatility overlay.
  - » Anecdotally uncapped sales continue to grow, with several new product announcements in 2016 indicating widespread interest.
- **Deferred Income Annuities (DIAs)**
  - » DIAs provide guaranteed annual income payments two to 40 years in the future, though most provide income between five to 15 years from issue.
  - » While guaranteed payout amounts are higher than living benefits offered on variable and fixed indexed annuities, there is no account value for the client to access.
  - » DIA sales totaled $1.55 billion in the year-to-date period ending June 30, 2016, 34 percent higher than the $1.15 billion in sales of DIAs at the midpoint of 2015. This puts DIA sales on track to exceed three billion in sales in 2016, a solid increase from 2015 total DIA sales of $2.62 billion.
  - » At least 14 companies are now offering QLAC products.
- **Investment-Oriented Variable Annuities (IOVAs)**
  - » Compared to traditional variable annuities, IOVAs differ in three significant ways:
    - No living benefits are offered.
    - Generally lower costs.
    - Many and varied investment options offered, including alternative asset classes and outcome-oriented strategies such as rising rate defense and inflation defense.
  - » Sales of IOVA products fell off in concert with a general drop in VA sales in 2016, but remain well-above 2012 levels. In total, 38 companies currently offer 174 versions of IOVA products.
  - » No significant innovations in IOVA took place in 2016, with efforts focused more in the mechanics of illustrating the tax deferral and investment strategy aspects of the product.

- **Structured Variable Annuities**
  - Sometimes referred to as collared VAs or indexed-linked VAs.
  - Structured variable annuities provide limited upside growth potential with limited downside protection.
  - The account value growth is linked to various equity-based indexes.
  - There are now five companies offering this product type, which first appeared in 2010.
  - Sales were roughly flat from 2015 at approximately $1.2 billion (sales are not broken out in the table on page five, as some are registered as variable annuities and some are non-registered and sold as fixed products).

Managed Volatility Funds

Though versions of them have existed for many years, the annuity industry began using managed volatility funds, or "vol funds," extensively in 2011 as a means to manage risk in VA products offering guaranteed lifetime income benefits. Vol funds typically allocate a percentage of the portfolio to the purchase of options, with the percentage at any given time varying based on market volatility, the goal being to mute the effect of significant movements in equities markets and maintain a more stable account value.

Vol funds were initially used by variable annuity providers to help mitigate the risk of offering living benefits, as stable account values lower the risk of offering such benefits. Nearly all of the top variable annuity living benefit writers require vol funds, or other market risk mitigation strategies, to be selected as investment options when guaranteed lifetime income benefits are included on variable annuity contracts, and maintained per the terms of the contract as long as the benefits are in force.

Some companies are offering vol funds for use outside their living benefits to offer some potential downside account-value protection to clients. It is expected that additional companies will add vol funds to their fund lineup as a way to offer clients more diverse options.

Tracking assets under management in vol funds can be a bit challenging, as they don't carry a standard definition and are not considered an investment category like "large cap blend" or "moderate allocation." Generally, vol funds include funds that actively manage tail risk when the market moves into a downturn that is outside of normal expectations, funds that are continuously managed for low volatility, and some even include "smart beta" funds that include volatility as a weighting metric. This report focuses on the tail risk strategies, as these are the type primarily used to hedge market risk in VA products with lifetime income guarantees.

As 2016 draws to a close, vol funds account for approximately $142.7 billion of variable product net assets, up 4.7 percent from $136.3 billion at the mid-point of 2015, according to data from Morningstar, Inc. (The 2015 version of this report cited lower AUM for vol funds. Refinements in identification and tracking provided a more complete picture of these funds for this year's report).

Outcome-Oriented Portfolios

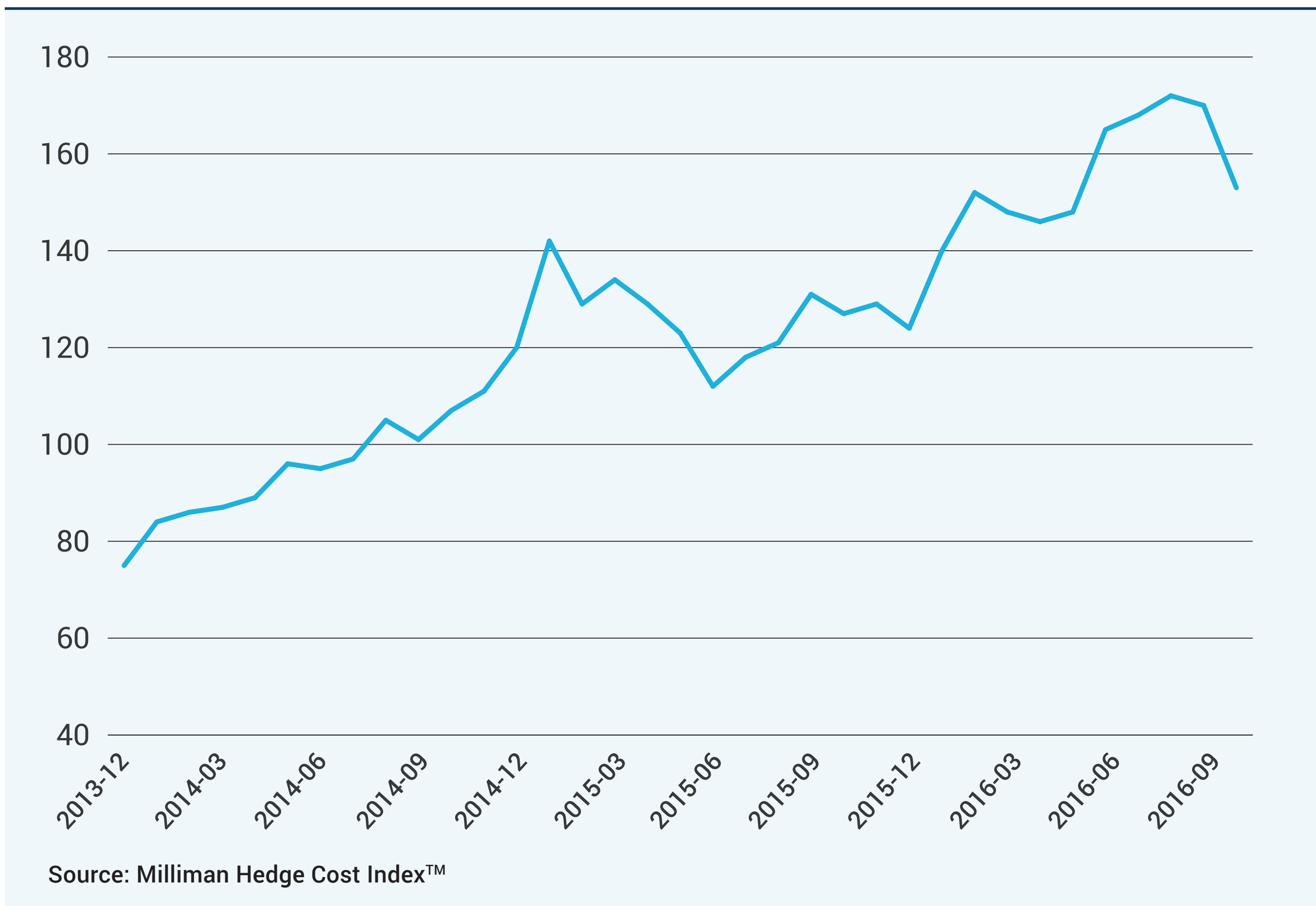
Increasingly variable annuity issuers position portfolio strategies within VAs that are designed to address specific risks. This is especially prevalent with IOVA products, as tax efficiency is a secondary consideration in such strategies. For example, a portfolio with a significant allocation to alternative investments, such as commodities, is designed to address diversification risk. Other strategies may include portfolios designed to deliver positive real returns in an inflationary environment, or hedge

against rising interest rates. Such strategies may consist of a passive core combined with a tactical overlay. That is, the bulk of the strategy's assets passively track one or more broad market indexes, while a smaller percentage is actively managed based on the manager's identification of investment opportunities that complement the investment thesis of the strategy. Tax efficiency when managing such strategies is a secondary consideration, if it is a consideration at all, so it can be advantageous to leverage the tax efficiency of the IOVA.

Managing In-Force Business

Total net assets in variable annuities dropped in 2015, but have been on the rise in 2016, totaling nearly $2 trillion. While a precise estimate of the amount covered by lifetime income guarantees is not available, an estimate of $800 billion to $1 trillion or more is not unreasonable given the high percentage of overall sales accounted for by VA products offering guaranteed lifetime income benefits. When it comes to managing this in-force business, low interest rates have increased hedging costs, with the cost increasing somewhat in 2016 as rates moved downward throughout the year. The Milliman Hedge Cost IndexTM (MHCI) provides the estimated hedging cost for a hypothetical Lifetime Guaranteed Withdrawal Benefit block of business. As of October 31, 2016, the expected hedge cost was 153 basis points, up from 124 basis points at the end of 2015, but down from a 2016 peak of 172 basis points in August. The recent spike in interest rates will likely drive the cost back down to that range as the end of 2016 approaches. A complete description of the Milliman methodology can be found at http://www.milliman.com/mhci-methodology/.

Expected Hedge Cost for Hypothetical GLWB



Source: Milliman Hedge Cost Index™

The Rise of Robo-Advice

A robo-advisor is considered to be an online wealth management service that provides automated, portfolio management advice, without the client interacting with a financial professional. Some regard robo-advice as a self-service asset allocation tool, but not "advice" in the sense that it does not provide an in-depth evaluation of an individual's goals, risk tolerance, investment time horizon, general comfort level with investing, and the application of sophisticated retirement income strategies. One study found that assets under management in robo-solutions grew from $11.5 billion in April 2014 to an estimated $61 billion as of June 2016.[6] While impressive in terms of growth, this represents only about 0.14 percent of the estimated $42.4 trillion U.S. savings market.[7] Growth in the robo space, however, has begun to flatten, and many start-ups are finding it difficult to scale client acquisition. In 2015 Morningstar, Inc., estimated that robo-advisors need $16 to $40 billion in AUM just to cover core operating and advertising costs, and $50 to $80 billion to justify current valuations — more than the current total managed by all robos collectively. However, robo-advice still has the potential to grow, and financial advisors will continue to need to find ways to differentiate the services they provide from these automated services. And as robo-advice continues to develop, other issues will need to be addressed, such as if and how robo-advice is regulated.

Public Policy

Department of Labor Fiduciary Rule

Nearly five years after withdrawing its original proposal and a year after issuing a revised proposal, the Department of Labor (DOL) released its final fiduciary rule in April 2016. The new fiduciary rule replaces a rule that had been on the books since 1975 to determine whether someone is a fiduciary under the Employee Retirement Income Security Act of 1974 (ERISA). The new rule significantly expands the universe of activities that would make someone a fiduciary under ERISA by treating almost any suggestion about investments as fiduciary advice.

Many common activities that have not traditionally been considered fiduciary in nature, would be under the new rule, including, for example, recommending or suggesting that a client:

- Rollover all or part of their retirement savings from a 401(k) plan to an IRA account, or transfer all or part of their savings from one IRA to another.
- Hire another person to provide investment advice or investment management services.
- Transition from a commission-based brokerage account to a fee-based advisory account.

While the rule broadly treats almost all interactions between advisors and clients as fiduciary advice, it does make clear that certain types of activities would not make someone a fiduciary under ERISA:

- General communications such as newsletters, research reports, general marketing materials, and speeches and presentations at conferences and widely attended events.
- Educational information about financial, investment, and retirement matters.
- Communications with a sophisticated independent fiduciary (which can be a bank, an insurance company, a broker-dealer, a registered investment adviser, or a fiduciary with at least $50 million in assets under management).

As part of the rulemaking, the DOL issued the Best Interest Contract (BIC) Exemption to enable firms

and advisers to continue to receive commissions and other types of compensation tied to specific products. The BIC Exemption requires firms to meet the following requirements:

- Firms and financial advisors must act in the client's best interest, receive only "reasonable compensation" for their services, and make no misleading statements.
- Firms must establish policies and procedures to prevent material conflicts of interest from causing violations of these promises.
- For IRA clients, firms must enter into a "best interest contract" with clients.
- Firms and financial advisors must provide clients with general information about the best interest standard and material conflicts of interest, with more detailed information available upon request.
- Firms must maintain a free website that is updated at least quarterly and provides information about arrangements with product manufacturers and other parties for third-party payments, and information about the firm's business model and advisor compensation arrangements.

The rulemaking also included adoption of a revised version of PTE 84-24, an exemption from the prohibited transaction rules that allows fiduciaries to receive "insurance commissions" for recommendations to purchase "fixed-rate annuity contracts." This exemption only covers the receipt of sales commissions by advisors from the insurance company. Revenue sharing payments, administrative fees, marketing payments and other similar types of compensation are not covered by PTE 84-24.

Historically, all types of annuities could be sold under this exemption, but the DOL significantly narrowed the scope of PTE 84-24 when it adopted the fiduciary rule. After April 10, 2017, PTE 84-24 will only be available for recommendations of "Fixed-Rate Annuity Contracts," which are fixed annuities such as single premium immediate annuities and deferred income annuities. Variable annuities, fixed indexed annuities, and other similar products will not be covered.

To rely on PTE 84-24 for sales of "Fixed-Rate Annuity Contracts," advisors will have to satisfy the following requirements:

- Act in their client's best interest;
- Receive only "reasonable compensation" for their services; and
- Provide their clients with information about the sales commission they will receive from the insurance company for the recommended transaction, as well as any charges or fees that may be imposed under the recommended annuity contract.

Most parts of the final rule will be applicable as of April 10, 2017, though certain elements of the BIC Exemption have a delayed applicability date of January 1, 2018.

Implementation Efforts

To help member companies prepare for implementation of the rule, IRI formed 17 subgroups to address common concerns, questions, and tools. These subgroups met on a weekly or bi-weekly basis and cover topics highlighted by members, from best practices and common interpretive issues to specific language of the rule and its effects on various aspects of the industry. The subgroups have more than 900 individual participants from across the industry, representing more than 120 organizations, including more than 50 insurers and nearly 40 broker-dealer firms.

Congressional Activity

The Republican controlled House and Senate pursued several possible options to block the rule from taking effect. The House and Senate passed a Congressional Review Act resolution to disapprove the rule that would have barred the DOL from implementing it. The resolution was vetoed by President Barack Obama, and an override vote on the President's veto failed in the House. In addition, the Fiscal Year 2017 Labor, Health and Human Services and Education spending bill approved by the House Appropriations Committee contained a policy rider to block the Labor Department from implementing the fiduciary rule, but the Senate Appropriations Committee bill did not.

Legal Challenge

In June 2016, IRI and several co-plaintiffs filed a legal challenge to the fiduciary rule and related prohibited transaction exemptions (PTEs) in the U.S. District Court for the Northern District of Texas. Legal challenges were also filed by other industry groups in the District of Columbia, Kansas, and Minnesota. IRI's lawsuit emphasizes that the plaintiffs and their members are dedicated to serving the best interests of retirement savers, and that they support the establishment of an appropriate rule by SEC that applies a "best interest" standard to their services. The lawsuit explains, however, that the rule and the PTEs amount to regulatory overreach that is flawed and will harm the very consumers that DOL purports to help, and seeks vacatur of the rule and its associated PTEs under the Administrative Procedure Act and the First Amendment of the U.S. Constitution.

2017 Outlook

The results of the presidential election in November have led to much speculation about the outlook for the fiduciary rule. At this time, it is not yet clear whether the incoming Trump Administration or the new Congress will take action to delay, modify or repeal the rule. IRI will be working with its members and coalition partners to engage with the administration on this issue.

Tax Reform

On June 24, 2016, the House Republican Tax Reform Task Force, led by House Ways and Means Committee Chairman Kevin Brady (R-Texas) and Speaker of the House Paul Ryan (R-Wisconsin), released a blueprint detailing recommendations for major tax code changes for Congressional consideration in advance of the next session of Congress commencing in January 2017. The blueprint included recommendations to:

- Continue current tax incentives for retirement savings, but "consolidate and reform the multiple different retirement savings provisions in the current tax code to provide effective and efficient incentives for savings and investment";
- Disallow a current deduction for net interest expenses — recognizing the need for special rules for financial services companies such as banks and insurance companies;
- Reduce tax rates to 20 percent for C corporations and 25 percent for sole proprietorships and pass-through entities;
- Simplify and lower individual tax rates on capital gains, dividends, and interest income;

- Reduce "tax preferences" and consider possible benefits of some movement toward consumption-based taxes; and
- Repeal the estate tax (unclear whether it would be replaced by carryover basis/capital gains tax).

IRI and coalition partners met with House Ways and Means member offices over the summer and fall to emphasize the importance of doing no harm to the current tax provisions related to retirement savings. During those meetings, IRI and its coalition partners stressed the following key considerations:

- With more than 10,000 Americans retiring every day, the need for tax incentives to encourage and protect retirement savings has never been greater.
- The current tax treatment for annuities and incentives for retirement savings are critically important as an impetus for individuals to save and for employers to offer retirement plans.
- Retirement savings represent a tax-deferral, not a tax exclusion, and annuities are a particularly vital source of retirement security for middle-income earners.
- Consolidating retirement plan options would risk disrupting retirement savings.

2017 Outlook

The November election results likely will ensure that tax reform will be at the top of the agenda for President-elect Trump and the Republican-controlled Congress in 2017. Proposals by Trump, Ryan, Brady and other Congressional leaders could be unveiled early in the next session of Congress. Budget reconciliation could serve as a vehicle through which a tax reform bill — possibly along with other high priority initiatives from the new administration, such as repeal or reform of the Affordable Care Act and a trillion-dollar infrastructure investment program — could be considered in the U.S. Senate without the need for the 60-vote majority that would otherwise be needed to call a vote on the measure. Whenever Congress does take up tax reform, it could have significant direct and indirect consequences for IRI member companies and the retirement and financial security of the vast majority of Americans they collectively serve.

Promoting Retirement Security and Increasing Access to Lifetime Income

Recognizing that lifetime income is an important part of a financially secure retirement, the Department of Labor (DOL) and the Treasury Department are working to reduce barriers that prevent Americans from accessing lifetime income within their retirement plans and to create incentives for plan sponsors to offer these products. The Treasury finalized its partial annuitization proposal in September and is continuing to explore options to address portability limitations. Meanwhile, the DOL's lifetime income illustrations proposal and its efforts to revise the annuity selection safe harbor are still pending,

Congress remained focused on legislation and policy proposals to increase retirement security and expand access to lifetime income in 2016. Legislation to promote access to and use of lifetime income also continued to gain traction in Congress. A number of bills were introduced, including the Lifetime Income Disclosure Act (S. 1317/H.R. 2317) co-sponsored by Sens. Johnny Isakson (R-Georgia) and Chris Murphy (D-Connecticut) and Reps. Luke Messer (R-Indiana) and Mark Pocan (D-Wisconsin). In

September 2016, the Senate Finance Committee unanimously approved the Retirement Enhancement and Savings Act of 2016, a bipartisan retirement bill sponsored by Committee Chairman Orrin Hatch (R-Utah). The bill includes IRI-supported provisions that would provide clear rules to plan sponsors for including lifetime income products in workplace plans, require lifetime income estimates on retirement plan statements, reduce the barriers to portability of investment options that provide guaranteed lifetime income, expand access to multiple employer plans (MEPs), and offer startup and automatic-enrollment tax credits for small businesses. The bill (S. 3471) was introduced in November.

Retirement security and lifetime income also gained significant attention at the state level. Under the leadership of Missouri Insurance Director John Huff, the National Association of Insurance Commissioners (NAIC) announced a new "Retirement Security Initiative" focused on education, consumer protection and product innovation. Among other things, the NAIC launched a retirement security resource center on the NAIC website, and produced a series of public service announcements promoting smart retirement planning.

2017 Outlook

It is unclear if any of the currently pending legislative proposals will pass in the lame-duck session before the new session of Congress commences in January 2017. Though the Senate Finance Committee bill was unanimously supported, the Republican-controlled Congress may prioritize other measures. In the House, Rep. Phil Roe (R-Tennessee) already announced his intention to propose a bill in 2017 that would begin retirement savings for all Americans at birth.

On the regulatory front, the incoming Trump Administration has not yet articulated its priorities for the departments of Labor and Treasury. As such, the prospects for pending DOL and Treasury initiatives on lifetime income, such as changes to the annuity selection safe harbor and the lifetime income illustrations proposal, are unclear.

Variable Annuity Summary Prospectus

Since late 2008, IRI has been advocating for the SEC to adopt a rule allowing for the use of a simplified summary prospectus for variable annuities to improve consumers' understanding of their investment choices through more streamlined disclosures. In support of this effort, IRI developed and provided the SEC with a proof-of-concept sample variable annuity summary prospectus. Consistent with the views expressed by all five SEC commissioners in a series of meetings held in late 2014, the SEC staff continues to strongly support IRI's proposal. This effort also had the support of former SEC Chair Mary Schapiro, as well as Director David Grim of the Division of Investment Management and all of his predecessors.

2017 Outlook

The SEC's regulatory agenda published in the fall of 2016 indicated that a proposal to create a summary prospectus for variable annuities is scheduled to be released in October 2017. This is not binding, however, and is subject to change. The impending departure of Chair Mary Jo White in January 2017 will leave the SEC with three open seats. Until those seats are filled, the agency's direction for 2017 and beyond will remain unclear. IRI maintains that all the work necessary to proceed with the variable annuity summary prospectus rule proposal has been completed, and will engage with the incoming Chair and the rest of the Commissioners to encourage prompt consideration of this proposal in 2017.

Senior Financial Protection Proposals

Measures to enhance senior financial protection were the focus of increased legislative and regulatory activity at both the federal and state level in 2016. Congress is considering legislation, the Senior$afe Act, which was co-sponsored by Reps. Bruce Poliquin (R-Maine), Mick Mulvaney (R-South Carolina), Patrick Murphy (D-Florida) and Kyrsten Sinema (D-Arizona) in the House, and by Sens. Susan Collins (R-Maine) and Claire McCaskill (D-Missouri) in the Senate. The bill would provide immunity from any administrative or civil liability for financial advisors, insurance companies and other financial institutions that report suspected financial abuse or exploitation of seniors. The legislation passed the House in July 2016 and was sent to the Senate, which is considering a number of possible amendments to the House bill. IRI publicly endorsed the Senior$afe Act during an event it held on Capitol Hill in June 2016 to recognize World Elder Abuse Awareness Day, and has sent letters to House and Senate leadership urging expeditious consideration and passage of the bill.

In addition, FINRA finalized a rule that would allow broker-dealer and investment adviser firms and their employees to report suspected financial abuse to regulators and adult protective services, and would also provide immunity for firms that delay disbursements when financial exploitation is suspected. The FINRA rule has been submitted to the SEC for final approval.

At the state level, the North American Securities Administrators Association (NASAA) adopted a model law in February 2016 to protect vulnerable adults from financial exploitation. The model provides new tools to help securities regulators, adult protective services agencies, investment advisers and broker-dealers detect and prevent financial exploitation of vulnerable adults. The NASAA model was adopted in Alabama, Indiana, Vermont and Louisiana in 2016.

2017 Outlook

IRI will continue to actively advocate for passage of the Senior$afe Act, and expects that Congress will enact the bill in 2017. IRI also anticipates that the SEC will approve the FINRA rule in late 2016 or early 2017.

Senior financial protection will also continue to be a priority across the states, many of which will likely consider adoption of the NASAA model. IRI will continue to advocate for a cohesive regulatory framework that allows, encourages, and provides adequate protections for firms and financial professionals seeking to take appropriate steps to protect seniors and other vulnerable investors from financial abuse and exploitation.

Cybersecurity

Action on cybersecurity increased significantly this year. Following up on the Cybersecurity Bill of Rights for Insurance Consumers issued in 2015, the National Association of Insurance Commissioners (NAIC) Cybersecurity Task Force proposed a draft model law, the Insurance Data Security Model Law. IRI submitted comment letters, both directly and through an industry coalition, offering constructive recommendations to improve the model and expressing concern that the model will not achieve its goal of creating exclusive, uniform standards.

Despite the fact that the NAIC has not yet completed its model, the New York Department of Financial Services issued its own cybersecurity proposal in September. IRI and the industry coalition submitted comment letters expressing concern that the proposal departs from the risk-based security approach utilized by current cybersecurity frameworks.

In November, the Federal Reserve, the Federal Deposit Insurance Corporation, and the Comptroller of the Currency issued an advanced notice of proposed rulemaking (ANPRM) as part of a process to develop cybersecurity standards for banks and financial institutions. "With advances in financial technology, financial institutions and consumers alike have become increasingly dependent on technology to facilitate financial transactions," they wrote in the Federal Register. Comments on the proposal are due January 17, 2017.

2017 Outlook

IRI expects cybersecurity to be an increasingly active issue in 2017 with regulations being introduced in states across the country and at the same time proposed by federal agencies. IRI will maintain engagement with the NAIC, individual state regulators and the federal agencies to advocate for appropriate and uniform cybersecurity regulations..

National Insurance Producer Licensing Legislation

The National Association of Registered Agents and Brokers Reform Act (NARAB II), enacted in January 2015, created a national insurance licensing clearinghouse for financial professionals operating in multiple states. The creation of this clearinghouse, known as NARAB, will help increase the availability of lifetime income products by removing a regulatory barrier that is impeding broker-dealers' ability and financial advisors' willingness to distribute these strategies. By making the licensing process more streamlined and compliance with licensing regulations less onerous, NARAB will encourage broker-dealers and advisors operating in multiple states to offer insurance products such as annuities with lifetime income guarantees.

Before NARAB can commence operations, the President must appoint a 13-member Board, comprised of eight current state insurance commissioners, three representatives of the property/casualty industry and two representatives from the life and health sectors. President Obama announced nominees for 10 of these seats in 2016. These appointments are subject to Senate approval.

2017 Outlook

While the legislation creating NARAB was enacted with bipartisan support, approval of the NARAB nominees is not expected to be a priority for the incoming Trump Administration or Congress in 2017. IRI will pursue opportunities to encourage the White House and Congress to finalize the NARAB board so that NARAB can commence operations as soon as practicable.

State-Run Retirement Plan Proposals

Over the past several years, approximately 25 states have considered proposals to establish or study the feasibility of establishing state-sponsored retirement plans for private-sector employees. In 2016, four states — California, Connecticut, Maryland, and New Jersey — enacted legislation to create retirement savings programs for private-sector workers, bringing the total number of state-run plans to eight. Most of those laws require employers that do not offer workplace savings arrangements to automatically enroll their employees in payroll deduction IRAs administered by the states, while other state laws create a marketplace of retirement savings options designed for employers that do not offer workplace plans.

Uncertainty about the applicability of ERISA to state-run plans has been one of the most significant reasons that some states have not yet progressed beyond their feasibility studies. To ease these concerns, the Department of Labor (DOL) issued guidance in January 2016 to clarify how state-run programs can be established in compliance with ERISA. In August 2016, the DOL finalized a rule creating a new safe harbor setting forth parameters for state-run plans that would not be subject to ERISA. Among other things, the rule allows states to require that a state-run plan with automatic enrollment be made available to employees of private-sector employers who do not offer a retirement savings plan. DOL also has proposed to expand the safe harbor to larger cities and counties in states without a state-run program. IRI submitted comments urging the DOL to modify the existing safe harbor for private-sector solutions to allow the same automatic features permitted in state-run plans under this new rule. To date, the DOL has declined to implement this recommendation.

2017 Outlook

The fate of the new safe harbor rule for state-run plans is uncertain at this time, as the Trump Administration has not yet opined on this issue. Despite this uncertainly, IRI anticipates continued state legislative activity to enact state-run retirement plans during the 2017 state legislative sessions.

State Annuity Suitability and Disclosure Regulation

In 2016, four states proposed revisions to their annuity suitability regulations based on the 2010 NAIC Suitability in Annuity Transactions Model Regulation — Alabama (adopted), Delaware (pending), Massachusetts (adopted), and Missouri (pending). The current suitability model has now been adopted in 40 states.

Maryland proposed to amend its annuity disclosure regulations based on the 2011 NAIC Annuity Disclosure Model Regulation. The current disclosure model has been adopted in seven states.

At the NAIC 2016 Summer National Meeting, the Life Insurance and Annuities (A) Committee announced its intention to review and consider revisions to the suitability and disclosure models.

2017 Outlook

Several additional states will likely consider adoption of the annuity suitability and disclosure model regulations in 2017. IRI will continue to advocate for uniform adoption, implementation and interpretation of these rules throughout the states. IRI also will work with the A Committee as it undertakes to review and consider possible modifications to the models.

Market Conduct Reform

In August 2016, the NAIC Market Regulation Accreditation Working Group adopted the Market Regulation Certification Program Self-Assessment Guidelines and Checklist Tool designed to provide an initial process that facilitates each jurisdiction's ability to conduct self-evaluation.

In October 2016, the Working Group issued the Market Regulation Program Proposal for Implementation that provides recommendations for certification standards, a process for the state implementation of the standards, a process to measure the states' compliance with the standards, and a process for future revisions to the standards.

2017 Outlook

The NAIC Working Group will continue its efforts to develop market regulation accreditation standards, including a timeline for implementation of the accreditation program. IRI will continue to work with the NAIC and other industry trade groups to ensure the market regulation accreditation proposal will result in a more effective, efficient and streamlined process that reduces burdens on IRI member companies.

Annuity Sales in 2017

Projecting future annuity sales is a difficult exercise given the various economic, financial, legislative, and regulatory factors that influence the annuity market, and is particularly challenging this year due to the uncertainty surrounding both the future, and potential impact, of the DOL fiduciary rule. Demand for annuities should remain strong given consumer desire for guaranteed lifetime income, an aging population, increased longevity, increasing reliance on retirement savings for income (i.e. the disappearance of private pensions), and market volatility fueling desire for strategies that can provide income while protecting against market losses. Meanwhile, challenges to overall annuity sales, presented by the continued low interest rate environment, are expected to be eased by rising rates. In IRI's view, if interest rates gradually ascend to a level reaching or exceeding 3.0 percent in 2017 and operational issues related to conducting business within the framework of DOL fiduciary are successfully addressed, given the wealth controlled by retirees and near retirees wrestling with the problem of generating guaranteed, sustainable retirement income for life, income-oriented fixed sales should continue to grow, and sales of variable annuities with income guarantees should begin to increase. Even in a continued environment of low interest rates, 2017 should see still modest gains in sales driven by demographics and a growing preference among consumers for guaranteed income and the exchange of upside potential for downside protection, provided the impact of DOL fiduciary is minimal. In a continued low rate scenario, the strongest growth areas will likely continue to be fixed indexed products — as an alternative to higher-risk equities and low-return CDs — and deferred income annuities.

Long-Term Outlook

The long-term outlook for the annuity industry is promising. Annuity products are evolving to meet consumer demand as Americans become more aware of their retirement income needs. Research conducted by IRI in 2017 found that only 24 percent of Boomers are confident their savings will last throughout their retirement years, down from 37 percent when the study was first conducted in 2011. Despite multiple years of stock market gains, those closest to or in retirement feel less confident rather than more confident. This implies that large numbers of Boomers may have exited risk assets after the financial crisis and could not tolerate the risk of re-investing in those assets given their proximity to retirement, and/or fears about health care costs and longevity are causing them to reevaluate the ability of their nest eggs to generate sufficient income. Recent research from BlackRock bears this out. In the third edition of their Global Investor Pulse survey, BlackRock found that 65 percent of Americans' wealth is held in cash.

A new IRI research study on recent retirees found that more than four in 10 study participants received at least 50 percent of their income from a traditional pension. Conversely, only one in four Baby Boomers expect significant income from a defined benefit plan. The opportunity for the retirement income industry is clear: insurance companies are the only entities able to offer strategies that insure retirement income for a person's lifetime. In other words, they can help Boomers and future

generations replace the pensions that today's retirees depend on to enjoy a secure retirement. Annuity providers alone can provide consumers with the products they need to incorporate guaranteed lifetime income strategies into their retirement portfolios.

Consumer demand for guaranteed lifetime income will remain strong for a number of reasons:

- ***Demographics:*** Pew Research Center estimates that 10,000 Baby Boomers will turn 65 every day for the next 14 years.
- ***Consumer needs:*** IRI research shows that "guaranteed income each month" and "will not lose principal" are among the most important traits of a retirement product.
- ***Increased longevity:*** As people live longer, guaranteed lifetime income becomes a key component to managing longevity risk. For a couple age 65, there is an 85 percent chance one will make it to age 85, a 67 percent chance one will reach age 90, and for one on four couples one will reach age 95.[8]
- ***Decline of traditional pension plans:*** In 1985, there were 114,000 private-sector defined benefit pension plans, but by 2013 there were only 23,769 of these plans remaining, according to the Pension Benefit Guaranty Corporation (PBGC). The October 2016 Bureau of Labor Statistics' National Compensation Survey reports that only about 18 percent of private-sector workers have access to a traditional pension.
- ***Holistic planning embraced:*** As financial professionals continue to embrace holistic retirement planning approaches, a greater emphasis will be placed on developing plans to meet clients' needs, as opposed to merely asset accumulation. A great focus on needs will lead to more conversations on income planning and allow advisors to leverage income-generating strategies within retirement plans.
- ***Large dollar amounts in qualified plans:*** The total assets in qualified retirement plans, as of the end of 2015, were $23.9 trillion, down about 3 percent from the end of 2013. The following table details this amount by the different types of retirement plans.

Assets in Tax Qualified Retirement Plans Year-End 2015

Private Trusted Defined Benefit Plans	$2.9 trillion
Private Trusted Defined Contribution Plans	$6.7 trillion
Individual Retirement Accounts (IRAs)	$7.3 trillion
State and Local Government Plans	$3.6 trillion
Federal Government Retirement Plans for Federal Employees	$1.5 trillion
Annuities	$1.9 trillion
Total	**$23.9 trillion**

Sources: Investment Company Institute with data derived from Federal Reserve Board, Department of Labor, National Association of Government Defined Contribution Administrators, American Council of Life Insurers, and the Internal Revenue Service Statistics of Income Division.

- ***Concerns about Social Security and other governmental programs:*** The 2016 Social Security Trustees Report projects the combined Old Age and Survivors Insurance and Disability Insurance Trust Fund will be exhausted in 2034. The 2016 Medicare Trustees Report projects that the Hospital Insurance Trust Fund (Part A) will be depleted in 2028, two years earlier than last year's report.

SUMMARY

Current retirees rely heavily on pension income to enjoy a secure retirement. As America ages, and particularly as Baby Boomers without pensions enter retirement at the rate of 10,000 per day, the need to efficiently use retirement savings for guaranteed lifetime income continues to grow. Baby Boomers, and Generation Xers that follow, have not saved enough to withdraw as needed to fund their lifestyles and be assured of both maintaining the ability to support themselves and defraying the expenses associated with health care and long-term care. The retirement income industry must work diligently to ensure that consumers are aware of the risks they face in retirement, and that they adequately protect themselves. "Winning" at retirement saving and investing is not defined as achieving the highest possible return or the lowest possible cost, but by creating sustainable income and protecting against financial ruin. Despite headwinds such as regulatory pressures and low interest rates, the retirement income industry continues to offer and innovate the products that can help consumers confidently sail into retirement and weather the storms. The industry will need to continue to promote the value of these strategies to consumers.

Insurance companies remain financially strong, and head into 2017 well capitalized and able to withstand financial shocks. On the public policy front, the DOL's fiduciary rule is still scheduled to go into effect in April 2017. While disruptive, the industry will survive and thrive as demographics drive consumers inexorably toward the need to create their own pensions. Finally, will 2017 be the year of the long-awaited rise in interest rates? Anticipated tax cuts under the new administration, coupled with infrastructure spending, are key ingredients in a recipe for rising rates. The jury, however, will remain stubbornly out until these events are cemented and begin to play out.

Research Citations

[1] BlackRock, "2015 Blackrock Global Investor Pulse"

[2] JP Morgan, "The Long And Short of Baby Boomer Balance Sheets," October 2015

[3] IRI, "Boomer Expectations for Retirement 2016"

[4] IRI, "It's All About Income: Inaugural Study on the American Retirement Experience"

[5] Fitch Ratings, "2017 Outlook: U.S. Life Insurance"

[6] Ignition House, Business Research Co.

[7] Hearts & Wallets, "Portrait of U.S. Household Wealth 2016"

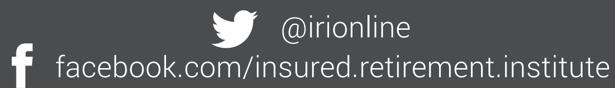
[8] Society of Actuaries, 2012 Individual Annuitant Mortality Tables With No Mortality Improvement

Additional supporting research for this report was derived from publicly available research from the 2016 Social Security Trustees Report; 2016 Medicare Trustees Report; American Council of Life Insurers; Beacon Research; the Bureau of Labor Statistics; the Department of Labor; the Federal Reserve Board; Internal Revenue Service Statistics of Income Division; Investment Company Institute; Morningstar, Inc.; the National Association of Government Defined Contribution Administrators; Pension Benefit Guaranty Corporation; St. Louis Federal Reserve Board, Federal Reserve Economic Data (FRED); Society of the Actuaries.

Special Thanks

IRI would like to acknowledge the following members of the IRI Research Committee, and thank them for their contributions to this report: Robert Chamerda, Guardian Life Insurance (Committee Chair); Joseph Powell, MetLife (Committee Vice-Chair); Jeremy Alexander, Beacon Research; Donnie Ethier, Cerulli Associates; Kevin Loffredi, Morningstar, Inc.; and Michael Raymond, Prudential Financial.

Insured Retirement Institute
202-469-3000 | 202-469-3030 (fax)
membership@irionline.org | myirionline.org


@irionline
facebook.com/insured.retirement.institute