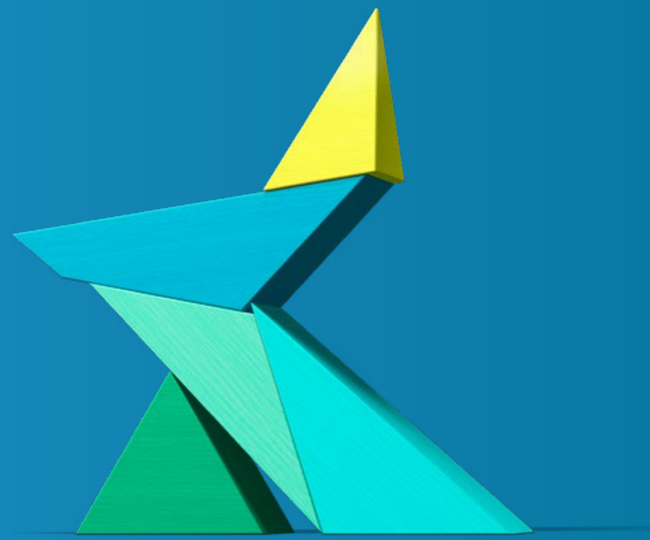
welcome to brighter



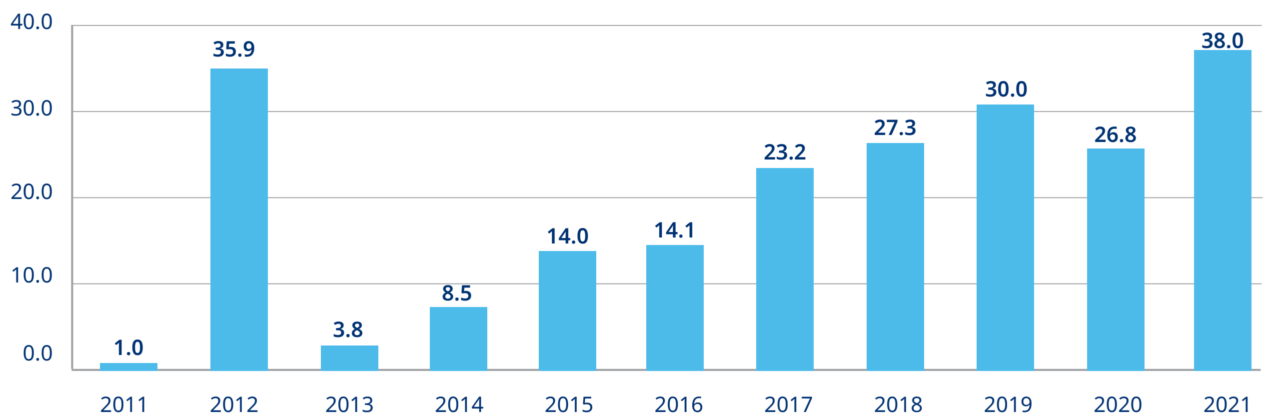
2021 was a record year for the

pension risk transfer market

The year 2021 saw $38B of pension liabilities transferred from the defined benefit pension system to the insurance system. To put this record-breaking activity in context, we are approaching the 10-year anniversary of the single largest pension risk transfer transaction ever (GM, $25B in November 2012). In what continues to be a growing and evolving market, plan sponsors completed over 430 successful risk-transfer transactions last year, covering both full plan terminations and cost-saving retiree lift-outs.

Great pricing, innovation and strong insurer competition is continuing to unfold, so plan sponsors remain in a good position to evaluate and execute on their pension journey plans.

Pension Risk Transfer Deal Volume
2011–2021



Sources: Mercer Quarterly Insurer Pension Risk Transfer Sales Survey and LIMRA annual market volume reports 12/31/21

During a period of continued business disruptions and challenges brought by the COVID-19 pandemic, pension risk transfer activity stayed strong in 2020 before accelerating in 2021. Adapting to a new work environment and challenges posed by the pandemic, insurers continued to participate in competitive bids and were dedicated to uninterrupted servicing of their current and new policyholders.

Retiree benefit buyouts increasingly attractive

After the wave of deferred vested cashouts, retiree buyouts have become another popular de-risking tool. In a retiree buyout, a plan sponsor transfers the liability and administration of pension benefits that are currently in pay status to an annuity provider. This type of transaction is seamless for the retirees who continue to receive their pension payment in the same form and at the same time as elected upon retirement, just from a different issuer. As seen below, retiree-only transactions have increased in popularity over the past three years, accounting for close to 75% of total market volume in 2021.

	2019	2020	2021
Buy-in	6%	7%	10%
Plan-termination buyout	41%	33%	15%
Retiree-only buyout	53%	60%	75%

Source: Mercer Quarterly Insurer Pension Risk Transfer Sales Survey for 12/31/19, 12/31/20 and 12/31/21

The apparent decline in plan termination activity in 2021 is an immediate impact of the pandemic: Plan terminations are actually on a 12- to 18-month lag, with plan sponsors having delayed plan-termination commencements when the pandemic hit in order to focus on stabilizing their businesses. Now that the pandemic appears to be largely behind us, plan-termination activity has picked up, and we expect to see them make up a larger share of future pension-risk activity.

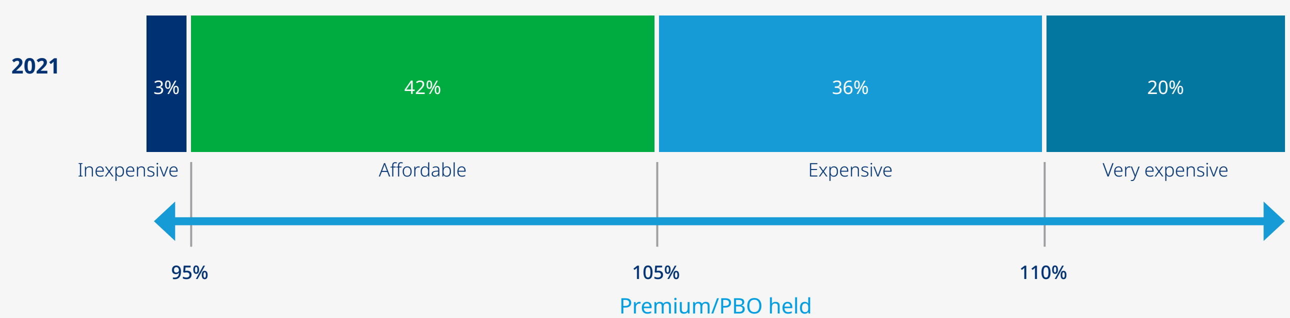
Pricing considerations

The Mercer 2021 CFO survey revealed that there is still a pricing misconception about the annuity market. Over half (56%) of respondents believe that the cost of an annuity buyout for retirees relative to the pension obligation held on the balance sheet is 105% or higher.

Risk transfer through annuity buyouts

Plan sponsors are unaware of the current annuity cost

What is your perception of the cost of an annuity buyout for retirees in your pension plan, relative to the pension benefit obligations held on your balance sheet?



Observation

Cost of annuities perceived to be more expensive than current experience would prove.

The average retiree buyout completed by Mercer during 2021 settled at 98% of market liability, based on the current mortality tables and an AA curve such as the Mercer Yield Curve. Many factors influence transaction pricing: deal size, complexity of benefits, quality of data and longevity expectations based on the population profile. To put forward the best possible price, insurers sometimes turn to reinsurance partners and look for assets that best support the transaction.

To assist plan sponsors in seeking further value through pension risk transfer, Mercer launched the Market Window Auction. This innovative approach allows the annuity buyout to occur over a series of bid days, rather than one day. By allowing multiple opportunities for insurers to meet client set targets, we help mitigate the risk of a "bad finals date" and help plan sponsors take advantage of opportunistic market pricing. Based on the transactions that Mercer executed in 2020 and 2021, Market Window Auction generated average savings of 100 basis points[1].

Small-balance retiree buyouts present opportunities for plan sponsors

The most common form of retiree buyouts focuses on participants with smaller benefits, which may offer several key advantages to sponsors. Participants with the smallest benefits carry a disproportionately large cost of holding and administering their liability in a defined benefit plan. Benefit size is considered a socioeconomic indicator and, as a result, lower benefit sizes tend to be correlated with higher mortality. Insurers price this type of liability more aggressively when compared to the accounting liability that plan sponsors are carrying. In Mercer's experience, this type of transaction settles for an average price that is less than the accounting liability, achieving financial success for plan sponsors.

Pension volume driven by jumbo transactions

Jumbo transactions are defined as having a premium in excess of $1B and generally involve the transfer of a large population to the selected insurer. In 2021, half of the total deal volume came from eight jumbo transactions, which was more activity at this market tier than in the prior two years combined.

Jumbo transactions	2019	2020	2021
Premium $	8.5B	5.2B	19.3B
Count	4	4	8
% of total	28%	19%	51%

Source: Mercer Quarterly Insurer Pension Risk Transfer Sales Survey for 12/31/19, 12/31/20 and 12/31/21

In 2021, the jumbo market saw new plan sponsors completing their first insurer engagement, as well as seasoned plan sponsors who have already executed several buyouts and buy-ins.

In a **buyout**, the obligation and administration are transitioned irrevocably to an insurance company. In a **buy-in**, the plan sponsor retains the administration while the insurance company has the financial liability.

In essence, the plan sponsor holds the annuity contract as a plan asset, hedging the risks carried by the defined benefit plan.

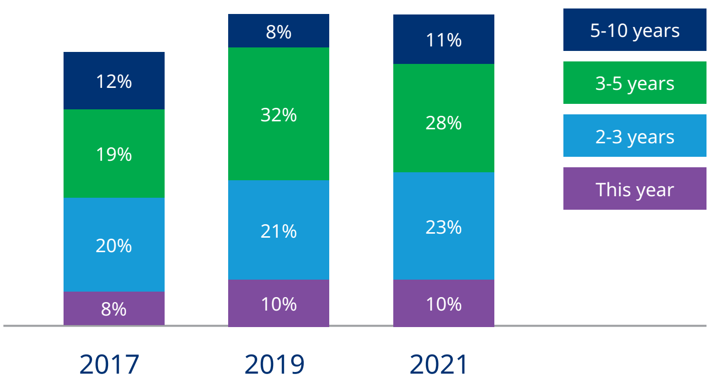
[1] Based on actual transaction data from Mercer deals using this structure. There can be no assurance that these results can be achieved. Actual results are likely to vary.

One notable transaction in 2021 was a $2.8B buy-in purchased as part of a plan termination. We expect this construct to become more common as plan sponsors pursuing plan terminations are looking for pricing certainty while going through the regulatory process of the plan termination.

Terminations are also becoming more prevalent

The Mercer 2021 CFO survey indicated that 72% of organizations are considering terminating their defined benefit (DB) plan within the next 10 years, up from 59% in 2017.

What is your organization's timeline for considering terminating the pension plan?



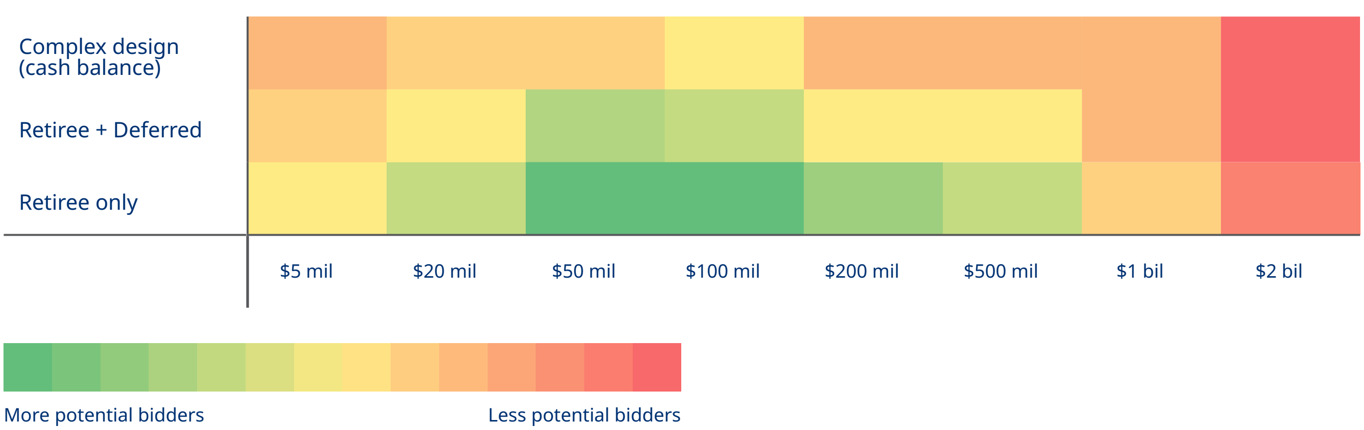
Source: 2017, 2019 and 2021 Mercer CFO Survey

Strong equity markets and increasing interest rates during 2021 significantly improved the funded status of pension plans. Nearly 40% of plan sponsors in the S&P 1500 are now more than 100% funded and are closer to a financial position to terminate their plans[2].

As noted earlier, 2021 termination activity was lower, but we expect it to increase markedly in 2022 and beyond.

Insurer market is expanding

There are currently 19 insurers in the US pension risk transfer market, up from just six a decade ago. In the last 18 months alone, we have had four new entrants, and we are expecting this trend to continue. High demand from plan sponsors looking to offload liability is met by increased capacity, with insurers finding their competitive edge and gravitating toward a certain segment of the market. Transaction size, liability type, demographic profile and industry are some of the categories that insurers use to define certain market niches. Some insurers are looking at expanding their current target markets. For example, some insurers that would formerly only underwrite retirees recognize the increase in plan terminations and are looking at entering the deferred-benefits market. Other insurers are now starting to explore pension risk transfer opportunities. We like to say there is a home for every liability. When there is a demand, the insurers will find a solution and implement it in an efficient manner. Plan sponsors may further benefit from this dynamic.



Source: 2021 Mercer's Annual Market Review Questionnaire

[2] Source: Standard & Poor's Capital IQ. Standard and Poor's is a division of The McGraw-Hill Companies Inc.

Outlook for 2022

Looking ahead, we expect the pension risk market to build on last year's momentum. Generally, improved funded status now allows more plan sponsors to consider transferring liabilities to an insurer, thereby reducing volatility and cost inherent in the pension plan.

We expect plan terminations to increase in number, allowing for a steady flow of transactions given the long regulatory process that plan sponsors need to undertake. We recommend that plan sponsors engage insurers early, to assess their interest and allow them to plan resources for the upcoming transactions. We have found that longer lead times ultimately benefit both sides. For well-funded plans, locking in pricing and capacity early via a buy-in might provide sufficient incentive to pursue a plan termination. We expect to see more insurers develop buy-in contracts to meet this anticipated increased demand.

Retiree-only transactions will continue to be popular, building on the success seen over the past 10 years. Plan sponsors can take steps to ensure they are transaction-ready by completing feasibility studies to determine the optimal population to target. Success will depend on the robustness of the process: ensuring data is insurer-ready, completing a mortality study (if needed) and engaging the insurers early to reserve capacity. Setting clear targets for insurers to meet also contributes to pricing transparency. Finally, by using innovative practices such the Market Window Auction, price-sensitive plan sponsors can have greater confidence in their strategic decisions.

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