Session 35 PD, Annuity Product Update

Moderator:
Kevin W. Rabin, FSA, MAAA

Presenters:
Aatman Naresh Dattani
Yuan Tao, FSA, CFA, MAAA
Judith Zaiken, CLU, ChFC
SOA 2017 Life & Annuity Symposium
U.S. Macro Annuity Trends
May 8, 2017

Judy Zaiken
LIMRA Secure Retirement Institute
Sales Trends – Product Mix
Annuity Sales Mix Over Time

Source: LIMRA Secure Retirement Institute, U.S. Individual Annuities survey
Back a decade ago…

Source: LIMRA Secure Retirement Institute, U.S. Individual Annuities survey
Source: LIMRA Secure Retirement Institute, U.S. Individual Annuities survey
Annuity sales have shifted dramatically

Source: LIMRA Secure Retirement Institute, U.S. Individual Annuities survey
Total annuity sales pulled down by VA’s

<table>
<thead>
<tr>
<th></th>
<th>Total</th>
<th>Variable Annuity</th>
<th>Fixed Annuity</th>
</tr>
</thead>
<tbody>
<tr>
<td>2012</td>
<td>$219.7b</td>
<td></td>
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</tr>
<tr>
<td>2013</td>
<td>$229.8b</td>
<td>$236.9b</td>
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<tr>
<td>2014</td>
<td>$236.9b</td>
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<tr>
<td>2015</td>
<td>$235.7b</td>
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<tr>
<td>2016</td>
<td>$222.1b</td>
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</table>

Source: LIMRA Secure Retirement Institute, U.S. Individual Annuities survey
VA Sales have only seen 1 quarter of growth since 2012

U.S. Individual Variable Annuity Sales (in billions)

Risk management key factor in slow decline

Source: LIMRA Secure Retirement Institute, U.S. Individual Annuities survey
U.S. Individual Variable Annuity Sales (in billions)

Fiduciary regulation accelerated decline

Source: LIMRA Secure Retirement Institute, U.S. Individual Annuities survey
VA GLB sales now make up less than half of total VA Sales

Variable Annuity Sales

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</thead>
<tbody>
<tr>
<td>VA Employer Plan Sales</td>
<td>16%</td>
<td>16%</td>
<td>15%</td>
<td>16%</td>
<td>17%</td>
<td>15%</td>
<td>16%</td>
<td>18%</td>
<td>20%</td>
<td>20%</td>
<td>20%</td>
<td>21%</td>
</tr>
<tr>
<td>VA sales - No GLB, Either not Available or not Elected</td>
<td>27%</td>
<td>28%</td>
<td>27%</td>
<td>30%</td>
<td>30%</td>
<td>32%</td>
<td>29%</td>
<td>29%</td>
<td>30%</td>
<td>32%</td>
<td>33%</td>
<td>35%</td>
</tr>
<tr>
<td>VA sales - GLB Elected</td>
<td>57%</td>
<td>56%</td>
<td>58%</td>
<td>54%</td>
<td>53%</td>
<td>53%</td>
<td>54%</td>
<td>53%</td>
<td>51%</td>
<td>48%</td>
<td>47%</td>
<td>44%</td>
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</tbody>
</table>

Source: LIMRA Secure Retirement Institute, U.S. Individual Annuities survey
LIMRA Secure Retirement Institute, VA GLB Election Tracking Survey
Income Later Sales – Less Dominated by GLWB

Source: LIMRA Secure Retirement Institute, U.S. Individual Annuities survey, VA & Indexed GLB Election Tracking Survey
VA GLB sales exclude GMAB sales
Analysis includes new/existing sales and excludes sales of FRD annuities with a GLB rider
66% of retail VA assets now have a GLB rider

IN-Force VA Assets with GLB

- 2010: $521 B
- 2012: $661 B
- 2014: $843 B
- 2015: $838 B
- 2016: $884 B

Note: Retail = VA with GLB + VA without GLB; Excludes individual annuities in employer plans.
14 Record indexed annuity sales in 2016

<table>
<thead>
<tr>
<th>Year</th>
<th>Q1</th>
<th>Q2</th>
<th>Q3</th>
<th>Q4</th>
<th>Q1</th>
<th>Q2</th>
<th>Q3</th>
<th>Q4</th>
<th>Q1</th>
<th>Q2</th>
<th>Q3</th>
<th>Q4</th>
<th>Q1</th>
<th>Q2</th>
<th>Q3</th>
<th>Q4</th>
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<tr>
<td>2012</td>
<td>$33.9b</td>
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<tr>
<td>2013</td>
<td>$39.3b</td>
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<td>$48.2b</td>
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<td>2015</td>
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<td>$54.5b</td>
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<td>2016</td>
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<td>$60.9b</td>
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A positive reaction to the initial DOL fiduciary proposal

U.S. Individual Indexed Annuity Sales (in billions)

April 2015 – Release of initial DOL fiduciary rule listing FIA’s under 84-24 exemption

2014
Q1: $11.3  Q2: $13.0  Q3: $11.9  Q4: $12.2

2015
Q1: $11.6  Q2: $12.5  Q3: $14.3  Q4: $16.1

2016
Q1: $15.0  Q2: $16.2  Q3: $15.7  Q4: $16.0

Indexed sales momentum changed in 2016

U.S. Individual Indexed Annuity Sales (in billions)

April 2016 – Release of final DOL fiduciary rule listing FIA’s under BICE

FRD sales strong in 2016 despite low interest rates


Fixed rate deferred = Market value adjusted + Book value

<table>
<thead>
<tr>
<th>Year</th>
<th>Q1</th>
<th>Q2</th>
<th>Q3</th>
<th>Q4</th>
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</thead>
<tbody>
<tr>
<td>2012</td>
<td>$24.7b</td>
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<tr>
<td>2013</td>
<td>$29.3b</td>
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<tr>
<td>2014</td>
<td>$30.8b</td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>2015</td>
<td>$30.9b</td>
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<tr>
<td>2016</td>
<td>$38.7b</td>
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</tbody>
</table>
Disappointing end to 2016 for income annuities

Sales Trends – Investor Objectives
Guaranteed income is the largest component of annual annuity sales.

Source: *U.S. Individual Annuity Yearbook – 2015* and VA GLB Election Tracking Survey, LIMRA Secure Retirement Institute, 2016. Note: Totals are for retail sales only and exclude sales in employer plans and structured settlements. Guaranteed income bucket includes VA sales with GLWB/GMIB/GMWB rider elected, fixed indexed sales with GLWB rider elected, immediate income annuity (SPIA) and deferred income annuity (DIA).
$1.1 Trillion* invested in annuities for guaranteed lifetime income/withdrawals

Annuity Assets Directly Associated with Guaranteed Lifetime Income/Withdrawals – 2015

- Fixed Income**: $98 B
- DIA**: $9 B
- Var. Income**: $4 B
- VA with GLBs: $836 B
- Indexed with GLWB**: $168 B

Set & Done

Set & Ready-to-Draw


*An important component, already annuitized assets in variable, fixed-rate and indexed annuities, is not reflected due to non-availability of the data. **Estimates of year-end annuity assets in reserve.
Annuity owners draw $8,000 – $11,000 in annual guaranteed lifetime income or withdrawals

- **Deferred Income**: $10,849 Per Year
  - Based on 11,497 contracts

- **Fixed Immediate**: $10,342 Per Year
  - Based on 34,530 contracts

- **VA with GLWB**: $8,167 Per Year
  - Based on 456,603 contracts

Focus on changing fiduciary requirements goes well beyond sales

IMPACT OF DOL FIDUCIARY RULE ON ANNUITY ASSETS

- $191 BILLION IRAs in Indexed
- $725 Billion IRAs in VAs
- $652 BILLION Employer Plans in VAs
- $14 BILLION Employer Plans in Indexed
- $725 BILLION IRAs in Indexed
- $100 Billion* Annual sales under BIC-E
- $652 BILLION Employer Plans in VAs

$750 Billion may be converted into guaranteed lifetime income

Opportunity for Annuity with Guaranteed Lifetime Income in Retirement (in billions)

LIMRA Annuity Sales Forecast
The VA landscape will continue to be shaped by regulation

Individual Variable Annuity Sales Forecast

2016
$104.7b
↓ 21%

2017
↓ 10-15%

2018
↓ 10-15%

Source: LIMRA Secure Retirement Institute, April 2017. Updated periodically on: www.limra.com/DOL.
Distribution disruptions will hinder indexed annuity sales

Individual Indexed Annuity Sales Forecast

2016
$60.9b
↑ 12%

2017
↓ 5-10%

2018
↓ 15-20%

Source: LIMRA Secure Retirement Institute, April 2017. Updated periodically on: www.limra.com/DOL
Fixed-rate deferred annuity sales are expected to grow

2016: $38.7b ↑25%

2017: ↑0-5%

2018: ↑15-20%

Source: LIMRA Secure Retirement Institute, April 2017. Updated periodically on: www.limra.com/DOL.
Income annuity sales will increase but not until 2018.
Annuity market will see single digit declines in next two years

**Individual Total Annuity Sales Forecast**

- **2016**
  - $222.1b
  - ↓6%

- **2017**
  - ↓5–10%

- **2018**
  - ↓0–5%

Source: LIMRA Secure Retirement Institute, April 2017. Updated periodically on: www.limra.com/DOL.
Agenda

Variable Annuities
- Overview of the Market
  - Sales by Company
  - Sales by Distribution Channel
  - Guaranteed Living Benefits – Sales, Distribution Channels and Elections

Product Related Updates
- Recent Product Changes
- Milliman Hedge Cost Index
- Structured Variable Annuities
- Predictive Model as a Potential Tool for Pricing and Product Development

Assets

Global Response to the Low Interest Rate Environment
Overview of the Variable Annuity Market

- 2016 Variable Annuity Sales ("VA") declined by 21% vs. 2015
- The VA sales to equity market correlation does not hold anymore

Source: LIMRA
Variable Annuity Sales by Company

- There has been a reshuffling in ranks of the top 10 VA writers vs. 2012
- De-risking, diversification of product offerings, changes in regulation (fair value, DOL) likely impacted sales

Sales in $ billions
Source: LIMRA
Variable Annuity – Sales by Distribution Channel

- Sales by distribution channel have stayed consistent in spite of an overall decline in sales
Variable Annuity – Guaranteed Living Benefit Sales

- The percentage of VA's available without GLB's has risen from 7% in 2013 to 20% in 2016
- GLWB is the most elected rider (around 70% of the time) with GMIB a distant second (7-10%)

Source: LIMRA

<table>
<thead>
<tr>
<th>Year</th>
<th>GLB Elected</th>
<th>GLB Available, Not Elected</th>
<th>GLB Not Available</th>
<th>Employer Plan</th>
</tr>
</thead>
<tbody>
<tr>
<td>2011 ($158bn)</td>
<td>17%</td>
<td>7%</td>
<td>9%</td>
<td>67%</td>
</tr>
<tr>
<td>2012 ($147bn)</td>
<td>19%</td>
<td>9%</td>
<td>9%</td>
<td>64%</td>
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<tr>
<td>2013 ($145bn)</td>
<td>17%</td>
<td>11%</td>
<td>12%</td>
<td>59%</td>
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<tr>
<td>2014 ($140bn)</td>
<td>16%</td>
<td>13%</td>
<td>15%</td>
<td>56%</td>
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<tr>
<td>2015 ($133bn)</td>
<td>16%</td>
<td>17%</td>
<td>14%</td>
<td>52%</td>
</tr>
<tr>
<td>2016 ($105bn)</td>
<td>20%</td>
<td>20%</td>
<td>12%</td>
<td>48%</td>
</tr>
</tbody>
</table>

Source: LIMRA
Independent Agents are the largest seller for GLWBs while Career Agents lead in GMIB and GMAB.

GLB elections, when available, have typically declined.

**Rider Sales by Channel 2Q 2016**

- **GLWB**
  - Wirehouses: 21%
  - Independent: 16%
  - Career: 19%
  - Bank: 44%

- **GMIB**
  - Wirehouses: 13%
  - Independent: 12%
  - Career: 41%
  - Bank: 34%

- **GMAB**
  - Wirehouses: 8%
  - Independent: 7%
  - Career: 84%
  - Bank: 8%

- **GMWB**
  - Wirehouses: 11%
  - Independent: 17%
  - Career: 63%
  - Bank: 49%

- **Hybrid**
  - Wirehouses: 21%
  - Independent: 31%
  - Career: -
  - Bank: -

**Election Rates - When Available**

Source: LIMRA
Variable Annuity Market Product Changes

- VA products in the last year have been de-risked using the following strategies:
  - Increase in Rider Fees
  - Limitations in Contributions
  - Reduction in Benefits
  - Benefits that Differ by Age
  - Fund Allocation Limitations
  - Links to VIX, Treasury Indexes
  - New Products e.g. IOVA
  - Closing Existing Products
  - Volatility Control Funds
Milliman Hedge Cost Index

- Estimated Hedge Cost for a typical Lifetime GMWB
- Rider fee of 1.15%; M&E and Investment Management Fees of 2.25%
- Annual 5% rollup and resets; lifetime withdrawal rates of 4-6% depending on attained age
- Modeling Assumptions based on typical actuarial and behavioral assumptions used by VA writers
- Target fund volatility of 10%; calculations based on end of month US swap rates
Structured Variable Annuities

- Companies introduced this product to diversify their product offering
- Built on VA chassis but share downside risk with policyholder
- Sales have increased over 100% in 2016 to $5.4 billion
- Impact of rising interest rates
- Demographics of buyers

Source: LIMRA
Predictive Modeling – Potential Tool for Product Development

- Rating Agencies and Regulators are placing higher scrutiny on company assumptions
- Predictive modeling of policyholder behavior offers a statistically defensible framework for demonstrating assumption effectiveness to internal and external stakeholders

Milliman GLWB utilization study (2m policies from 7 VA writers, 2007-2015 experience):

- Policyholders who are older at issue are up to 30 times more likely to begin withdrawals in the first quarter
- Policyholders are half as likely to utilize on a policy with a roll-up than one without, regardless of length of roll-up period
- Less than half of policyholders utilize their lifetime benefits with 100% efficiency
Variable Annuity Assets

- 2015 VA Assets declined for the first time since the financial crisis
- Stagnant equity markets and negative net flows resulted in the drop
  - Outflows exceeded inflows in all four quarters

Source: LIMRA

<table>
<thead>
<tr>
<th>Year</th>
<th>Dollars in Billions</th>
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<tbody>
<tr>
<td>2006</td>
<td>1,397</td>
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<tr>
<td>2007</td>
<td>1,517</td>
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<td>2008</td>
<td>1,151</td>
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<td>2009</td>
<td>1,389</td>
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<td>2010</td>
<td>1,561</td>
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<td>1,593</td>
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<td>2012</td>
<td>1,762</td>
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<td>2013</td>
<td>1,908</td>
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<td>2014</td>
<td>1,967</td>
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<tr>
<td>2015</td>
<td>1,922</td>
</tr>
<tr>
<td>2016</td>
<td>1,984</td>
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</table>
Strategic shift

- Low Rates here to stay
- Move away from interest rate risk
- Focus on unit linked and protection products
- Pension reforms

Q1 2016 Sales dropped 8% in UK, 45% in France and 18% in Rest of Europe.

- GMWB sales dropped while GMAB sales rose.
- Product De-risking to blame?

- Negative Interest Rates
- USD, AUD and NZD denominated products replaced GMAB (JPY)
- SPWL with VA Features
- Variable Life with GMDB converted to fixed life in 15-20 years (FIT)
- Premium invested in two buckets during FIT: stable + aggressive
- Stable fulfills guarantee, aggressive allows for upside

Global Impact of the Low Interest Rate Environment on VAs
Thank you

Aatman Dattani
aatman.dattani@milliman.com
Fixed and Indexed Annuity Product Update

Sessions 23 & 35 PD

2017 Life and Annuity Symposium

Seattle - May 8, 2017

Yuan Tao, FSA, MAAA, CFA
Agenda

1. Sales and market trends
2. Impact of DOL
3. Product trends
4. Key takeaways
Indexed annuities continue to gain in importance while income annuities remain a small segment.

Source: LIMRA and Wink Sales Market Report
Top 10 FIA writers make up nearly 70% of industry sales

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<td>Allianz Life</td>
<td>10.20</td>
<td>8.75</td>
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<td>2</td>
<td>American Equity</td>
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<td>-16%</td>
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<td>3</td>
<td>Athene</td>
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<td>Midland National</td>
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<td>20%</td>
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<td>7</td>
<td>Nationwide</td>
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<td>2.49</td>
<td>8%</td>
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<td>8</td>
<td>Global Atlantic</td>
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<td>1.53</td>
<td>42%</td>
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<td>9</td>
<td>North American</td>
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<td>1.47</td>
<td>39%</td>
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<tr>
<td>10</td>
<td>Symetra</td>
<td>2.00</td>
<td>2.39</td>
<td>-16%</td>
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</table>

Source: Wink’s Sales & Market Report and LIMRA
Impact of DOL Fiduciary Rule
If the Rule survives…

<table>
<thead>
<tr>
<th>Potential impact</th>
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<tbody>
<tr>
<td><strong>Sales / distribution</strong></td>
</tr>
<tr>
<td>• Lower FIA sales, particularly in IMOs due to BICE financial institution requirement</td>
</tr>
<tr>
<td>• Higher fixed-rate annuity sales, due to less onerous requirements under PTE 8424</td>
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<tr>
<td>• Shelf standardization by distributors</td>
</tr>
<tr>
<td>• More focus on RIA channel</td>
</tr>
<tr>
<td><strong>Product design</strong></td>
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<tr>
<td>• More fee-based products</td>
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<tr>
<td>• Simpler designs</td>
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<tr>
<td>• Downward pressure on commissions</td>
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<tr>
<td>• Pressure to reduce size and length of surrender charge</td>
</tr>
<tr>
<td><strong>Product pricing</strong></td>
</tr>
<tr>
<td>• Lower and more dynamic lapse behavior</td>
</tr>
<tr>
<td>• More rational GLWB utilization behavior</td>
</tr>
<tr>
<td>• Lower commission</td>
</tr>
<tr>
<td>• Higher acquisition and maintenance expenses for DOL compliance</td>
</tr>
</tbody>
</table>
FIA product trends
Half of FIA writers have or plan to introduce a fee-based FIA in 2017, according to LIMRA

- Fee-based FIAs had insignificant market share in 2016 (~1%)
- Recent launches are shown below:

  **Great American**
  Launching Indexed Protector 7
  (August 2016)

  **Lincoln**
  Launching Lincoln Core Capital and Lincoln Covered Choice 5 and 7
  (February 2017)

  **Allianz Life**
  Launching New Retirement Foundations ADV Annuity
  (February 2017)

The success of fee-based FIAs remains to be seen
Hybrid indices continue to gain popularity

**Trend**

**S&P 500**
- Continues to be the most popular choice but losing market share
- Slightly less than 50% of sales as of 4Q 2016

**Hybrid**
- Gaining popularity, representing 30% of sales as of 4Q 2016
- Often proprietary, typically volatility controlled
- Typically used for uncapped strategy
- Often “illustrates” more favorably

**Fixed**
- Increased share, possibly due to relative attractiveness of fixed rate

**Other**
- Combined share less than 7%

Source: Wink’s Sales and Market Report
FIA product trends (continued)
GLWBs continue to be the main driver of sales with secondary features helping writers differentiate

<table>
<thead>
<tr>
<th>Trend</th>
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<tbody>
<tr>
<td><strong>GLWB index-linked income growth</strong></td>
<td>• “Stacked” rollups (e.g. 4% + account value performance)</td>
</tr>
<tr>
<td></td>
<td>• “Turbocharged” account value driving income</td>
</tr>
<tr>
<td></td>
<td>• Income increases after income start</td>
</tr>
<tr>
<td><strong>Other GLWB structures</strong></td>
<td>• Rollups are compound / simple / or absent (e.g., vary income by age / duration)</td>
</tr>
<tr>
<td></td>
<td>• Less breakpoints in income bands</td>
</tr>
<tr>
<td></td>
<td>• More income options (flat, guaranteed increase or index-linked increases)</td>
</tr>
<tr>
<td><strong>Nursing home income riders</strong></td>
<td>• Offered for free or additional charge (e.g. 10 bps)</td>
</tr>
<tr>
<td></td>
<td>• Typically doubles the income for up to 5 years if cannot perform 2 of 6 ADLs</td>
</tr>
<tr>
<td></td>
<td>• Complex to price from first principles</td>
</tr>
<tr>
<td><strong>Enhanced death benefits</strong></td>
<td>• Offered with or without GLWB (sometimes for an additional charge)</td>
</tr>
<tr>
<td></td>
<td>• Maximum payout</td>
</tr>
<tr>
<td></td>
<td>• Payout periods / reduced lump sum</td>
</tr>
</tbody>
</table>
Fixed annuity product trends
GLWB riders on fixed deferred annuities provide an attractive alternative to DIAs

Case Study: Male, 55-year old, $100,000 single deposit *

<table>
<thead>
<tr>
<th></th>
<th>FA with GLWB</th>
<th>Deferred Income Annuity</th>
</tr>
</thead>
<tbody>
<tr>
<td>Deferral Period</td>
<td>10 years</td>
<td>10 years</td>
</tr>
<tr>
<td>Annual Increase Rate</td>
<td>5% compounding</td>
<td>N/A</td>
</tr>
<tr>
<td>Income Base end of Deferral Period</td>
<td>$162,889</td>
<td>N/A</td>
</tr>
<tr>
<td>Guar Lifetime Withdrawal Rate</td>
<td>5.5%</td>
<td>N/A</td>
</tr>
<tr>
<td>Monthly Lifetime Income Amount</td>
<td>$747</td>
<td>$760 (with cash refund)</td>
</tr>
</tbody>
</table>

* Product features and quote are based on Fidelity.com as of April 4, 2017

Several writers offer a GLWB rider on fixed deferred annuities: New York Life (entered in 2015), American Equity, Midland National and National Life
Key takeaways

1. FIAs continue to be the fastest growing annuity segment
2. DOL ruling is driving the near-term market outlook
3. Writers and product will continue to adapt
Session Q&A