Challenger chief executive Brian Benari says the retirement income reforms "will drive product innovation". PHOTO: BEN RUSHTON

# New market for deferred annuities a boon with risks for Challenger

Sally Rose

Most pundits reckon new tax breaks and booming demand for deferred annuities will be a boon for Challenger Group, but sceptics worry about the associated market risks.

Deferred annuities are insurance-like financial products that entitle the owner to a fixed income if they live to a certain age.

Consensus analyst forecasts for Challenger were upgraded last month after the 2016-2017 federal budget confirmed the government plans to change the tax rules to make deferred annuities more attractive for new retirees.

"The retirement income reforms in the recent federal budget are a big positive for Challenger and will drive product innovation," Challenger chief executive Brian Benari told investors at the wealth management firm's annual strategy day in Sydney last week.

Shares in Challenger have surged more than 50 per cent over the past year amid growing demand from an ageing population for its broader range of annuities and other retirement income products.

In December the government said it would accept a recommendation of the 2014 Financial System Inquiry, headed by David Murray, to force all superannuation providers to default their retiring members into a "retirement income" pension account.

As the biggest annuities maker in the market Challenger is ideally placed to profit from the regulatory changes.

The stock hit an all-time high of $9.57 on May 31 as investors digested a raft of positive analyst reports in response to the budget announcement. Challenger's share price has come off slightly since then, last priced at $9.41.

Annuity sales are tipped to swell as more superannuation funds incorporate Challenger's products into their offerings.

Two industry funds, Vic Super and Legal Super, will begin offering Challenger annuities to their retiring members from next month. Care Super will start including Challenger annuities in its pension solutions from October.

The biggest super fund administrator, Link Group, has said it expects to sell more Challenger annuities to the super funds using its platform.

Commonwealth Bank-owned Colonial First State has also said it expects its customers to buy more of the products.

A more favourable tax treatment on deferred annuities is tipped drive a boom in demand. "We are keen to bring new deferred lifetime annuities on to the platform as soon as they are available," a CFS spokesman said.

Challenger is forecast to sell a record $200 million worth of deferred annuities in the December quarter this year.

Analysts from Macquarie Group, Deutsche Bank, and Morgans all reiterated their "buy" ratings on Friday.

JP Morgan analyst Siddarth Parameswaren took a more pessimistic view. He has an "underperform" rating on the stock.

Mr Parameswaren accepts the forecasts for increased sales, but is worried about the extra risk this will require the company to take on in its investment portfolio that backs those contracts.

Record low interest rates and sluggish economic growth, when share and property market prices have already been inflated by seven years of extraordinary monetary stimulus, means it is a challenging time for investors.

Mr Parameswaren believes Challenger is understating how difficult it will be to find enough quality assets to deploy the increased annuities revenue in.