

Gulf Actuarial Society

Investment Strategies in the GCC

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- 1. Setting the scene**
- 2. Investment strategies in MENA**
- 3. Impact on profitability**
- 4. Conclusion**

- 1. Setting the scene**
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Today's presentation



OBJECTIVE

- Focus on insurers based in MENA markets (including Turkey)
- Identify different investment strategies employed
- Evaluate their impact on insurers' profitability

MAIN DATA SOURCE: AM BEST STATEMENT FILE GLOBAL

All data is from the analysis of the financial statements of +220 companies over a period of 10 years (2004-2014) unless otherwise stated

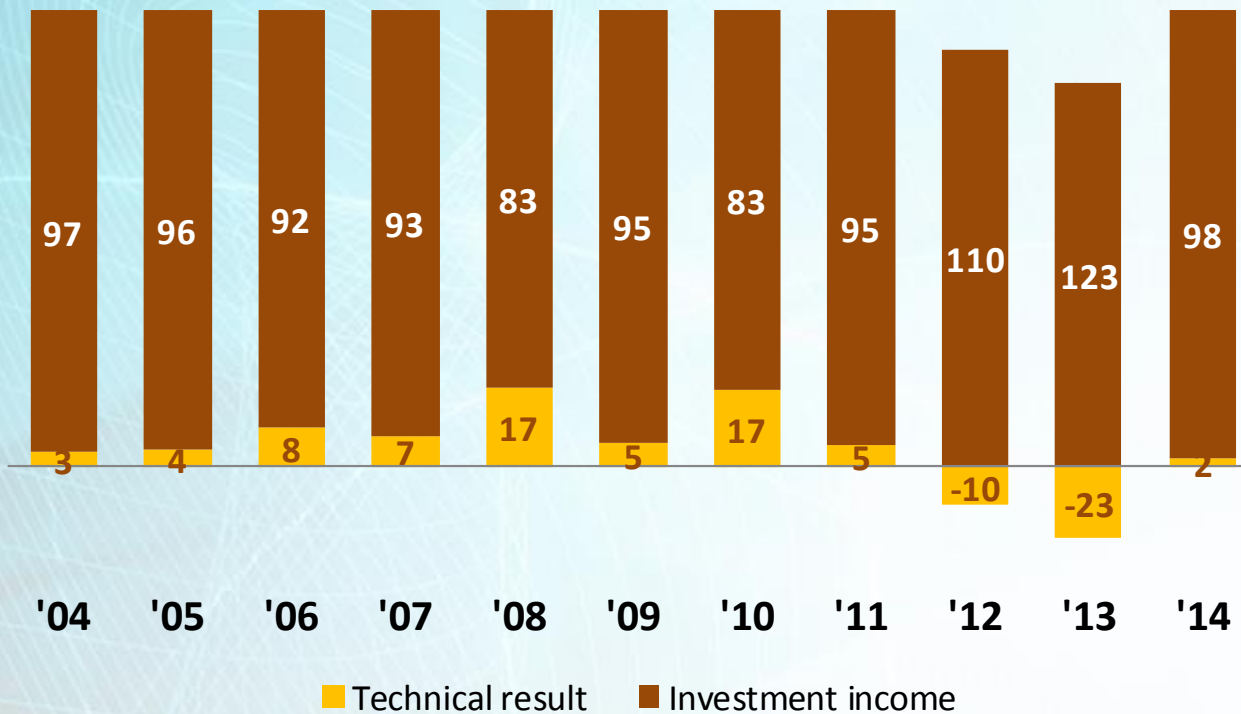
NAMING CONVENTION

- Investment strategies with more than 35% of invested assets into one asset class are considered “focused” on this class e.g. 35% of assets are cash then the strategy is “cash” focused strategy
- Strategies with two asset classes over 35% each are called “dual”
- Strategies with no class over 35% is considered “balanced”

Importance of investment returns in insurers' profitability



COMPONENTS OF INSURER PROFITABILITY IN MENA (%)

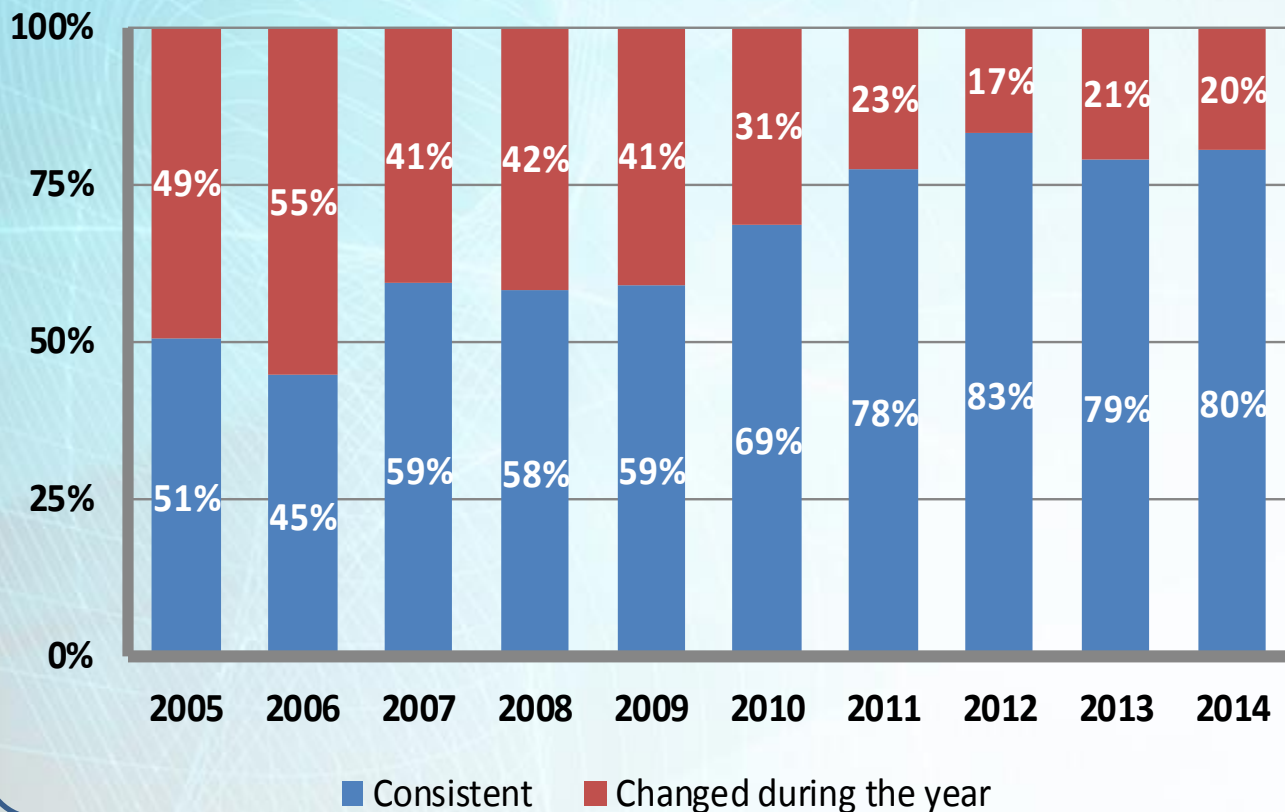


- Investment returns are the most important component of profitability of MENA insurers
- Together with reinsurance commissions they are the two most important profit contributors
- Significant variations in investment strategies between markets and companies

Increasing consistency in investment strategy



CHANGE IN INVESTMENT STRATEGY



- Historically a large proportion of insurers have been changing their investment strategies
- Post economic crisis companies have tended to retain their investment strategy year-on-year
- Major drivers for the increased consistency have been:
 - a. the prevailing market prices and
 - b. regulatory pressures

Agenda

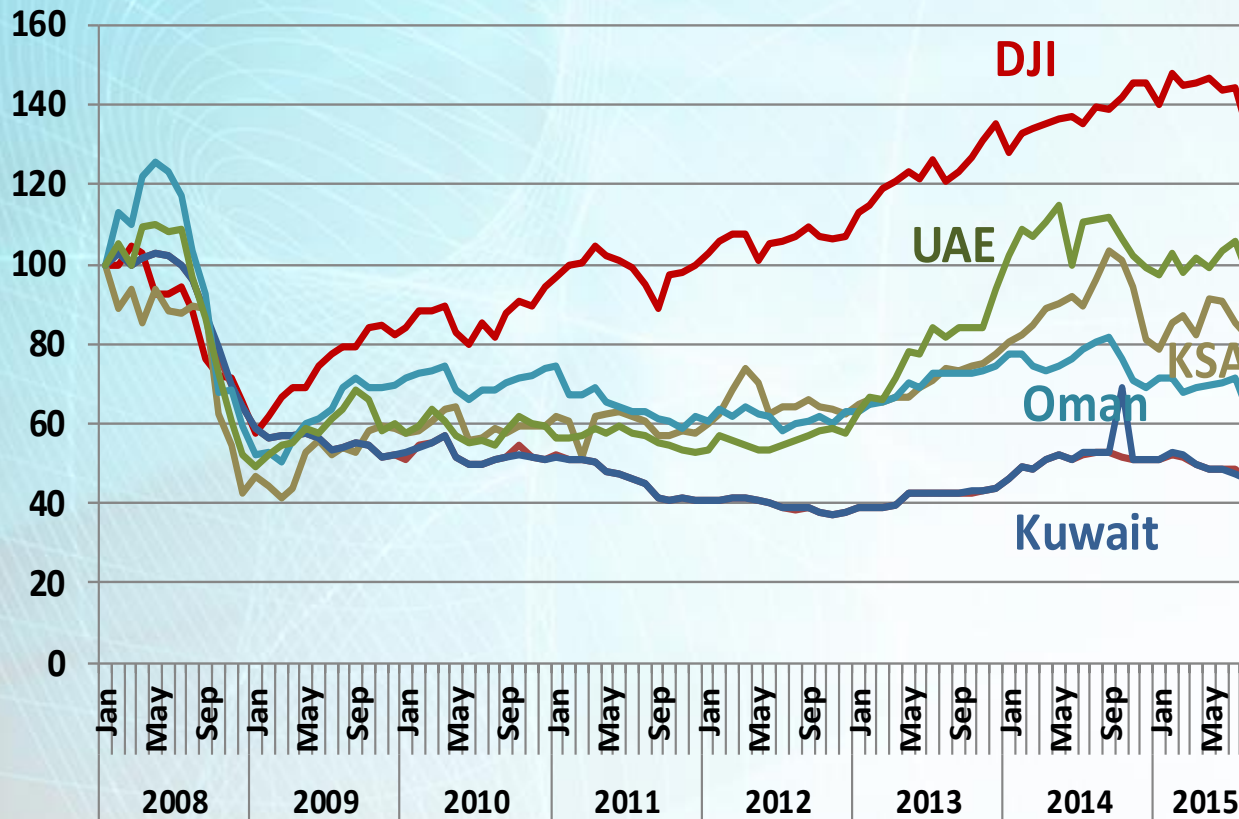


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Equity markets fail to deliver ...



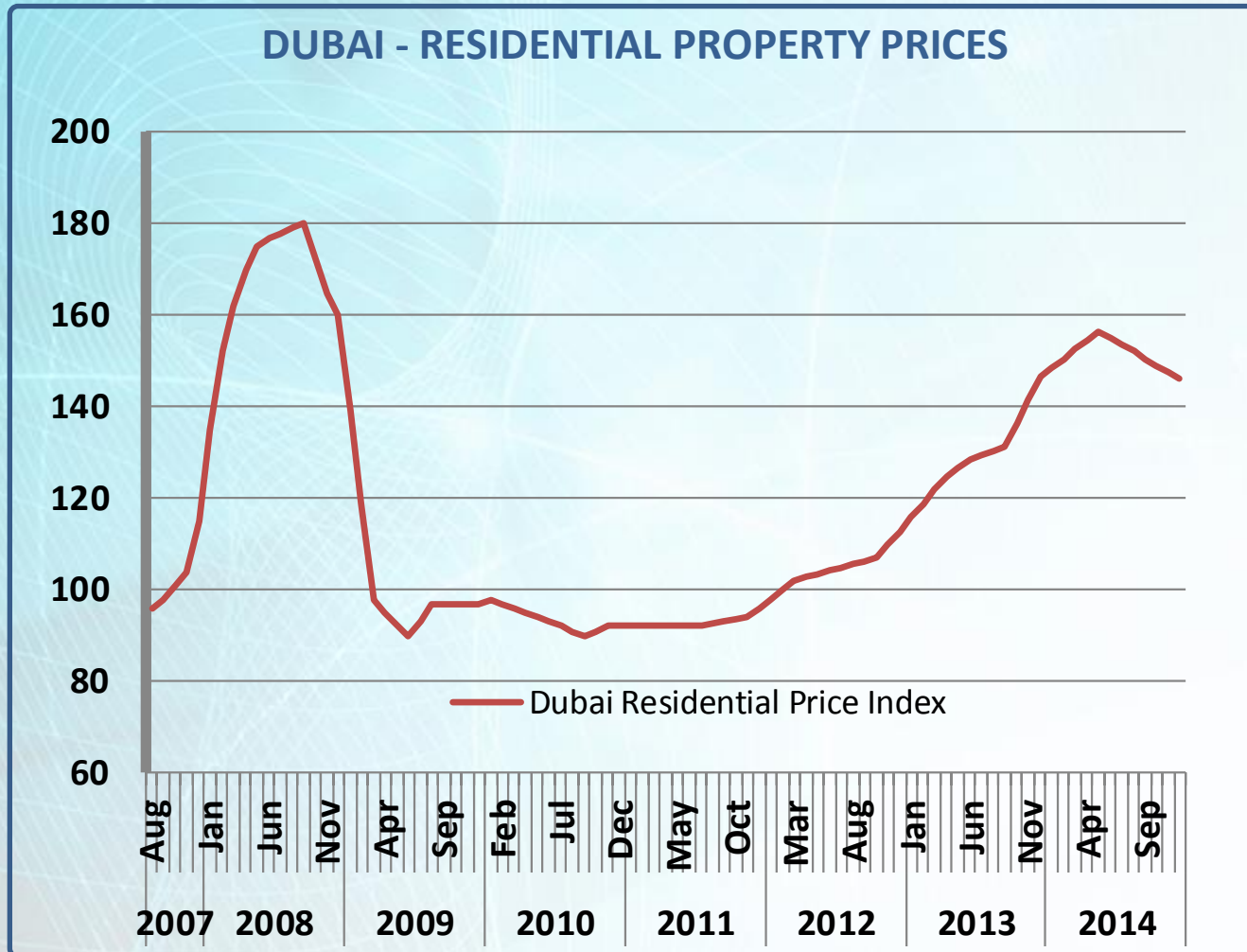
DEVELOPMENT OF EQUITY INDICES



Source: Local bourses

- Equity markets in the region have been underperforming when compared to international indices (Dow Jones Industrial)
- UAE (Abu Dhabi) and KSA bourses have performed better over the last 3 years
- Non-oil economies have fared even worse (with the exception of Turkey)
- Bourses of oil based economies likely to continue their declines

...and real estate markets have followed suit



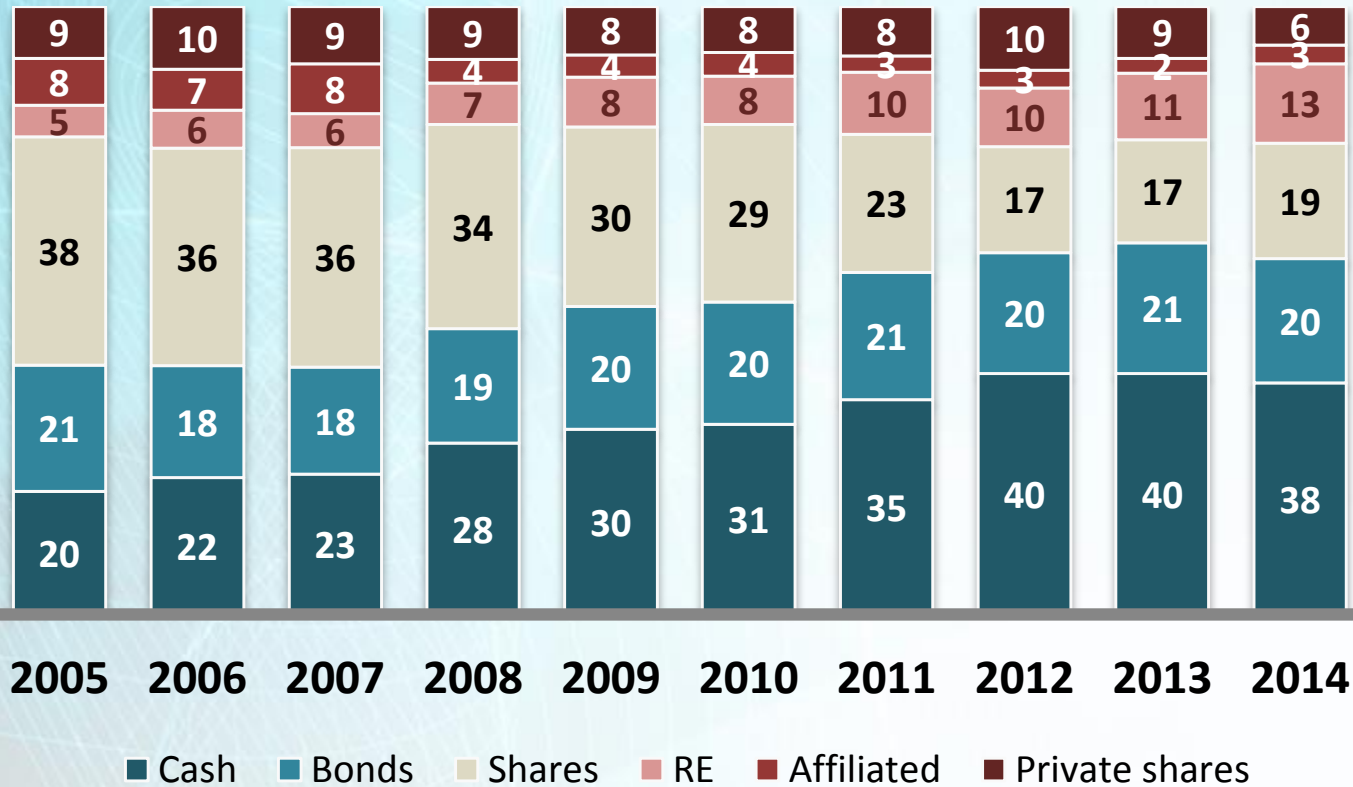
Source: Knight Frank Market Insight

- Real estate prices declined significantly during recent economic crisis
- Prices remained depressed for 3 years
- Recent market upturn did not reach historical highs nor is it likely to continue

Increasing emphasis of investment strategies on cash



INSURERS' INVESTMENT STRATEGIES BY MAIN ASSET CLASS

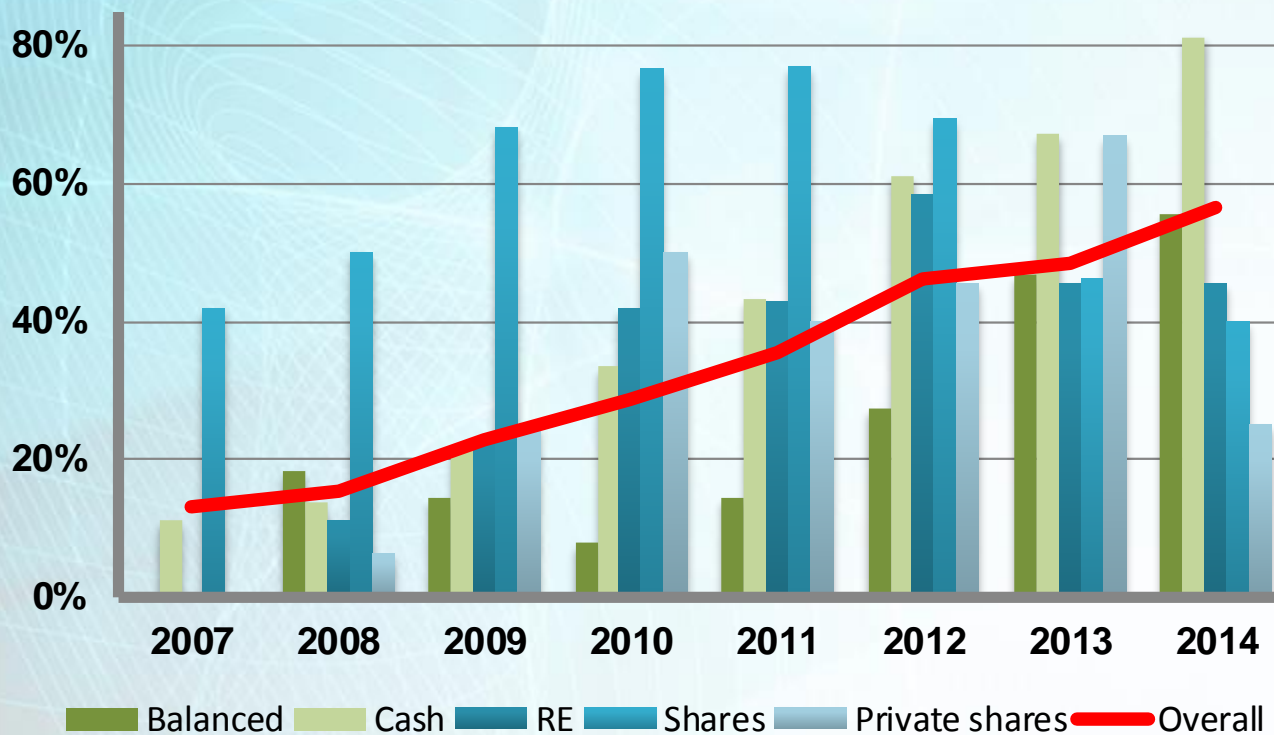


- Most companies have strategies focusing on one asset class
- Historically companies have been focusing on:
 - cash
 - shares and
 - real estate
- Most dual strategies are focused on real estate and shares
- Equity and real estate focused strategies declined during latest economic crisis

Reducing appeal of more aggressive investment strategies



COMPANIES WITH CONSISTENT INVESTMENT STRATEGY OVER 3 YEAR PERIOD

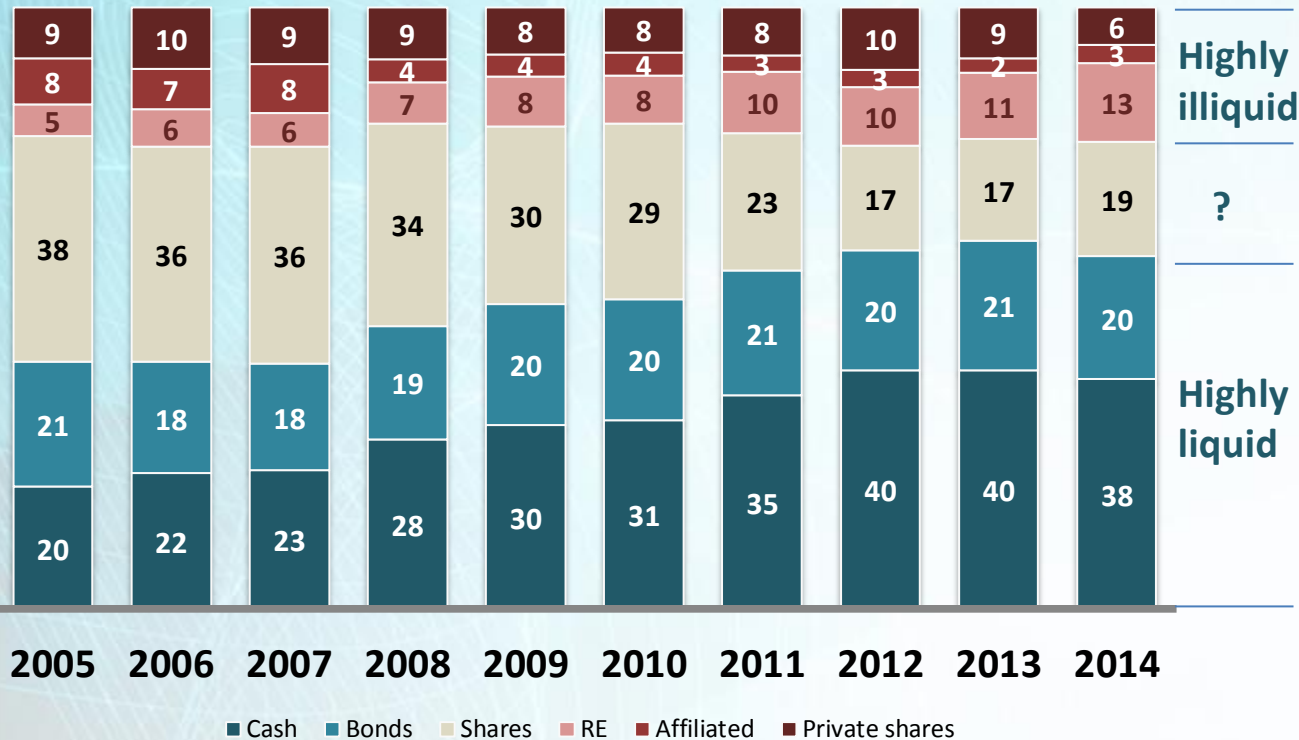


- More than 50% of MENA insurers are retaining the same investment strategy over 3-year period
- Most consistent strategies are those focused on cash and the “balanced” strategy
- Cash strategy can be a holding position for many companies
- Peak of share-focused strategy in 2013 is, in many cases driven by asset appreciation

Investment liquidity improved over the last 10 years



ASSET ALLOCATION OF MENA INSURERS



- Highly liquid assets accounting for approximately 60% of invested portfolio
- Highly illiquid assets have remained stable at around 20%

Points to note:

- In most cases publicly listed shares have limited liquidity due to the poor breadth of the local bourses
- Real estate can be more/less liquid depending on if it is valued at historical or market values

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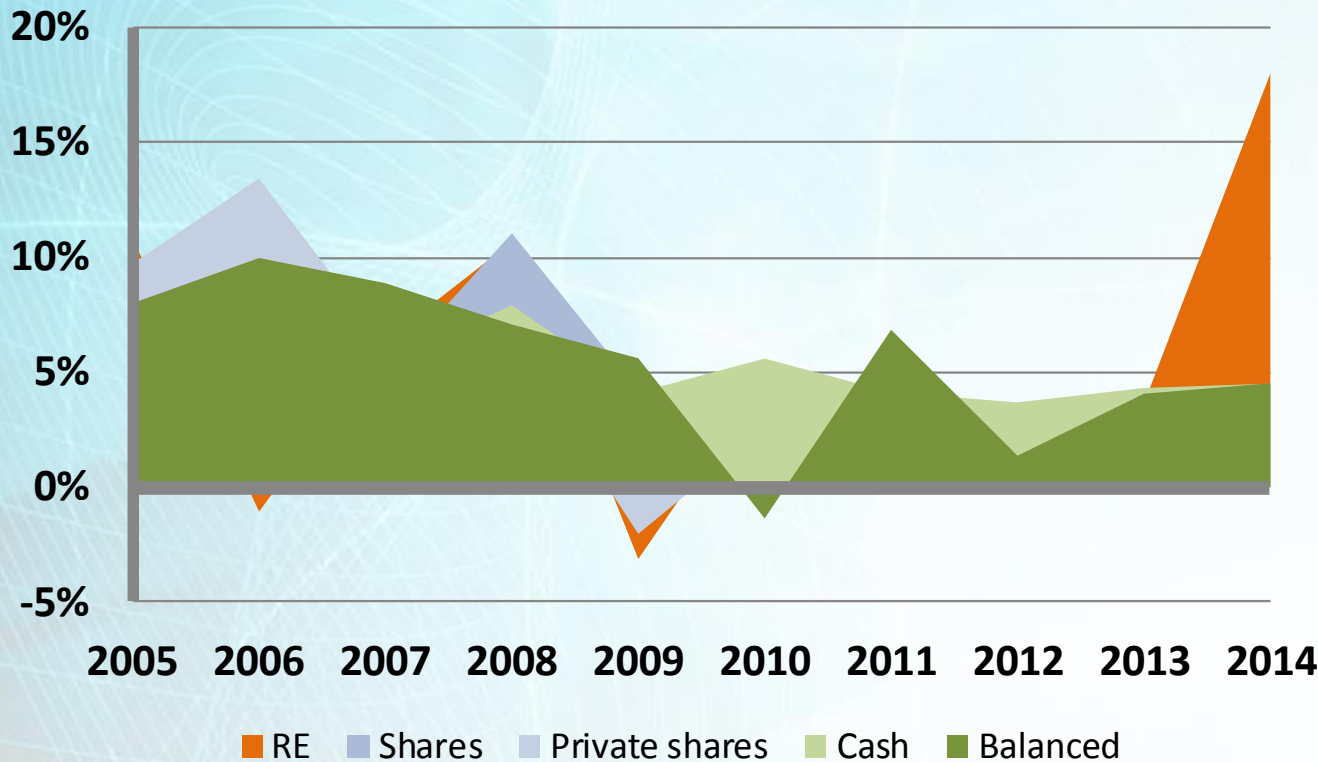


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Yield of different investment strategies – all markets



INVESTMENT YIELD OF DIFFERENT INVESTMENT STRATEGIES

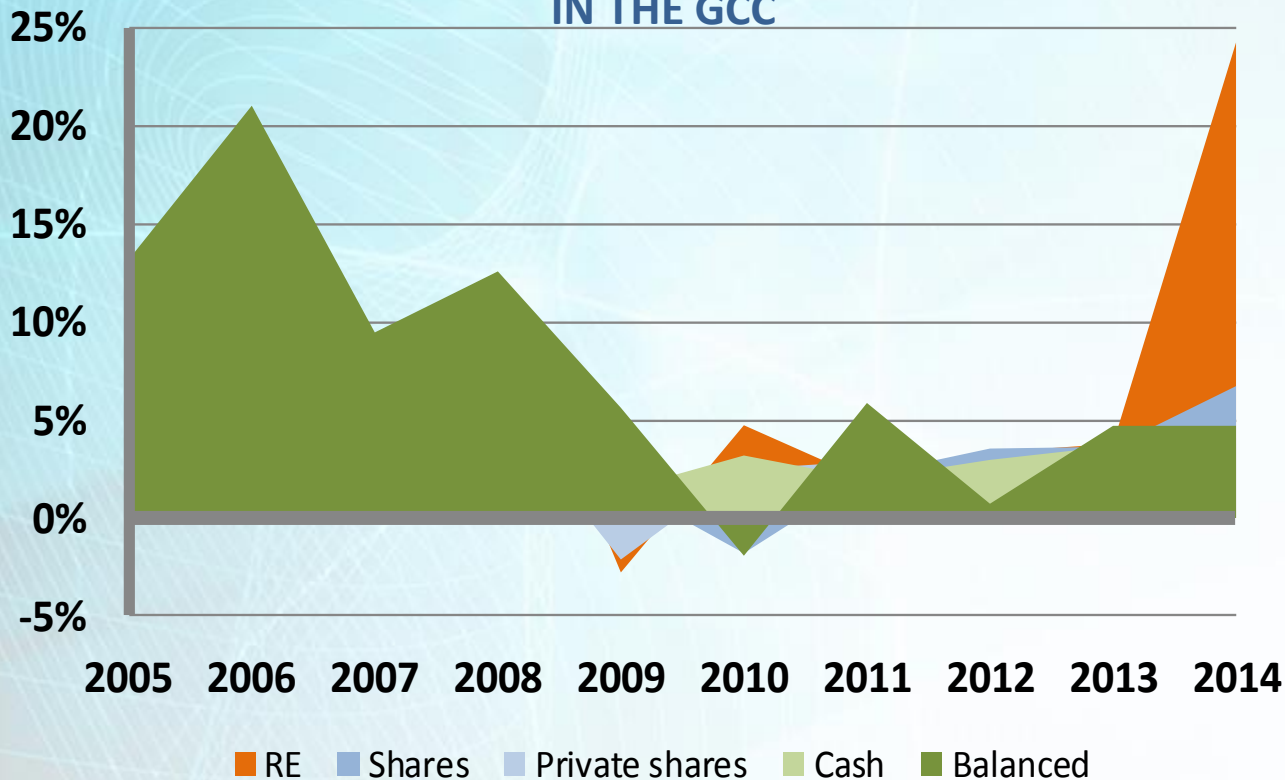


- Real-estate focused strategies provide volatile results. They performed best in pre-crisis years
- Cash-focused strategies performed well after the crisis
- Balanced strategies have provided the best risk-reward
- Share-focused strategies outperformed the market in 2008

Yield of different investment strategies – GCC



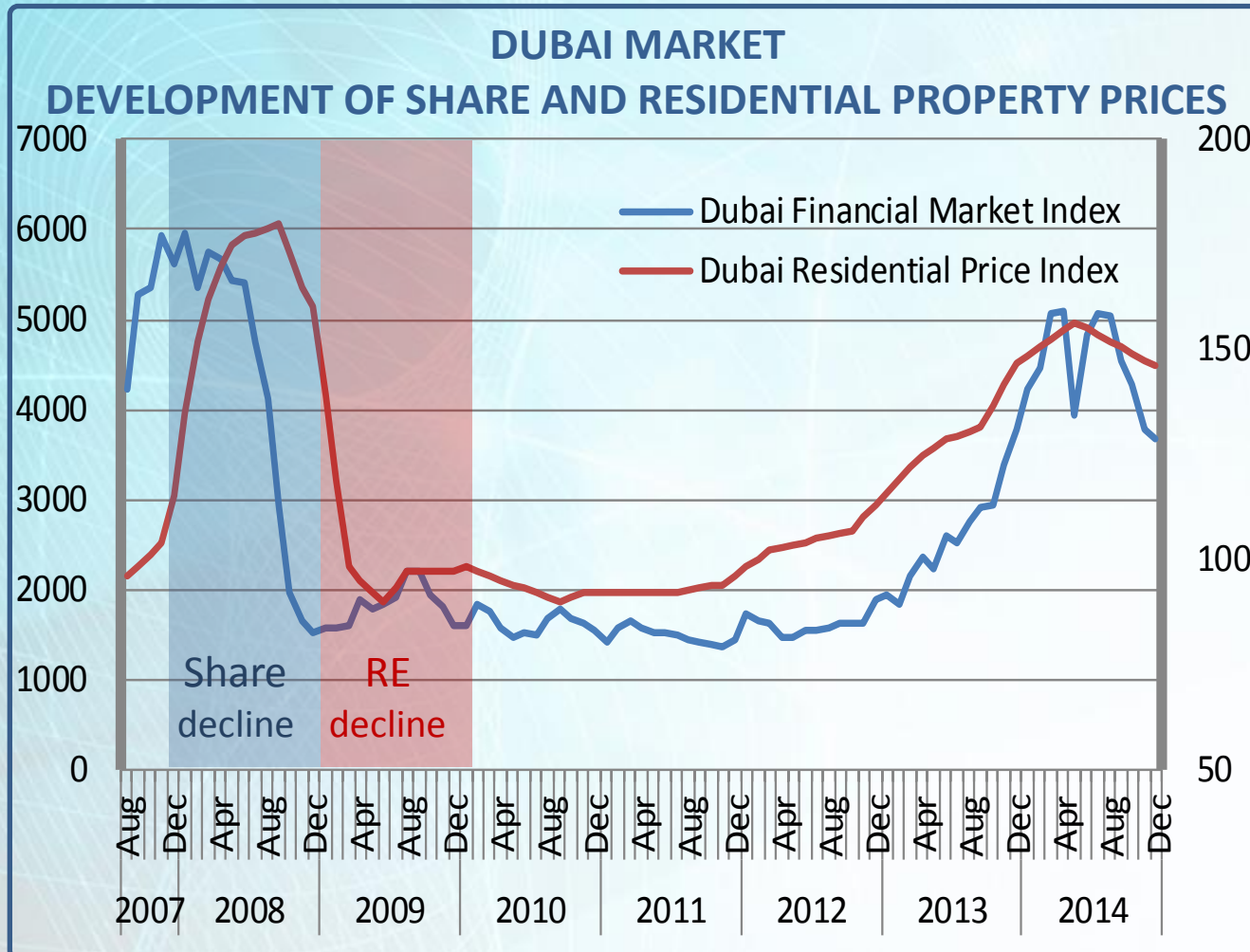
INVESTMENT YIELD OF DIFFERENT INVESTMENT STRATEGIES IN THE GCC



- Picture more accentuated in the GCC economies
- Balanced strategies have consistently outperformed other strategies up until 2010
- Real estate strategies the top performers in the last four years
- Disparity since 2010 is mainly due to capital gains

Need to focus on impairment policies of different companies

Development of real estate and equity markets – Dubai example

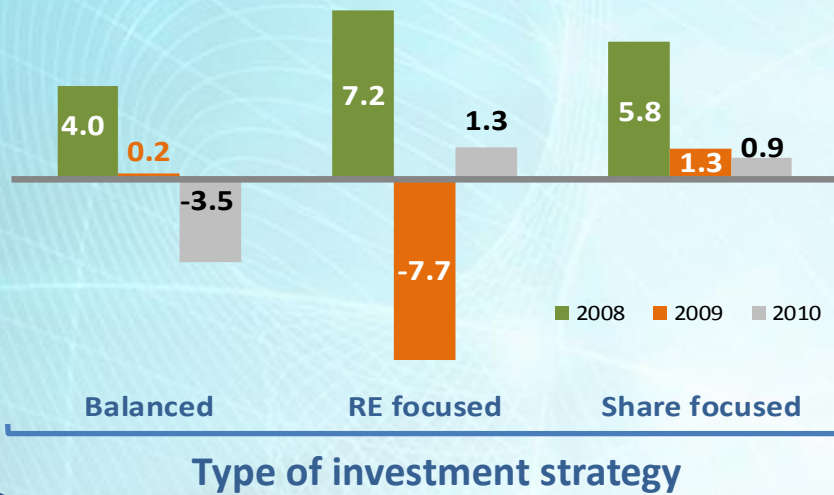


- Significant correlation between share and real estate pricing in many markets
- Shares peaked in 2007 and RE in 2008
- Majority of price declines should have impacted financial statements of:
 - a. 2008 for shares
 - b. 2009 for real estate

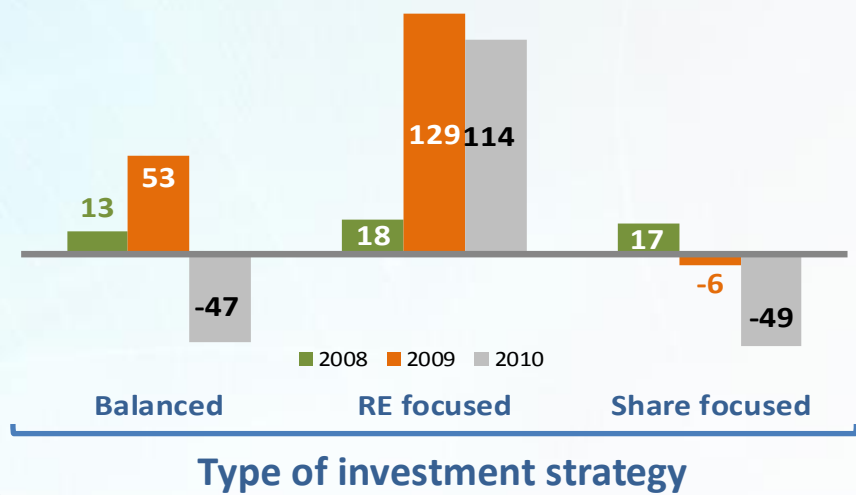
Source: Dubai Financial Market and Knight Frank Market Insight

Impact of price decline on companies' financial statements

P&L: GAINS AS % OF INVESTED ASSETS



BALANCE SHEET: % CHANGE IN RE VALUE



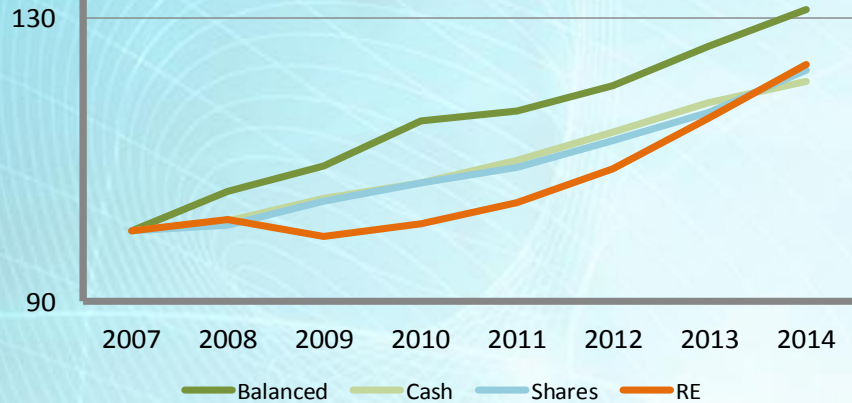
- Indications of significant trading in real estate both in 2008 and in 2009
- Sales of RE in 2008 makes sense in terms of profit-taking
- Reasoning of RE sales in 2009 is not obvious

- Many real estate assets kept on balance-sheet on historical values
- Significant revaluation of real estate during 2008 from historical to market values
- Despite decline in 2008 real estate values this had a positive effect on companies' balance sheets

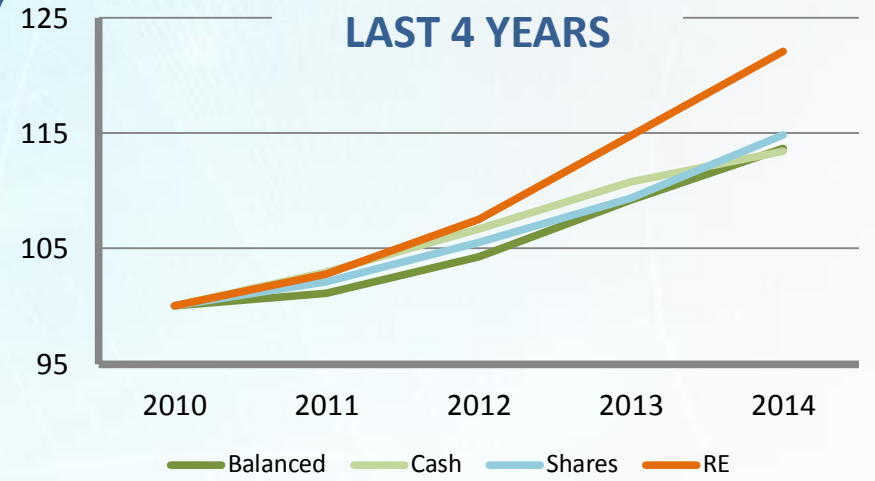
Index performance of investment strategies in GCC: is your risk being rewarded?



SINCE LAST ECONOMIC CRISIS



LAST 4 YEARS

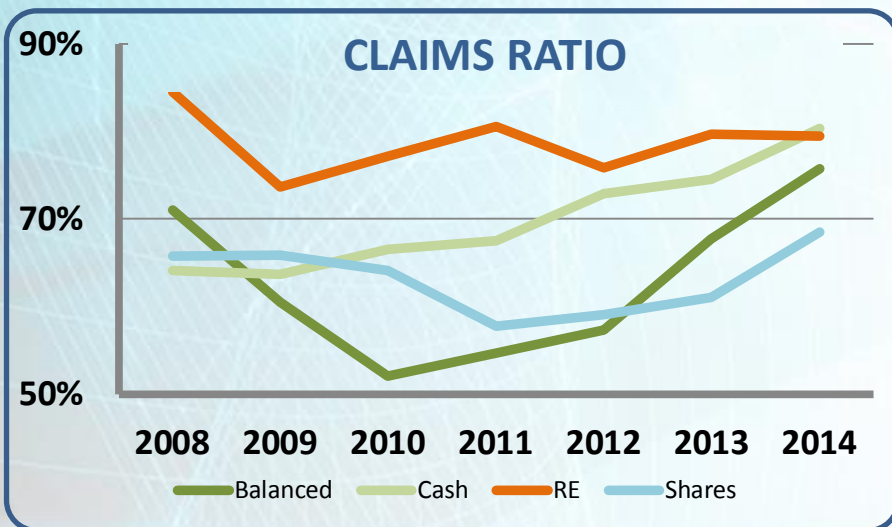
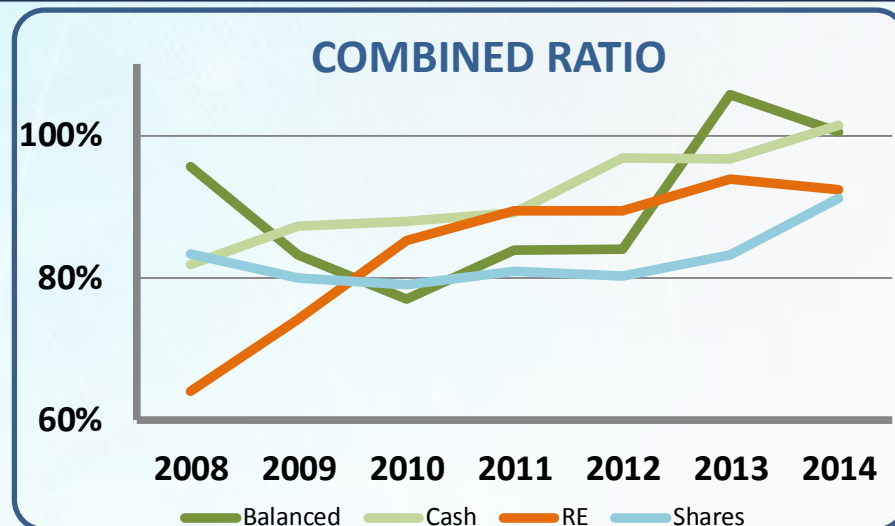
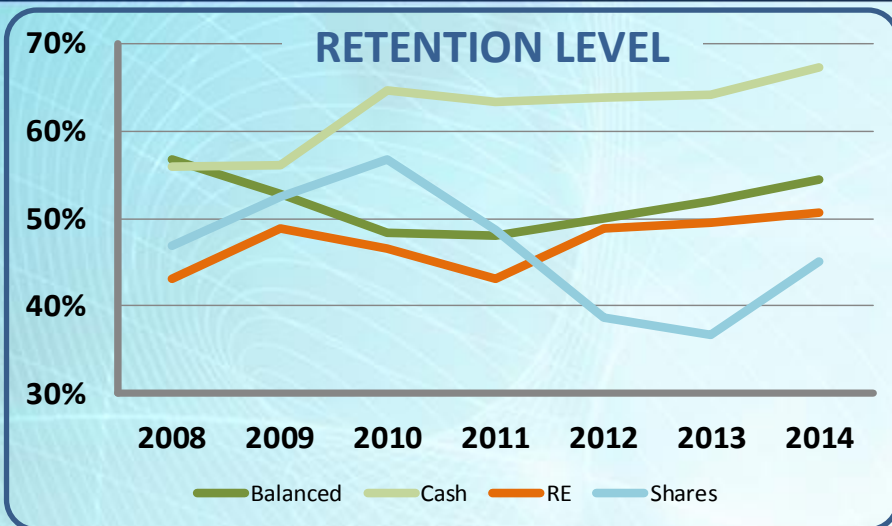


LAST 10 YEARS



- Balanced strategies have provided the best results over most of the time-frames examined
- Real estate strategies have outperformed the rest during the last 4 years
- Cash based investment strategies have consistently outperformed those focused on shares

Link between investment strategy and underwriting profitability



Companies with more aggressive investment strategies (i.e. those with high concentration on shares and real estate) have:

1. Higher claims ratio
2. Low retention levels which result in
3. Higher reinsurance commissions

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Mainly good news



1. Insurers' investment strategies have been typically focused on riskier asset classes i.e. shares and real estate
2. Investment yields have failed to reflect the increased risk assumed
3. Post economic crisis there has been a move to more conservative strategies
4. Companies have adjusted their reporting practices as a result of the decline in real estate prices of 2009
5. Apparent de-risking of investment portfolios is still de-linked from risk appetite and ERM

Q&A

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