Can non life firms generate better investment returns?

Sam Tufts and Ryan Allison

EY
What are the key themes emerging from the macro-economic environment?

What are the challenges facing insurers’ investment portfolios?

How do insurers typically manage their investments?

How have GI firms performed with different investment strategies?

What questions should we ask ourselves to achieve a good return for the appropriate risk in 2018 and beyond?
What are the key themes emerging from the macro-economic environment?
Despite apparent global growth…

GDP % annual change

Source: EY analysis, Oxford Economics
…investors face an uncertain world with high geographical correlation due to globalisation

**US**
- Growth or slowdown?
- Policy shifts on taxes & spending
- Potential trade wars

**Europe**
- Rise of populism
- Negative yields, mixed growth
- Future of EU

**Asia**
- China slowdown?
- Korean spotlight
- Japan’s demographics

What other themes have you observed in financial markets in past 6 – 12 months?

What investment risks do you see as a threat to the insurance industry?
...investors face an uncertain world with high geographical correlation due to globalisation

**Global themes in an increasingly globalised world**

- Central bank policy driving markets
- Inflation (/deflation) concerns
- Search for yield – illiquid & alternative assets
- Asset class valuations – ‘It’s all expensive’
- Signs of deteriorating liquidity conditions
- Increased political uncertainty – protectionism & populism
- Wage divergence & gig economy
- Demographics - genomics & millennials
- Climate change, clean energy, ESG
- Increasing regulation
- Tech, big data, social media, AI & robotics – better for all of us?
What are the challenges facing insurers’ investment portfolios?
There are various internal pressures on investment approach

Risk Takers
CEOs, CFOs, CIOs?

Risk Reducers
CROs, CCOs?

“Are we an insurer or an investor?”

“Is trying to achieve a positive investment return like last year possible?”

“Are we taking unintended risks?”
Spreads are below long term averages

Source: Markit
While there are no ‘free lunches’ or ‘low hanging fruit’

Non-life investment returns: 1986 to 2017

Source: S&P
How do insurers typically manage their investments?
Insurers can adopt a range of different investment strategy approaches

**Conservative**
Targets <1% and holds traditionally “Core” assets like cash & short duration fixed income to closely match liabilities.

“We’re looking to minimise capital, not lose money and target a conservative return”

**Mixed**
Targets <2%. Holds “Core” and some “Non Core” assets like diversifying credit, property, absolute return or other alternative strategies.

“We want to make some extra returns for some extra risk”

**Innovative**
Holds a mix of diversified strategies with an aim to generate risk-adjusted returns in line with business objectives and can react quickly to markets.

“We have an investment strategy and holistically think about risk and return and accept a higher capital charge”

No ‘one size fits all’ or ‘correct’ approach
How have non-life firms performed with different investment strategies?
Case study: Beazley

Stuart Simpson, CIO in 2016: “In investment management, conservatism does not mean being slow off the mark and decisiveness need not be rash. Sometimes you need to act quickly and decisively in pursuit of a conservative strategy, to extract additional value or to protect returns” [Source: 2017 Beazley Annual Report]
Case study: Argenta

“During 2017 Insight Investment Management (Global) Limited (“Insight”) has been responsible for investing the vast majority of the syndicate’s assets within a fixed income portfolio. The syndicate’s Canadian dollar assets in the regulated trust funds are managed by Lloyd’s treasury within a fixed income portfolio. The returns achieved on these portfolios are measured with reference to appropriate benchmarks.”

“In addition to the fixed income portfolios Insight also managed a separate portfolio of multi asset absolute return fund within a UCITS structure. Initially this represented approximately 18% of the syndicates assets although it was reduced closer to 14% by the year end. The objective of this asset class is to optimise investment returns consistent with capital preservation and liquidity, within regulatory constraints, whilst using assets that give diversification from the fixed income portfolio.”

Source: 2017 Argenta Annual Report
...and non-life investment income is becoming increasingly important

Lloyds’ specialty aggregate syndicates profits split by investment income & other sources

Source: 2017 Lloyds Syndicate Data

<table>
<thead>
<tr>
<th>Year</th>
<th>Profit</th>
<th>Other Income</th>
<th>Investment Income</th>
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<tr>
<td>2012</td>
<td>2,371,872</td>
<td>1,100,000</td>
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<tr>
<td>2013</td>
<td>2,610,250</td>
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<td>2014</td>
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<td>2015</td>
<td>1,937,913</td>
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<tr>
<td>2016</td>
<td>1,350,572</td>
<td>1,500,000</td>
<td>200,000</td>
</tr>
<tr>
<td>2017</td>
<td>(1,856,660)</td>
<td>2,000,000</td>
<td>(200,000)</td>
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</table>
Varying asset allocation leads to varying investment return outcomes

Source: S&P
What questions should we ask ourselves to achieve a good return for the appropriate risk in 2018 and beyond?
What questions should we ask ourselves to achieve good returns for the appropriate risk in 2018 and beyond?

1. Investment strategy
   Are we targeting the right objectives?

2. Investment risk
   Is our investment risk appetite appropriate?

3. Investment visualisation
   Can we create MI to better understand our investments?
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Contact

Simy Prakash, GI Investment Advisory Lead
Simy.Prakash@uk.ey.com
Office: +44 207 951 7901
Mobile: +44 7764 757 237
Ernst & Young LLP
25 Churchill Place,
London E14 5EY

Sam Tufts, EY Investment Advisory
STufts@uk.ey.com
Office: +44 207 951 6671
Mobile: +44 7468 357 674
Ernst & Young LLP
25 Churchill Place,
London E14 5EY

Ryan Allison, EY Investment Advisory
RAllison2@uk.ey.com
Office: +44 (0) 20 7951 4479
Mobile: +44 (0) 73 9210 6193
Ernst & Young LLP
25 Churchill Place,
London E14 5EY

Thank you