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# CFO Network

Charles Pears  
22 February 2013

► A BNY MELLON COMPANY<sup>SM</sup>



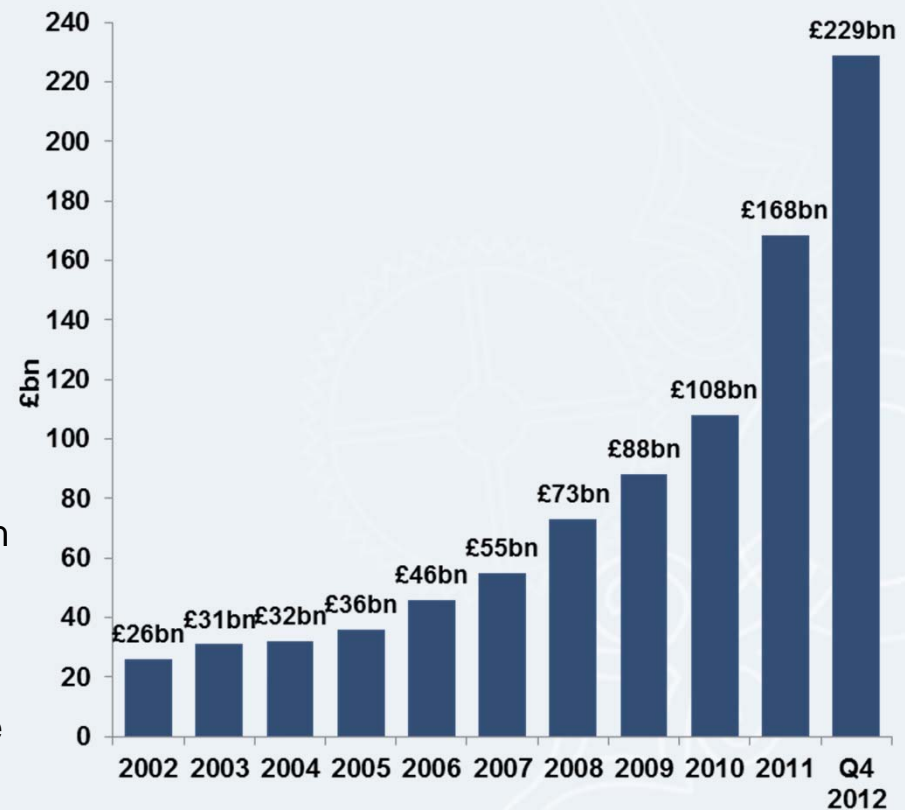
# Insight Investment

## Our credentials



- Autonomous asset manager owned by BNY Mellon
- Locations in London, New York, Sydney and Tokyo
- Reputation for excellence in:
  - liability risk management
  - active fixed income
  - currency risk management
  - multi-asset and absolute return
- Highly-rated capability:
  - one of the world’s most experienced currency specialists
  - ranked number one for LDI with UK consultants in the Greenwich Associates Survey for 3rd consecutive year
  - Financial News LDI manager of the year 2010, 2011 and 2012 and Fixed Income Manager of the Year 2012

**Insight Investment assets under management<sup>1</sup>**



The assets under management figure represents the combined assets under management of Insight Investment Management (Global) Limited and Pareto Investment Management Limited, which became part of the Insight group on 1 January 2013. Data as at 31 December 2012. Assets under management are represented by the value of cash securities and other economic exposure managed for clients.

<sup>1</sup> Excludes previous parent introduced assets prior to 2009.

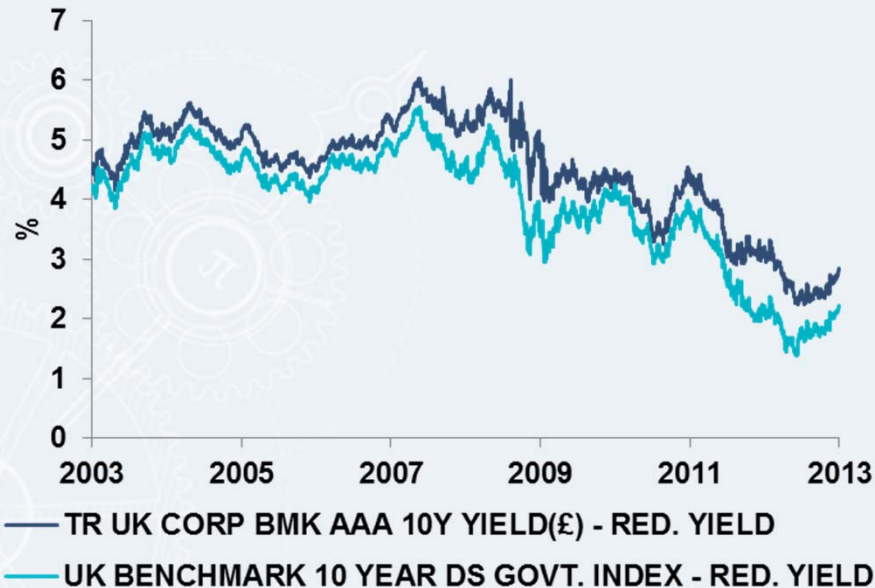
# The environment is challenging for all insurers ~ investments



## Trend

- Low yields on government bonds and high quality credit as the traditional safe haven for insurers

## Evidence



Source: Thomson Reuters Datastream.

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## Response

- Insurers are extending core fixed income mandates while seeking to maintain credit quality
  - Non-sterling issuance (hedged back to sterling)
  - ABS
  - Emerging Market Corporates
  - Short-dated High-Yield
  - Interest rate swaps used to achieve duration management (so allowing credit positions to be taken independently of duration management)

## Implication

- Increased use of specialist fixed income managers able to assess and incorporate these opportunities

# The environment is challenging for all insurers ~ investments



## Trend

- Highly uncertain economic environment with a number of wildly divergent outcomes as credible scenarios

## Evidence

- Unconventional monetary policy becomes the norm
- Lower average growth
- Shorter business cycles
- The patient moves from an acute to chronic phase in rehabilitation
  - The ECB gets serious
  - A softening attitude towards austerity
  - Political will to be tested in the periphery
- A world where monetary policy has still been working
  - Negative global real rates pose a challenge
  - Different responses suggest divergent performances

## Response

- Insurers are not able to make strategic and long-term allocations to asset classes like equities
- Increased use of Diversified Growth Funds
  - Broad opportunity set
  - Exposures managed dynamically
  - Focus on liquidity to enable positions to be quickly changed
- Increased use of UCITS Absolute Return Funds
  - Implicit downside protection

## Implication

- Investment strategies adopted demand different skills from investment managers
- Reporting and data provision to secure capital benefits of low volatility strategies

# The environment is challenging for all insurers ~ investments



## Trend

- Banks deleveraging creating “once in a cycle” opportunities for those able to take advantage

## Evidence

Description	Yield	Rating	Expected default	Recovery	Expected loss	Loss adj. Yield
Real Estate Loan	4.50%	AAA*	0.01%	90%	0.00%	4.50%
RMBS	1.25%	AAA	0.01%	90%	0.00%	1.25%
Covered Bond	0.75%	AAA	0.01%	60%	0.00%	0.75%
Real Estate Loan	8.00%	A*	0.12%	90%	0.04%	7.96%
Financial	2.00%	A	0.12%	25%	0.09%	1.91%

Source: Barclays and Credit Suisse 21 November 2012.

## Response

- Insurers with long-dated liabilities and/or surplus capital are looking to provide loans to infrastructure and commercial real-estate companies
- Attractive returns can be secured by those willing and able to assess and negotiate these opportunities

## Implication

- Investment strategies adopted demand different skills from investment managers
- Reporting and data provision to secure capital benefits of high quality but unrated loans requires transparent and insurance specialist investment managers

# The environment is challenging for all insurers ~ regulatory



## Trend

- Regulatory minefield with highly technical changes such as central clearing for derivatives and Solvency II creating an additional layer of complexity to conventional risk/return decision-making

## Evidence



## Response

- Insurers require the skills and resources to assess and respond to these initiatives (both for existing positions and when formulating future investment strategies)
- Solvency II creates an ongoing cost to the industry with limited short-term benefit to participants
- Increased use of liability driven investment approach to manage VaR

## Implication

- Cost and resource stretch acutely felt by smaller insurers
- Emergence of a cohort of insurance specialist investment managers with these capabilities in house (so creating scalability in delivery)

# The environment is challenging for all insurers ~ regulatory



## Trend

- FSA looking for mutuals and with profits firms in run off to have credible plans to manage the repatriation of value to policyholders

## Evidence



## Response

- Insurers in long-term run off need to define a long-term plan to address:
  - Sustainability as fixed costs rise as a proportion of a declining revenue stream
  - Management of illiquid exposures
  - Incorporation of liability matching approach for some or all guaranteed benefits / targeted risk reduction
  - Next round of consolidation

## Implication

- Use of pooled funds and/or external investment managers
- M&A challenging insurers to seek help dealing with the very different challenges this presents

# The environment is challenging for all insurers ~ consumers



## Trend

- Increased commoditisation of the value proposition and relationship with consumers

## Evidence



## Response

- Insurers focusing less on administration and more on where they really add value
  - Annuity firms and longevity risk management
  - Segment specialists looking to develop product benefits relevant for their customers
- Insurers recognising that in many cases investment management gives rise to non-core risks for their business

## Implication

- Business models being revisited with a focus on outsourcing non-core activities



# The environment is challenging for all insurers ~ consumers



## Trend

- Customers becoming both more activist and litigious in part inspired by claims management firms looking to capitalise on a poorly protected insurance industry

## Evidence

Quote:

“Aviva said premiums had risen by 80pc since October 2008 due to an increase in personal injury claims, especially whiplash.

The insurer found the average current legal fee for a whiplash claim is £2,500, nearly half of which is due to intermediaries including claims management companies and personal injury lawyers.

Aviva estimated that if insurers handled claims directly it would cut £1.5bn from UK motor insurance premiums.”

Source: Aviva quote from the Telegraph online.

## Response

- Internal governance requires strengthening as part of the final line of defence
- Increased use of specialists to provide for functions directly impacting policyholder outcomes/benefits
- Industry bodies having to take a more active role in marshalling the defence at a collective level

## Implication

- Increased visibility and at times aggressive challenge to investment decisions and active participation by members at AGMs

# How are investment managers responding?

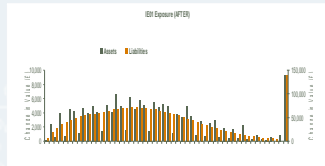
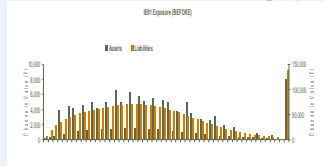


# Insight Investment

## Insurance expertise



### Understanding your liabilities:



- Sophisticated ALM tools for analysing and managing assets and liability risks for clients
- Working with clients to devise solutions to meet their individual needs
- Input from UK Insurance Actuary with 18 years experience supported by solutions team familiar with a wide range of insurance clients

### Bespoke reporting:



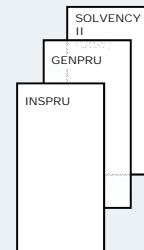
- In conjunction with our custodian, Insight has sophisticated systems to produce regular reports for UK Life, General and Lloyd's syndicates
- Additionally, ad hoc reports can be generated to deliver bespoke reporting outputs and formats for clients
- Already providing Solvency II QRT reports for Lloyd's syndicates

### Generation and filtering of ideas:



- Generation of new investment ideas to improve risk-return trade-off for insurers, in response to changing market conditions
- Filtering of other investment solution ideas to ensure suitability for UK insurers under current regulations and known future developments

### Regulatory support:



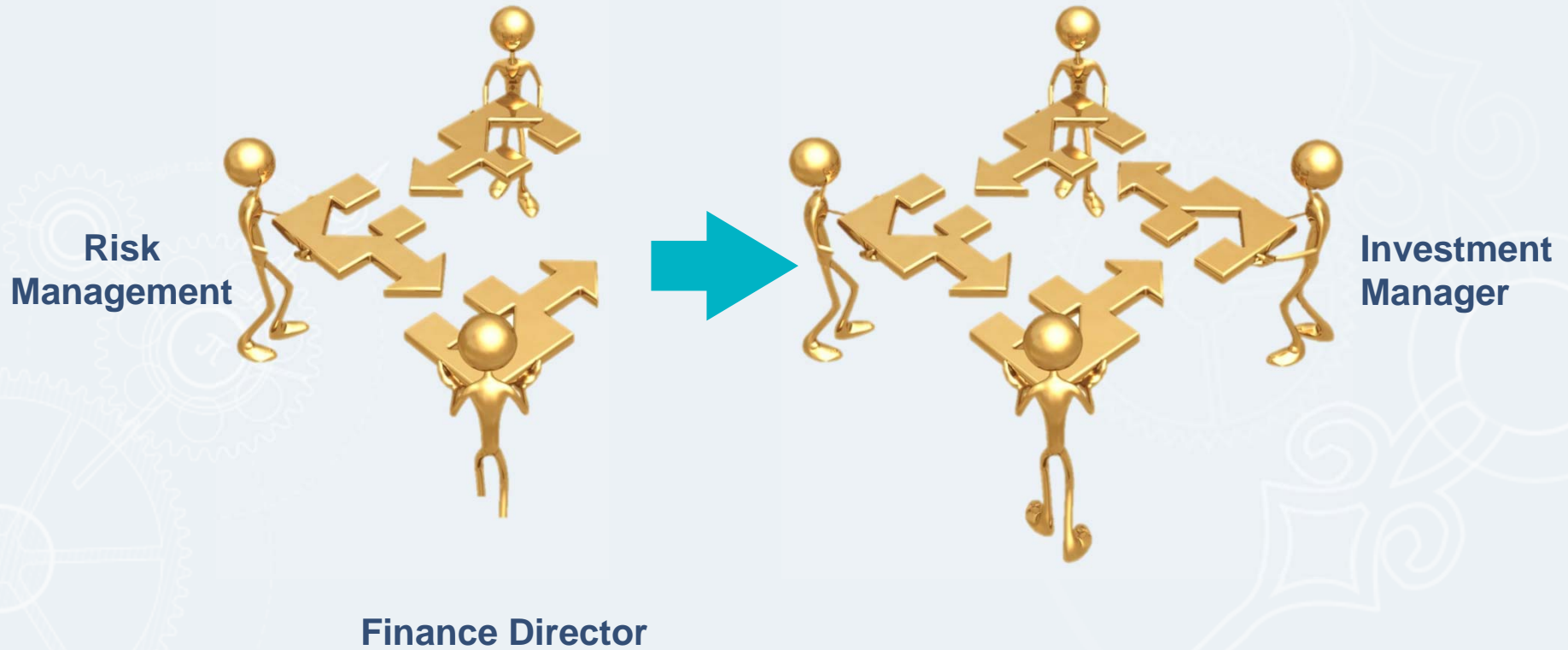
- Insight actively supports Insurance clients to meet the needs of the regulator:
  - Stress testing for Regulatory Capital assessment
  - “What if?” Regulator scenario analysis
  - Analysis for Solvency II

# Why Insight for insurers?

An investment partnership arrangement



**With Profit Actuary**



# Biographies



## **Charles Pears – Head of Business Planning and Insurance Strategy**

**Charles joined Insight in October 2008 as Head of Insurance Product. He joined from Lloyds TSB where he was Head of Bancassurance, Protection and Retail Share Dealing. Prior to this he worked for HBOS Financial Services as Head of Bancassurance. Charles has also led strategy teams at both MLC, the investment management division of National Australia Bank Group and Aviva plc. He began his industry career in October 1995 with Commercial Union (Aviva Group) where he held various roles within their general insurance and corporate partnerships teams. Charles graduated from the University of Durham with a BA honours degree in Philosophy. He is an Associate of The Chartered Insurance Institute.**

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